

A PRELIMINARY REPORT TO THE MINISTRY OF FINANCE

on

THE SPANISH SECURITIES MARKETS - 1973

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June, 1973



SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

DIVISION OF
INVESTMENT MANAGEMENT
REGULATION

June 28, 1973

Excmo. Sr. Antonio Barrera de Irímo
Ministerio de Hacienda
Calle de Alcalá 11
Madrid, Spain

Dear Sr. Barrera:

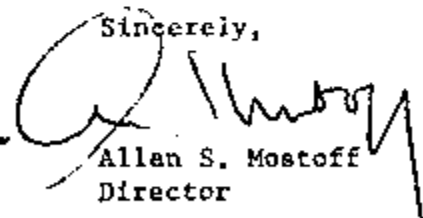
I am pleased to submit our Preliminary Report on the Spanish Securities Markets - 1973. Arrangements for this confidential study were made by the Director General of Financial Policy of the Ministry, under the auspices of the International Finance Corporation through contacts with the Chairman of the Commission and its Office of Executive Director.

The Report has been prepared under my general coordination and that of Lewis J. Mendelson, Assistant Director for Planning and Policy of the Division of Investment Management Regulation. At our request Norman S. Poser, Senior Vice-President of the American Stock Exchange and David V. Green, C.P.A., a member of the international accounting firm of Haskins & Sells agreed to participate in this project.

As a matter of policy, the Commission always disclaims responsibility for the private views of its employees. I must advise you that the Report does not necessarily reflect the views of the Commission nor of any of our colleagues on the staff. Similarly, this report reflects the personal views of Messrs. Green and Poser, rather than those of the organizations with which they are associated.

We are pleased to have had the opportunity to participate in this project. We have enjoyed our association with the Ministry and appreciate the cooperation of those concerned with this study.

Sincerely,



Allan S. Mostoff
Director

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PART I

INTRODUCTION

This is a confidential report to the Ministry of Finance of the Government of Spain. It analyzes the principal problems of the Spanish securities markets today and outlines a general program and alternatives for correcting those problems and strengthening the markets. Long term goals and intermediate targets for achieving them are spelled out along with specific recommendations for dealing with some of the most urgent aspects of these problems. However, it should be emphasized that because it is based on only seven days of interviews, this is merely a preliminary report. A more definitive final report is contemplated after further study and consideration of the recommendations contained herein.

A. Background

Arrangements for this study were initiated in June 1972 by the Director General of Financial Policy of the Ministry of Finance, Jose Vilarasau, through contacts with the Chairman of the U. S. Securities and Exchange Commission ("SEC") and the SEC's Office of Executive Director under the auspices of the International Finance Corporation.^{1/} In September, 1972, Sr. Vilarasau

^{1/} Two senior staff officials of the SEC's Division of Investment Management Regulation, Allan S. Mostoff, Director and Lewis J. Mendelson, Assistant Director for Planning and Policy, participated in this project on an individual basis and the report has been prepared under their general coordination. Norman S. Poser, Esq., Senior Vice President of the American Stock Exchange and David Green, C.P.A., a member of the international accounting firm of Haskins & Sells also agreed, at the request of Messrs. Mostoff and Mendelson, to participate in this project on an individual basis. Both Mr. Poser and Mr. Green have extensive experience in the operation of the securities markets and in securities regulation in the United States. As a matter of policy in all such matters, the SEC disclaims responsibility for the private views of its employees. They do not necessarily reflect the views of the SEC nor of their colleagues on the SEC staff. Similarly, this report reflects the personal views of Messrs. Poser and Green rather than those of the organizations with which they are associated.

discussed the nature and scope of the proposed report with Messrs. Mostoff and Mendelson, and on October 19, 1972 mailed to them a tentative written summary of the main problems in the Spanish securities markets.^{2/}

Early in November 1972 a Spanish delegation^{3/} visited the United States to gain greater understanding of the operation of the U. S. securities markets and system of regulation and to discuss problems in the Spanish securities markets. They met with Messrs. Mostoff, Mendelson and Poser and with various officials of the SEC, the National Association of Securities Dealers, the American Stock Exchange and the New York Stock Exchange as well as with private brokers.

2/ A copy of that memorandum is attached as Appendix A to this Report.

3/ The delegation consisted of

1. Sr. Antonio Rua - Subdirector General Internal Financing,
Capital Markets, Division of Financial Policy,
Ministry of Finance
2. Sr. Raimundo Poveda - Chief of the Research Department, Division
of Financial Policy, Ministry of Finance
3. Sr. Javier Garcon - President, Barcelona Stock Exchange
4. Sr. Jaime Aguilar - Broker of the Madrid Stock Exchange

B. Method of Study

The factual information and observations upon which this report is based are the product of seven days of extensive interviews and consultations in Madrid and Barcelona with representatives of the Ministry of Finance, the Bank of Spain and officials of the Madrid and Barcelona Stock Exchanges, and the Corredores de Comercio. Senior officials and knowledgeable staff members of major banks, investment companies, mutual funds, insurance companies and of private companies whose stocks are listed on the Madrid and Barcelona Stock Exchanges were also interviewed.^{4/} Visits to the exchanges, bank vaults and computer facilities were included in the program as well as a first-hand review of exchange liquidation procedures, i.e. clearance and settlement of transactions. In addition, a wide variety of written materials were studied including memoranda, regulations and reports provided by the Ministry, the Exchanges and others.

Sr. Vilarasau and Sr. Ruá were particularly helpful in arranging a balanced and complete program during the seven day visit. Sr. Povedá and Sr. Martínez provided valuable assistance. Sr. Planesdemunt and Senorita Vidal of the Barcelona Stock Exchange were also helpful. Special gratitude is due to Sr. Moro, Alternate Executive Director of the World Bank for Spain, Italy and Portugal for his overall assistance and cooperation.

^{4/} A partial list of the persons interviewed is included as Appendix B of this report.

C. Scope of the Report

A broadly-based and efficient securities market in Spain with an enlarged public participation can play a critical role in the economic expansion of the country. However, despite recent increases in listings and volume, the Spanish securities market is not yet equipped for that role. It remains extraordinarily narrow and beset with technical and structural weaknesses. Relatively few companies are listed on the exchanges and the stocks of many officially listed companies are almost never traded. In practice, trading is concentrated in the stock of about 40 companies whose transactions account for 75% of total share transactions. Even for these, prices are often dominated by banks. Further, and of particular urgency, the existing system for the settlement of securities transactions is inadequate, even for the present volume of trades. As a result, delays of as much as six months in clearing securities transactions have occurred. These delays are tangible evidence of inefficiency. They undermine public confidence, divert the attention of the brokers and the regulators, discourage public participation and thwart the immediate growth and long-range development of the markets.

In considering the Spanish markets, special care has been taken to develop recommendations which fit the particular situation, without regard to whether such recommendations would also be appropriate in the United States. It should be noted, of course, that the breadth and strength of a nation's securities markets are influenced greatly by fiscal and economic policy and the general climate that prevails in the economy. These factors, and the broader policy questions they present, are beyond the scope of this report.

Part II of this report focuses on the liquidation process and on developing an efficient system for liquidating securities transactions. It concludes that the ultimate solution to the liquidation problem will be immobilization of certificates in a central depository and strongly recommends that a committee be formed to study the feasibility of achieving this goal. With immobilization, it suggests how securities transactions could be settled through accounting entries between members of the depository without disturbing the traditional role and confidential relationships between individual member banks and their clients.

Part II also recommends a number of steps which could be taken to end the current delays in liquidation if it is determined to proceed with immobilization gradually over an extended time. They include suggestions for developing a formal reporting system to monitor outstanding transactions, introducing efficiencies through mechanization and consolidation of electronic data processing operations, elimination of certain manual back office procedures and extending current procedures, now used for money, to the settlement of certificates as well. This part was the primary responsibility of Mr. Green.

Part III of this report discusses the operation of the markets and considers steps to achieve greater depth and liquidity. This section sets forth a program for developing more efficient securities markets - increasing the numbers of brokers, permitting brokers to associate and creating incentives to improve exchange services. It suggests that banks be permitted to own brokerage firms and defines as a longer term goal the development of a centralized market structure. This part was the primary responsibility of Mr. Poser.

Part IV concentrates on the importance of disclosure, a basic ingredient of an efficient and fair market, in attracting capital to the securities markets. It concludes that the lack of information is a particularly acute problem in Spain and recommends steps for increasing the quantity and quality of disclosure and attracting more companies to the securities markets.

Part IV also recommends development of uniform accounting standards and points out how fiscal incentives impede full disclosure and listing.

It comments upon the need for financial intermediaries to assist companies in issuing securities to the public. Finally, it analyzes the impact of issuing shares at market value rather than at nominal or par value on the efficiency and narrowness of the markets. This part was the primary responsibility of Mr. Mendelson.

In conclusion, Part V sets forth some general observations.



PART II

LIQUIDATIONS

A. Introduction

This section discusses liquidations, i.e., clearance and settlement, the processes involved in completing a purchase or sale of securities. Clearance involves comparing both sides of the trade to insure agreement on such details as the number of shares traded and the price. Settlement entails delivery of the securities from one broker to the other in exchange for payment.

Most countries that have experienced a very active stock market, including the United States, have encountered, in varying degrees, the problems in clearing and settling securities transactions encountered in Spain during the year 1972. The problems in Spain, however, are particularly acute. The present volume of transactions is relatively small yet the existing system does not provide adequate service. Delays of up to six months in the liquidation of securities transactions have not been uncommon. Such an inefficient system undermines public confidence in the markets and impedes their continuing growth.

1. Settlement

Transactions should generally settle within eight days in the case of bearer shares and twenty-one days in the case of registered shares. However, because certificates are generally not delivered to the buyer for purchases, when he in turn becomes a seller, he cannot deliver those certificates within the customary time. Thus, as undelivered shares are traded - but not delivered - an ever increasing chain is created which intensifies the liquidation problem.

On each securities transaction, the brokers manually record the certificate numbers on the following documents:

- A. The "Nota de Intervencion," the delivery slip handed by the selling broker to the buying broker.
- B. The "Vendi," the receipt signed by the seller to his broker.
- C. The "Poliza," the title deed delivered by the broker to his purchasing client.
- D. The "Registro" book of the seller's broker.
- E. The "Registro" book of the buyer's broker.
- F. The transfer deed in the case of registered stocks.

When it is considered that certificate numbers may have as many as nine digits and the certificates may or may not be in numerical sequence, recording certificate numbers in connection with a transaction can require an enormous amount of clerical time and thereby contributes to the delay in the processing of outstanding securities transactions.

3. Clearing House Procedures

Under the settlement system used today securities must be passed for each trade. The seller's broker is required to present securities and the buyer's broker must receive securities on a trade by trade basis. In contrast, the cash involved in the same transaction is settled on a net basis between each broker and a bank.

B. Factors Which Delay Liquidation

Upon analysis, the problems presented by these practices can be summarized as follows:

(1) Failure of clients, institutions as well as private individuals, to deliver to the selling broker the securities sold on or before settlement date. This slows down the clearance process and also presents opportunities for unfair riskless trading.^{5/}

^{5/} Because a purchaser is not required to pay for his shares until they are received, in a rising market he can take advantage of the delay in receiving his certificates by realizing stock appreciation without committing any of his own funds. Conversely, in a falling market, a purchaser could attempt to cancel his trade and thus subject the broker to the loss in market value from the trade date.

(2) The existing back office procedures followed by brokers, including the manual recording of certificate numbers on numerous documents, inhibit an efficient operation.^{6/}

(3) The present clearing house procedure of liquidating the securities on each trade separately instead of on a net basis is cumbersome and unwieldy.

(4) In certain areas of both the Madrid and Barcelona exchanges, conditions are overcrowded and not conducive to the efficient processing of securities transactions. In the clearing house areas at the Madrid Stock exchange especially, brokers' employees work in extremely crowded areas with stacks of securities out in the open on tables and in some cases even on the floor. This work area has very poor lighting and during the trading session each day the level of noise from the exchange floor is high. Moreover, there is limited physical space for expansion of exchange facilities.

Efficiency in the clearance process is complicated by other factors as well. First, as discussed in detail in Part III, the present structure of the Spanish Law does not allow brokers to join together.^{7/} Because they must operate independently of one another, brokers are limited, as a practical matter, in the amount of funds they can direct to hiring qualified employees and providing for a more efficient processing operation. Second, Part III also points out^{8/} that the principal source of income

^{6/} Two of the basic documents outlined above, the "Poliza" and the "Registro," which are required to properly process a security transaction in Spain are unique as compared with the documents required in the United States.

^{7/} Part III, p. 27, infra.

^{8/} Part III, pp. 26-27, infra.

for many brokers, is the function of notarization. This factor may tend to encourage brokers to devote more of their resources and concentrate more of their attention to the notarial function. As a result, liquidation and other exchange related procedures may suffer. Finally, listed companies generally issue shares in very small denominations, as little as 500 or 1,000 pesetas for each bond certificate and 500 pesetas for each stock certificate. Therefore, a considerable number of certificates are printed for each new issue, maximizing the processing problem for the people who have to handle and record the certificates. In addition, certificate dimensions are not standard and, because most of the certificates are in bearer form, cutting of coupons also can contribute to delays in processing.

C. The Long-term Goal

The entire investment community, the brokers and the exchanges and the banks should begin now to develop a more efficient low cost processing system which will permit transactions to clear in a reasonable period of time. To achieve this goal, the stock certificate should be immobilized in a central depository and securities transactions processed through the use of accounting type entries among members of the central depository. Eventually, if practical, the stock certificate may be completely eliminated.

It is readily apparent that this is much easier said than done. However, with the full cooperation of all interested parties, it should be possible to adopt a system that will fit current and future needs.

D. Improvements Already in Process

The failure of clients to deliver securities sold to the selling broker is not a problem unique to Spain. What has been unique however, has been the inability of the Spanish brokers to determine the magnitude of this problem both for bearer and registered shares.

A number of significant steps have already been taken to deal with this situation and improve the liquidation process.

1. Utilization of Computers

The Madrid Stock Exchange installed its computer in October 1972 while the Barcelona Stock Exchange computer had been installed some time earlier that year. ^{9/}

With the installation of the Madrid Computer, the Exchange requested all Madrid brokers to submit to the Exchange their open transactions in securities that were executed before the electronic data processing (EDP) equipment became operative. A Liquidation Committee was established by the Exchange to follow-up on older trades which did not match-off between the buying and selling brokers and to monitor the brokers' progress in liquidating outstanding transactions.

^{9/} We understand that neither the Barcelona nor the Bilbao Stock Exchange has a significant liquidation problem.

In general terms, the computers at both the Madrid and Barcelona Stock Exchanges for each trading day now produce a daily listing of "Operaciones del Agente." This provides each broker with a list of the trades he has executed that day, the name of the broker on the other side and a comparison of the essential information required by each broker including the name of the security, the number of shares bought or sold and the price. In addition, it provides each broker with other information such as his commission, taxes and total amount for each transaction.

The computer also provides each broker with the following documents for use in processing each transaction.

-
- (1) "Operaciones Al Contada" - a confirmation slip to his client of the details relating to the trade the broker has executed.
 - (2) "Poliza De Operaciones Al Contada" - the title deed delivered by the broker to his purchasing client.
 - (3) "Vendi De Operaciones Al Contada De Todas Clases" - the receipt signed by the seller to his broker.

This information is available to each broker the next morning at which time he must have his employees perform procedures such as adding the name and address of the clients and recording the certificate numbers. The broker himself must sign these documents and place his seal on them.

The exchanges' computers also provide each broker with a listing of those trades he has cleared-up (liquidated) the previous day and indicate the net amount of money due to him or payable by him. This listing is referred to as "Operaciones Liquidados Por."

2. Programs Established by the Ministry of Finance

In addition to Exchange monitoring of liquidation problems, the General Director of Financial Policy for the Spanish Government has established two committees composed of representatives from the government, banking and the stock exchanges to work on these problems.

The first committee is assigned the responsibility of clearing-up older transactions through a repurchase procedure. With respect to bearer securities, in January 1973 the committee had established certain repurchase dates through March 1973 which were designed to reduce the delay in liquidating outstanding transactions to approximately two and one-half months. It had also prepared a list of banks that were delaying the transfer of registered securities and was considering submitting the list to the Banking High Board. In addition, the committee was considering applying the repurchase procedure to older outstanding registered securities transactions.

A second committee was assigned to work on a long range solution to the problems of the Spanish Securities Markets.

3. Multiple Certificates

The Compania Telefonica has developed a system to overcome the problem of handling many certificates with the issuance of multi-certificates ("SERLIVAL"), but it still requires the issuing company to print the original certificates and leave them on deposit with a bank. The multi-certificate is issued based on the instructions of the purchaser through his broker.

Briefly, this system utilizes the computer to maintain control over the certificate numbers, issues one multi-certificate for the required number of shares, machine prints the original certificate numbers and maintains a record for dividend and interest payments. This system may be helpful in certain instances but we are not in a position to make any specific recommendations about it because no study was made of the costs involved nor of the feasibility of its application to the securities markets generally.

4. Bank Central Depositories

In Spain, less than a dozen banks are involved in about 85% of the trading volume on the exchanges. Most of these banks have already consolidated their customer's securities into one main vault location for each bank. Thus the banks themselves have made an interim step in attempting to immobilize the stock certificates for the internal custodial services they provide for their customers.

E. Creation of a Central Depository

The ultimate solution to the liquidation problem will be immobilization of the certificate in a central depository. To this end a high level committee composed of representatives from the banks, various financial institutions, listed companies, private shareholders, the exchange and the government should study how quickly this can be accomplished. They should set a realistic target date and agree upon a program to achieve immobilization of the certificate.

They may wish to consider whether banks should join together with brokers, exchanges and clearing associations to participate in the ownership of such a company under an arrangement similar to that used in the United States.

^{10/}
10/ There is now available in New York and three cities outside New York a Central Certificate Depository which holds the stock certificates for the customers of many brokerage firms and the customers of many banks. The development of this depository has resulted from the effort to immobilize the certificate. The central depository operates through instructions from the members of the depository. Certificates remain in one place and accounting entries are made to record the required security movements for such activity as buy and sell orders, collateral for bank loans, securities loans, and securities borrowed and dividends.

Recently, the Central Certificate Depository was reorganized as a separate company (previously it was a division of Stock Clearing Corporation - a wholly-owned subsidiary of the New York Stock Exchange) with ownership based on the use of the depository by its participants. The board of directors is presently composed of representatives of member banks of the New York Clearing House Association, the American and New York Stock Exchanges, the National Association of Securities Dealers and seven persons chosen by the New York Stock Exchange.

It is intended that this Depository will be reorganized shortly into a limited purpose trust company chartered by the New York State Banking Department. Because of present legal restrictions it would be owned by the New York Stock Exchange. This company would then seek membership in the Federal Reserve System. Efforts will be made to amend various laws to make it possible for a depository to be owned by entities in addition to a national stock exchange so that ownership of the trust company's stock could be adjusted annually based on the extent to which participants in the depository used its services during the previous year. Thus, brokers, clearing corporations, banks, insurance companies would have the opportunity to own and share in the trust company.

One method of creating such a central depository would be to utilize the vaults and other facilities which the larger banks have already established in order to consolidate their customers' securities. These dozen or so centralized vaults could be rented from the banks or purchased by the depository, perhaps in exchange for its own securities or by reduced usage fees. Under such a system, securities could either be placed in any vault controlled by the depository or each depository could take custody of the securities of those companies whose names began with designated letters of the alphabet. Personnel of the banks, who presently operate these vaults, could be employed by the depository.

In essence, the depository could be a computerized bookkeeping system. Officials of the depository would know the number of shares of a particular security belonging to a particular bank's customers but not the names of those customers. For example, the depository responsible for companies A through C might have the physical securities for 100,000 shares of the Asland Cement Co. In such a case its records would show that 20,000 of those shares belonged to customers of Banesto; 40,000 to customers of Banco Bilbao; and 40,000 to customers of Banco Urquijo. Each bank could maintain the records of the accounts of each of its customers. When a dividend is paid, the company would send a check to the central depository for all shares it holds, the depository would then credit each bank for its proportionate share. Each bank in turn, utilizing its own records, would credit each customer for the amount based on the shares that customer owned.

Certificates would be immobilized but none of the prerogatives which the banks presently enjoy would be disturbed. Each bank would retain its traditional role and its traditional relationship with its individual clients such as voting proxies and receiving custodial fees.

There may be other processing systems that can be utilized in Spain. Instead of designing a new system, it might be more advantageous to adopt an existing system. The experience of present users and operators of the system would provide better cost estimates and the pool of expertise available would make a shorter period of implementation likely.

We have been informed that the systems of immobilizing certificates presently in use in France and in Germany have been studied by various interested groups and they have passed on their recommendations to the government. We are not aware of the status of these recommendations and because we have no experience with either of these systems we cannot comment on them. We suggest that, in addition to the systems being developed in the United States, ^{11/} the systems in those countries should also be considered.

^{11/} One of the earliest and now most nearly complete movements toward a comprehensive book entry system for transfer of U.S. Government securities is that developed by the U.S. Federal Reserve in cooperation with the U.S. Treasury, banks in the money market and money market dealers. In essence, definitive paper government securities are eliminated, and a record of ownership is stored in a computer operated by a Federal Reserve Bank. Interest on all book-entry securities is directly credited to owners' accounts. In other words, the piece of paper representing a Government obligation is simply recorded on the "books" - generally computerized - of a Federal Reserve Bank.

F. Intermediate Steps

Depending upon how quickly the committee studying this question comes up with its conclusions and thus provides everyone with a goal and a timetable and how immediate that timetable may be, it may not be advisable for brokers and exchanges to make any sizeable investments for space, equipment or developing new systems because those systems may not be required once the certificate is immobilized. If it is decided to move to immobilization on a gradual, extended basis, a number of interim steps could be taken to reduce delays in liquidation. Many of these can be adopted without significant disruption and with relatively little cost; others should be viewed as practical only if it is determined that ultimate immobilization is not attainable within the reasonable future.

1. Reporting System Regarding Liquidations

The reporting procedures already instituted for older transactions involving bearer securities are an initial step in reducing the problem. Depending upon the backlog for registered securities, the same type of procedures should be considered for them.

A formal reporting system should be adopted under which brokers would be required to report to the Liquidation Committee which in turn would report to the Exchange's Board of Governors who would in turn report to the government-formed committee. The system should require:

(a) A report to be prepared at least as frequently as each month-end summarizing the number of open transactions, their contract price and the current market price (so as to determine the broker's risk) on an aged basis of from 30 to 60, 60 to 75, and for over 75 days for each transaction, with an explanation why each is still not liquidated.

(b) A report showing this information should also be prepared by name of broker to enable the monitoring of the performance of individual brokers and also to determine which customers (banks) contribute to the failure to deliver the securities on settlement date.

Most of the information required for these two reports is presently available as out-put from the computer of the Madrid Stock Exchange and can be summarized. The computer does not yet provide the current market price which is needed. If the market price were included, the report could highlight those items with the greatest market risk (i.e., where the trade price is higher than the current market price on the buy side or conversely is lower than the current market price on the sell side). Because such items have the greatest potential exposure to the individual broker if the trade is not honored the Liquidation Committee could then require brokers to liquidate them on a priority basis.

2. Length of Time Before Exercising Repurchase Rule

In the United States, the repurchase rule is normally exercised when a transaction between two brokers is outstanding for 30 days. Recently a new rule has been adopted

which requires that those customers who sell their securities but fail to deliver them to their broker within 10 days must be repurchased. As the Spanish brokers become familiar with the repurchase procedure, the current lag of 2-1/2 months should be reduced to a shorter period of time.

3. Article 139 of the Stock Exchange Regulations

Article 139 of the Stock Exchange Regulations which relates to "spot transactions" permits the exchanges to require those banks and other institutions as well as private individuals, who are continually late in delivering their securities or funds, to present such securities or funds before the broker executes a trade. This Rule should be applied when appropriate and, if it cannot be applied generally, consideration should be given to adopting a similar rule for regular transactions. Under it the Exchange would be granted the authority to require that sellers have securities in hand before the broker could proceed to execute a transaction.

4. Study Elimination of the Registro and Poliza

As an interim step to provide for a more efficient system for processing securities transactions, a study should be made of the possibility of eliminating the "Registro" and the "Poliza" or, if deemed required, of substituting more practical and efficient procedures for completing these forms. We realize that this is a complex problem and

we understand that these two documents are a very important part of the role performed by the Spanish broker. However, in light of the need for a more efficient system for processing securities transactions and the goal of eliminating the certificate, elimination of these documents should be considered.

As possible alternatives to the present procedures, we suggest that if the Study concludes that the "Registro" is necessary, it could be adapted to a microfilm presentation. Brokers could be allowed to microfilm security certificates as they are processed through their offices in lieu of manually recording the certificate numbers in a book. Such microfilm records could be considered the "Registro." As a substitute for the "Poliza," the study might consider having the broker place his stamp as a guarantee of good title on the certificate to his purchasing client.

5. Denomination of Securities

It is readily apparent that the current practice of issuing securities in denominations as small as 500 pesetas adds to the processing problem. Therefore consideration should also be given to requiring a higher minimum denomination for the issuance of securities.

6. Consolidation of Clearing Houses

A study should be made of requiring only one clearing house system to be used by all the exchanges with the eventual possibility of consolidating the EDP operations into one place. Such a consolidation of clearing house operations can be accomplished without requiring the exchanges themselves to consolidate.

The study should determine the present advantages and disadvantages of such a consolidation and also consider the experience to be gained under such a consolidation and the costs involved. It would seem most logical that only one clearing house system be required if and when the certificate is immobilized.

7. Consolidation of Processing Systems

The processing systems used by the Madrid and Barcelona Stock Exchanges appear similar in many respects. We recommend that a study be made of the economies to be achieved of a uniform processing system for both exchanges and the possible eventual consolidation of their EDP operations into one location. This would save money and duplication of effort.

8. Net Settlement of Securities Transactions

As indicated above, a major problem with the existing settlement system is that the broker must present securities for each trade when he is on the sell side and receive securities for each trade when he is on the buy side. In contrast, he is allowed to settle money on a net basis. The use of a net settlement system should be expanded.

In the United States most exchanges have clearing corporations which compare the trades of the buying and selling broker. Two systems have evolved: the "daily balance order" method used by the New York Stock Exchange's Stock Clearing Corporation and the "continuous net settlement" system used by several other exchanges and in connection with over the counter transactions.

Under the "daily balance order" method, the clearing corporation nets out on settlement date each day's purchases and sales submitted by firms which are clearing members. This process produces a daily net balance of shares to be delivered or received, depending upon whether a firm that day was a net seller or a net buyer of a particular security. As the brokerage firms deliver or receive their designated balances of securities through the clearing corporation, the money balances, which have been similarly netted, are also settled. When a firm cannot deliver its stock, this creates a "fail."

Under the "continuous net settlement" system, the clearing corporation acts as an intermediary rather than a keeper of accounts between

different firms. The brokerage firm settles with the clearing corporation, which, in effect, stands on one side or the other of every transaction. Thus, the firm becomes either a debtor or creditor of the clearing corporation. This system provides for more effective control over "fails" because the clearing corporation is on the opposite side of every transaction.

In Spain, individual orders are issued for each transaction. If the "Poliza" and "Registro" were eliminated it would be possible to offset similar buy and sell orders and to issue balance orders for the remainder or ultimately to shift to a continuous net settlement system. This change would be a very important one but, as with the case for all of the intermediate steps, it should be weighed in light of the target date for immobilization of the certificate.

9. Back Office Procedures

A study should also be made of the back office procedures which will be required in the future as the exchanges and clearing houses develop more sophisticated processing systems for handling securities transactions. It is important that efficiencies - such as reducing the number of records required, eliminating manual recording, and reducing the volume of securities to be handled - be incorporated into the back office operations. If such improvements are not made, the back office operations will still not be able to clear the volume of trading even though the exchanges and clearing house are processing the transactions more efficiently.



PART III

OPERATION OF THE MARKETS

A. Introduction

The underlying purpose of a nation's capital markets is to facilitate the channeling of savings into productive investment. This function necessarily involves the distribution of newly issued securities to public investors and the trading of outstanding securities in a secondary market. A good secondary market mechanism is an efficient mechanism for establishing the prices at which securities are bought and sold and thus allocating the savings of investors to the most efficient and productive industries and companies. This part of the report is directed to the secondary market - its effectiveness is directly related to the liquidity it provides: can securities be converted into cash, or cash into securities, without delay and at prices which are fairly arrived at.^{12/}

It evaluates the performance of the secondary markets. To the extent these markets are less than effective, problems are identified and possible remedies suggested.

The dominant elements in the secondary markets in Spain are the financial institutions of the country; in particular, the brokers, the exchanges themselves and the banks.

^{12/} The quality and quantity of information available to the public with respect to the securities traded in the secondary market also has an important influence on its effectiveness. This is discussed in Part IV.

B. Stock Exchange Brokers

The Spanish stock exchanges, located in Madrid, Barcelona and Bilbao consist of associations of brokers (Agentes de Cambio y Bolsa). Each broker must receive the approval of the Ministry of Finance for his appointment.^{13/} The number of brokers on each exchange is limited by exchange rules, which also require the approval of the Ministry of Finance. The present limit on the number of brokers is 63 in Madrid, 45 in Barcelona and 30 in Bilbao.

To become a broker a person must have a university degree in law, economics or some other related discipline and he (or she)^{14/} must pass a difficult and comprehensive examination administered by the Ministry of Finance. Since preparation for the examination requires at least a year of study, and it is given only at infrequent intervals, it is often not possible to fill vacancies until a number of months, or even years, have passed. Perhaps for this reason, in

^{13/} There are also approximately 400 local brokers (corredores), located in 34 other cities and towns, who have official status and handle brokerage transactions. With a few exceptions, however, the amount of securities business which these brokers account for is minimal. The major portion of brokerage orders received from customers outside the three cities in which there are stock exchanges is handled by the banks.

^{14/} Barcelona has one woman broker, who, we were told, is the only woman in Europe to hold a position of this kind.

January 1973, the actual number of brokers was substantially smaller than the maximum number permitted. While Madrid, with 60, was close to the maximum, Barcelona with only 31 and Bilbao with 21 had only about two-thirds of their allotted members.

Despite the fact that most brokers need to pass the examination,^{15/} family connections may also be a relevant consideration in their appointment. For example, we were told both in Madrid and Barcelona that about 25 percent of the brokers were sons of brokers.^{16/}

1. The Broker as a Notary

The principal function of the Spanish broker, in contrast to the situation in the United States and many other countries, is not to provide brokerage services to customers, such as research, investment advice, and execution of transactions for the purchase or sale of securities. Rather, it is to provide an official imprimatur in order to complete a securities or credit transaction and make it valid in the eyes of the law. In this respect, his function is more closely comparable to that of a notary rather than that of a broker.

It is important to understand the significance of the notarial function. Although brokerage commission rates are low by the standards of most countries (.25 percent of the value of the transaction), the

^{15/} A certain number of brokers are ex-clerks of the exchange who are appointed on the basis of their seniority.

^{16/} On the other hand, to some extent the choice of the brokerage profession, like many others, may be influenced by a natural desire to follow in the footsteps of one's father.

rigid limitations on the number of brokers and the notarial requirement combine to make appointment as a broker extremely valuable. The Spanish broker is assured of a good income by exercising his function as a public notary. As a consequence, and because of the low commission rates in effect, there appears to be little incentive for most brokers to encourage members of the public to purchase securities or to make available to customers a full range of brokerage services.

The position of the broker as an essentially neutral, if not passive, factor in the market is reinforced by certain limitations which are placed upon his activities. First, he is not permitted to establish or join a firm or any other association, whether with another broker or with a non-broker. Every broker is thus required to act as an individual, independent of any outside interest. Second, a broker is not permitted to purchase or sell securities for his own account. He must act purely as an agent for others. These restrictions are strongly defended by some brokers and stock exchange officials, on the ground that the brokers form a "pure," egalitarian society, independent of any political or economic group.

There is a question, however, whether the independence of brokers is more a matter of form than substance. As described more fully below,^{17/} many brokers appear to be dominated by banks, and one Barcelona broker

^{17/} Pp. 34-36, *infra*.

is a "silent partner" in a firm which acts as portfolio manager and financial consultant. To this extent, one must question whether the "purity" of brokers is real, rather than illusory.

In any event, these two limitations - independence, whether nominal or real, and the prohibition against acting as a dealer - result in several very real disadvantages.

2. The Requirement of Independence

The requirement that a broker be independent of a business association or firm effectively limits the scope and nature of his activities. If he wishes to provide better services to his customers, either with respect to research, execution of transactions, or handling of securities, he is forced to rely entirely on his own capital resources and what he, as an individual, can borrow.

Operating on an individual basis, a broker is also denied the economies of scale which may be available to a firm in connection with the handling of accounts, automation, etc. Furthermore, a broker's business lacks continuity, since it lasts only until he retires or dies. This may, over the years, prevent the growth of a large clientele. Finally, it may also impede the development of an effective staff. Every employee of a broker knows that, when his employer dies or terminates his brokerage business, he will need to find a new position.

3. The Prohibition Against Acting as a Dealer

A broker's activities are further limited by the prohibition against a broker also trading in the market as a dealer for his own account. This prevents him from "making a market" in securities, i.e., using his own capital to contribute to the liquidity and orderliness of the markets. This is an important function of "specialists" and other broker-dealers in the United States, and is a major factor in providing liquidity to those markets. Under the specialist system, every listed stock is assigned to a particular "specialist unit," which is then required to minimize price variations between successive transactions and add stability to the market by purchasing stock when the market price is declining and selling stock when the market price is rising. Since the specialist has a critical role in the market, his activities are closely watched and regulated.

Certainly the restriction against trading for their own account has the advantage, at least in theory, of preventing brokers from involving themselves in conflicts between their own interest and the interest of their customers for whom they act as agent. Nevertheless, it seems doubtful whether forbidding brokers to trade for their own account is, on balance, a positive factor in enabling the Spanish stock markets to serve the economy of the country effectively. In the first place, as will be indicated later, the Spanish banks and other companies, through their affiliates, sometimes perform this

market-making function through purchases and sales of their own shares.

To this extent, this activity is performed without any disclosure to the public, the stock exchange, or the Ministry of Finance, and is therefore vulnerable to abuses such as market manipulation.

Secondly, and of even greater importance, it may well be that if such activity were permitted under careful regulation by the exchanges and the Ministry of Finance, it could actually contribute to the liquidity of the markets, without adding significantly to the potentiality for abuse.

C. The Stock Exchanges

The Madrid and Barcelona stock exchanges^{18/} are governed by seven-man councils of brokers which are elected by the membership of each exchange. One of the seven is elected as president. Members of the council and the president are elected for two-year terms. The councils do not include any representatives of the public, the banks, or the companies whose securities are traded.

The exchanges are open four days a week (Tuesday through Friday) for trading sessions which last from 10 a.m. to 11:15 a.m. Although several hundred securities are listed on each exchange,

^{18/} The much smaller Bilbao Stock Exchange was not visited and will not be specifically discussed in this report. Nevertheless, we understand that many of the observations which we make here concerning the two larger exchanges are equally applicable to Bilbao.

only about 50 corporate stocks are traded on a daily basis. During the trading session, particular stocks or groups of stocks are traded for periods lasting between 5 and 15 minutes. In Madrid, the focus of activity moves from location to location on the trading floor; whereas in Barcelona, all stocks are traded at one location while bonds are traded at another. After the trading period has ended for any particular stock, transactions in that stock may take place on the exchange (not necessarily within the restricted area where only exchange members may go), but only within the price range established during the trading period that day and posted on the wall of the exchange.

1. The Five Percent Limitation

In many instances, stocks are traded at only one price during a given trading session, but this is not always true. Under the rules of the exchanges, the price of a stock may not vary more than five percent from the previous day's price. If the price of stock reaches this limit, trading must be halted immediately, unless a special ruling can be obtained, for example, in the event that news concerning a company suddenly changes the market value of this stock.

This limit on daily price fluctuations (for which there is a counterpart in the United States commodities markets, but not in its securities markets) can be regarded in a sense as a method of ensuring the preservation of the fairness and orderliness of the markets in unusual situations. As indicated above, in the major United States

stock exchanges this is accomplished by imposing on an exchange member called a "specialist" the responsibility for maintaining fair and orderly markets.

It seems questionable whether preventing a stock from moving beyond an inflexible price limit adds to the liquidity of the market. On the contrary, it may do precisely the opposite, since its effect may tend to be to prevent investors from buying or selling at prices determined by the market mechanism, or, perhaps more likely, it may actually divert from the floor transactions by investors who desire to trade secretly without regard to the five percent limitation.

2. Arbitrage in Dually Traded Securities

A number of stocks are traded on both the Madrid and Barcelona exchanges, and a limited amount of arbitrage^{19/} takes place in some of the more active issues. Some concern has been expressed with respect to this practice and the existence of price differences in securities traded on both exchanges has been described as a problem resulting from the lack of good communications links between the exchanges. An automated system, whereby quotations in dually traded stocks could be shown simultaneously on both exchanges and orders automatically switched to achieve the best execution, would eliminate this situation.

^{19/} Arbitrage is the simultaneous or nearly simultaneous buying and selling of the same security traded in two markets to reduce or eliminate any price disparities which may arise. For example, if a stock can be purchased at 10 in one market and sold at 10 1/4 in another market, an arbitrageur can make a profit, without risk, by executing these two transactions.

Undoubtedly the opportunity for arbitrage does exist.

However, to move to such an automated system at this time may not be necessary. A review of the trading data for one stock, chosen at random (January 9 to 12, 1973), does not indicate that price variations in dually traded securities between the Madrid and Barcelona stock exchanges are unreasonably large. Furthermore, it does not appear that the volume of trading at the present time would justify incurring the substantial costs which would be involved in developing such a simultaneous quotation system. In this context, if a choice must be made, it is clear that the necessary fundamental institutional changes in the Spanish markets should be given priority over the extremely expensive task of creating a "central market system," which, on the basis of this study, might bring only marginal benefits within the foreseeable future.

D. The Banks

Probably the most important single fact about the Spanish securities markets is that they are dominated by the banks. The influence of the banks extends to every phase of the securities business. Banks with their customers account for the vast majority (estimated at about 80-95 percent) of customers' brokerage orders. Banks retain custody of the securities of their customers and, through their representatives, are able to control how these securities are voted. Through control of customers' securities, together with

their own holdings and control over available sources of credit, banks are able to place representatives on the boards of directors of a substantial number of companies whose shares are publicly traded. One large bank interviewed had no less than 370 directorships through its representatives, while another held approximately 200. An American observer^{20/} has stated: "Banks operate virtually as holding companies, controlling or owning most Spanish industry through a network of interlocking directorates."

Banks also play a leading role in the initiation, execution and settlement of securities transactions. As indicated, most orders to purchase or sell securities are placed, as a matter of course, through their local banker. Throughout the country bank branch managers tend to act as general financial counselors for their customers, advising them whether to invest their savings in stocks, bonds, mutual funds or other securities or to leave them as bank deposits. Thus, what in the United States would be called the "retail" end of the securities business is largely in the hands of banks.

1. The Banks and the Brokers

Although Spanish law does not permit banks to become exchange members, in practice banks also control the execution of orders on the Madrid and Barcelona stock exchanges. Each of the principal banks normally maintains between one and three representatives on the floor

^{20/} Szulc, Portrait of Spain, New York, 1972 (p. 225).

of each exchange in order to handle brokerage orders. It appears that these representatives normally have a high degree of discretion as to the price and timing of the execution of transactions. Because they are not exchange members, bank representatives are not permitted to enter certain delineated areas on the exchange floor where trading takes place. Nevertheless, they remain in close proximity to the brokers and provide continuous instructions throughout the trading session.

By and large the brokers are given little discretion by the bank representatives and tend to act on their direct instructions.^{21/} In some instances, it appears that the bank representatives on the floor actually perform the brokerage function by bidding for and offering stock and that they only go to the broker for his official-- and legally necessary--authorization of a transaction after it has been completed. In situations where a bank does not have a representative on the floor of the exchange, it may instruct a broker to keep it continuously informed about the market situation in securities in which it has an interest. This is done by a direct wire from the bank to its telephone booth on the exchange floor.

^{21/} It may also be observed that other institutions, particularly investment companies, also maintain representatives on the floors of the exchanges for the same purpose. With only a few exceptions, the investment companies are themselves controlled by banks.

Through their control of the source of brokerage orders and their physical presence and their activity on the exchange floors, the banks dominate the stock exchanges. This dominance is reinforced by their ability to select the broker or brokers whom they use, both for orders to purchase and sell securities and for the signing of the authorization for credit transactions. Thus, most brokers appear to be largely dependent on the banks for the business which they receive. Particular banks use particular brokers, who "specialize" in particular stocks and are known to be the broker to go if one wishes to buy or sell these stocks. It would seem logical to suppose that, under these circumstances, brokers will normally act in accordance with the wishes of the banks.^{22/}

2. The Banks and the Markets

The role which banks play in the Spanish securities markets is further complicated by the fact that bank stocks are the most active and important group of securities traded on the stock exchanges. Furthermore, it appears to be a common practice for banks, through their subsidiaries or affiliated companies,^{23/} to buy and sell their own

^{22/} In this context it is apparent that broker "independence" is largely nominal.

^{23/} Spanish companies, including banks, are prohibited by law from repurchasing their own securities directly. There apparently is no prohibition, however, against making repurchases indirectly through an affiliate.

securities and securities of other companies in which they have an interest. Since, as indicated above, brokers are not permitted to trade for their own account, this market activity by banks appears to perform the function (which the specialist performs in the United States) of stabilizing, and maintaining the orderliness of, the markets for the securities of banks and, to a lesser extent, other companies whose securities are traded on the exchange. In fact, it appears to be not at all uncommon for a bank (through an affiliate) to purchase its own shares for the purpose of preventing too rapid a decline in the market, and to sell its own shares in order to prevent too rapid a price rise.

While market operations of this kind can fulfill a legitimate function of preventing extreme price fluctuations and thus helping to maintain public confidence in the markets, such operations can also be used to manipulate the market, i.e., to influence market prices for the private purposes of the persons generating the activity. Furthermore, since this activity is entirely secret, there is no way for the public, the stock exchanges, or the Ministry of Finance to know whether activity in a stock is a reflection of the free interplay of public buying and selling interest, or whether it merely reflects the decisions to buy or sell by a bank or other company which is dominating or perhaps manipulating the market in the stock at a particular time.

It is, of course, impossible to know the extent to which stock prices are manipulated, particularly on the basis of seven days of discussion and observation. It is noteworthy, however, that several persons whose position and background merit respect, expressed the belief that stock prices often are not established through the meeting of public orders on the floors of the exchanges, but rather through arrangements made in private away from the exchanges. Inaccessibility of data concerning transactions does not permit these observations to be verified or disproved but in view of the dominant role of banks in the markets, the potential for abuse certainly exists.

A number of persons indicated that it is not unusual for banks to "ration" customers' orders on one side or the other of the market in order to affect the market price of a security. "Rationing" is accomplished by holding back customers' purchase or sell orders for a period of time if the orders go against the direction of the market favored by the executing bank. In some instances, we learned, orders are not executed until as long as three weeks after they are placed by the customer. Such delays may sometimes be the result of inefficiency, but sometimes, apparently, they are intentional.

Another alleged bank tactic for influencing the market is to prevent customers' orders from reaching the market by taking the shares into their own account or selling shares from their own account. In some instances, we understand, two orders to purchase and sell the same security placed by customers of the same bank will not be executed with each other at the market price; instead, the bank will interpose itself between the two orders and thus make a dealer's profit, giving each of the customers a less favorable execution than he might have received if he had been permitted to deal directly with the customer on the other side of the transaction subject only to a brokerage charge.

In addition, many of the quotations on the two major stock exchanges are "theoretical"; in other words, although a quotation may be made in good faith, it may not be possible to obtain an execution of even a small transaction at the price quoted. In other instances, a price may be established by a small transaction on the floor of the exchange, to enable a bank or other financial institution to execute a large transaction at that price.

These observations, made by various people who appear to be knowledgeable about the Spanish securities markets, are repeated here because they underscore substantial questions as to whether the present

institutional structure of these markets is well adapted to perform market functions. On the one hand, there are the exchange members, a relatively small group, whose major occupation and source of revenue is not the handling of brokerage business but rather the performance of an essentially ministerial function - notarizing credit transactions and stock purchases and sales - over which they have what amounts to an official monopoly. On the other hand, there are the banks, which appear to dominate the securities business through their practical control of the customers, the companies whose securities are traded, and even the brokers. Furthermore, since the banks are permitted neither to be members of the exchanges, nor to be represented on their governing boards, they have little or no responsibility as to how they exercise their overwhelming power.

From the viewpoint of the individual investor, the present dichotomy in the role of the brokers and banks in the securities markets makes it difficult to obtain disinterested investment advice.^{24/} As described above, most customers purchase or sell securities through banks, which may have an interest either in discouraging purchases of securities in order to avoid reducing the size of their deposits, or in persuading customers to purchase the securities of the bank itself

^{24/} The importance to a viable securities market of adequate and reliable current information about the issuers whose securities are traded in the market place is discussed in Part IV below at pp. 51-53, infra.

or of affiliated companies. In either case, the customer's interests can be subordinated to those of the bank. Furthermore, a customer has no assurance that his orders will be executed promptly and efficiently at the most favorable price available. Finally, the brokers, restricted by the prohibitive aspect of establishing or joining brokerage firms, are limited in their financial capability to compete with banks and are not in a position to provide customers with the research and other brokerage services which would serve to encourage broad public participation in the markets.

I. Recommendations

The institutional problems discussed above not only tend to lessen public confidence in the Spanish securities markets, but also restrict their growth and development. The restrictions and prohibitions imposed upon these markets, and on participants in them, need to be re-examined. The following are preliminary and general recommendations in this area intended only to serve as a starting point in the analysis necessary for a fundamental restructuring of the markets.

1. The Role of the Broker

Serious consideration should be given to permitting brokers to associate themselves with others and to form brokerage firms. Whatever the historical merits of the present restriction which prohibits brokers from acting otherwise than as individuals, it appears to be outmoded in light of the needs today. It is highly important that brokers have enough capital to be able

to provide their customers with a full range of brokerage services and (as indicated below)^{25/} also to acquire positions in securities. In order to provide this capital base and to enable brokers to furnish such services, brokers should be permitted to associate either with other exchange members or with non-members, subject to restrictions against allowing persons of doubtful reputation, background, or competence to become members of a brokerage firm; and subject also to appropriate regulatory requirements applicable to all persons engaged in any aspect of the brokerage business. It may be pointed out, in this connection, that in the United States a brokerage firm is permitted to be in the form of a sole proprietorship, partnership, or corporation; and that, in the latter case, it may even raise money from the public by the issuance of its own securities.

2. The Role of the Banks

(a) Separation of Banking and Brokerage

In view of the current importance of the banks in the brokerage business, there appear to be sound reasons for permitting these institutions to own brokerage firms. While connections between the brokerage and the banking businesses give rise to difficult problems of conflicts of interest - which in the United States led to the enactment of legislation 40 years ago requiring the separation of commercial banking from investment banking - it may well be that the

^{25/} See recommendation No. 8, pp. 46-47, infra.

present situation in Spain justifies a different solution. An important consideration is that a securities industry, as it is known in the United States, with underwriting, research and other capabilities, does not exist in Spain to any appreciable extent.

It therefore appears desirable to encourage banks, which have the needed resources and expertise, to participate in the development of the securities markets. Furthermore, in view of the fact that banks already exercise practical domination over the brokerage business, it would seem a healthy thing for them also to assume formal responsibility for their activities as exchange members and as participants in the governing boards of the exchanges.

(b) Access to the Exchange Floor

The practice of permitting bank representatives on the floor of the exchanges and permitting them to operate in close proximity to trading operations places them in a position where they can exercise considerable influence on the brokers and enjoy significant economic advantages. The same problem exists to the extent that any other person or institution has access to the floor. Consideration should be given to limiting such access and to developing appropriate regulatory controls over all persons admitted to the floor whether or not they are members of the exchanges.

3. Limitations on Exchange Membership

(a) Number of Members

The present restriction limiting the number of exchange members acts as an inhibiting factor to the growth of the markets. It probably would be advisable to gradually increase the permissible size of exchange membership by stages over a period of time. Certainly, it would seem reasonable for the Madrid Stock Exchange to have a membership of perhaps 200 - 250 and for the Barcelona Stock Exchange to have a total of 150-200, as opposed to the present maximums of 63 and 45, respectively. Since the floors of the two exchanges already accommodate a large number of representatives of banks and other institutions, such an expansion would not seem to place an undue strain on the facilities of these exchanges.

(b) Qualifications for Membership

Related to the above point, the present membership qualifications appear to be too rigid and impractical. It is, of course, important that every exchange member be a person of competence and integrity, but his or her qualifications should be tied to the practical needs of the market. It seems unrealistic and unproductive to require prospective exchange members to take the present exhaustive examination which covers virtually all phases of economics and finance. Rather, the examination should be geared to ensuring that brokers understand thoroughly the business as it is actually conducted and the need to protect the interests of public customers. Furthermore, the examinations should be given with reasonable frequency and more

opportunity should be provided for persons with practical experience-- for example, as employees of members or of financial institutions--to become members, if their training can properly be considered a substitute for part or all of the revised examination.

4. Commission Rates

Serious consideration should be given to increasing the commission rates on brokerage transactions, as opposed to purely notarial services, so as to make the brokerage business stand by itself as an independent profit center for exchange members. One of the salient facts about the present Spanish markets is that no group of persons appears to rely principally on customers' brokerage business for its income. There are probably few if any countries which have lower commission rates than Spain, and this anomaly must be rectified in order to provide adequate economic incentives for a broker to concentrate on providing securities brokerage services rather than performing the notarial function. In revising the rates, consideration should be given to reflecting the lower unit costs of handling larger transactions.

5. Separation of Notarial and Brokerage Functions

Consideration might also be given to separating the notarial function of brokers from the brokerage function. It is recognized that such a separation of functions would be likely to cause dislocations, and we are not recommending any immediate action in this direction. Nevertheless, the eventual goal should be to enable

brokers to earn an adequate living, solely by engaging in the business of servicing brokerage customers. When this is achieved it may be appropriate to consider segregating the notarial function from the brokerage function to the extent that the notarial function might still be needed.

6. Brokers and the Investing Public

Brokers should be encouraged, or perhaps even required, to serve the public, as a condition of admission to exchange membership. They should have offices which are open and accessible to the public and should be willing and able to provide customers with a research capability and other services necessary to a public brokerage business.

7. The Five Percent Price Fluctuation Limit

The 5 percent limit on daily price fluctuations is an artificial restraint on the market, and consideration should be given to its elimination. If a market is to provide for the benefit of public investors, it would seem inappropriate to limit price movements by any arbitrary amount. On the other hand, if the price of a security is influenced by unexpected events, the exchanges have (we understand) authority to halt trading until the information can be generally disseminated to the public. This authority should be exercised to the extent that it is desirable.

8. The Broker as a Dealer

The broker, both individually and, as recommended, as a firm, should be permitted to deal for his own account to the extent necessary to contribute to the orderliness and liquidity of the

markets. While the present prohibition against such activity has the advantage of avoiding certain conflicts of interest, it also precludes the broker from attempting to reduce temporary fluctuations by buying or selling for his own account. It is not suggested that the United States specialist system, or the system used by any other particular country, would necessarily be suitable for Spain. In fact, it would be advantageous to examine the market system of various countries in which brokers are permitted--or required--to deal for their own account in order to develop a system which is appropriate to the Spanish situation. Such dealings by brokers--and perhaps by other financial institutions, such as banks and mutual funds--should be disclosed to, and regulated by, the stock exchanges under the supervisory authority of the Ministry of Finance, in order to reduce the possibility of manipulative or otherwise wrongful activity.

9. Government of the Exchanges

In view of the importance of the stock exchanges to the national economy and to the public generally, it is important that persons other than brokers should also participate in determining the policies of the exchanges and ensuring that they properly perform their public functions. Consideration might be given to including representatives of financial institutions, listed companies, and public investors, along with exchange members on the governing boards of the stock exchanges. Such representation has the additional benefit of providing exchange members with a kind of "window to the world"--access to viewpoints

of the business community and the public, which may differ significantly from their own viewpoint. Such an organizational change should be an important step in enhancing public confidence in the markets.

10. Self-Regulation

Finally, it would be clearly desirable, in order to increase investor confidence in the securities markets and to develop these markets to the maximum degree possible, for additional regulation to be introduced over the operation and structure of the markets and the professionals who participate in them. A large portion of this regulation can best be implemented and administered by the stock exchanges themselves, as is the case in the United States, where an officially sanctioned self-regulatory system has operated for many years, with generally beneficial results.

Such a system of self-regulation has several important advantages over direct governmental regulation. Those who are involved in the securities business on a day-to-day basis necessarily have more expertise and closeness to the markets than even the most competent government regulator could acquire. Furthermore, self-regulators, being closer to the scene, can act faster, move flexibly and more efficiently than the government can. Perhaps most important, industry self-regulators can hold brokers to ethical standards of conduct which go beyond purely legal rules imposed by a government agency.

It is imperative, however, that the Ministry of Finance be in a position

adequately to supervise the self-regulation to assure that it will be effective. The Ministry should also have the authority to take action itself in case of necessity. An adequate staff at the Ministry should be trained to perform the self-regulatory oversight function.

It is premature in this report to attempt to describe the details of the areas in which self-regulation can be particularly fruitful. It should require brokers and financial institutions to keep records of, and periodically to report, data concerning trading from accounts in which they or their affiliates have an interest. Prohibitions against manipulations of securities prices are also essential. The development of a "specialist" system would require additional self-regulatory controls to prevent conflicts of interest and to ensure that the specialists are properly performing their market-making functions. As discussed in Part IV, the stock exchanges through their standards for listing, can also be instrumental in developing standards for disclosure of financial information by listed companies.



PART IV

IMPROVING DISCLOSURE AND ATTRACTING CAPITAL
TO THE SECURITIES MARKETS

A. Introduction

The Spanish securities markets are not representative of Spanish industry. In January 1973, 166 of the 300 largest industrial companies in Spain were not listed. Of the 134 which were listed, many are closely held companies, quoted simply to reduce transfer taxes for their small groups of owners. Only 67 had meaningful quotations. No more than 40 had a meaningful trading volume. In fact, a mere 10% of the companies listed accounted for 75% of total volume.

With the present limited capacity for transfer of securities and liquidation of transactions and the impediments to the improvement of market mechanisms, expansion of the securities markets has been difficult. However, to the extent these problem areas are alleviated, as suggested in Parts II and III, significant broadening of the markets and increased investor participation should become possible. Unless this broadening is achieved, Spanish industry will continue to be deprived of a significant source of capital to finance further expansion. In fact, without broader markets and increased investor participation, adoption of electronic data processing techniques to clearance and liquidation problems, restructuring of the exchanges and revision of the regulations applicable to brokers and banks, will provide the structure of a viable marketplace but not its substance.

This part of the Report first discusses the need to establish an environment designed to build investor confidence and build greater public participation by the provision of adequate information about the companies whose securities are traded in the markets. It then discusses steps which might be taken both to provide a market for securities of privately or narrowly-held companies and to encourage the companies to seek greater public ownership of their securities. Conclusions and recommendations in both respects are then presented.

B. Improved Disclosure

Full and complete information is essential for evaluation of the merits of a security investment. It is fundamental to reach that level of investor confidence necessary to a broad-based public participation in the markets. A wide range of financial data on results of operations, profitability and prospects are the raw material of the securities markets. This data can be disseminated to the public as a basis for investment analysis and informed investment decisions in the form of statistics, market letters, periodic and annual reports, company and industry studies.

With very few exceptions, however, present practices do not provide the investing public with adequate financial information. Very little information is given to the public by most companies. ^{26/} and

^{26/} There are two major exceptions: banks are required to and do furnish a great deal of information to the Bank of Spain and investment companies operate under a system of auditing and disclosure. Also, it should be noted that in recent years several of the actively traded companies have significantly improved the quality of their annual reports.

what information there is may not be easily understood by an unsophisticated investor. Even for the sophisticated investor, sources of information are limited. Annual reports can be quite helpful, but if a company is not listed it is not required to publish an annual report and even some listed companies do not provide an annual report to the exchanges despite market regulations which require them to do so.^{27/} Perhaps 40 companies issue quarterly reports. Generally speaking these are the same 40 whose securities already have an adequate market. Relatively few companies publish complete profit and loss statements. The tax rolls and the bank index are also sources of information for skilled analysts.^{28/} Ironically, in many cases, a company's published books are often the last place to find dependable information. Assets, costs of goods, and sales may be understated; dividends and services may have been paid but not declared; one set of books may be kept for the tax collectors and another for the banks. As a consequence, investment information, to a large degree, is concentrated in the major banks, thereby reinforcing their dominant position in the markets. Further, to the extent that investment information is concentrated with the banks, a relatively small group who may tend to view matters from the same perspective, narrowness and volatility of the markets tend to be maximized.

^{27/} Stock Exchange Regulations, Article 47.

^{28/} The bank index, published by the Department of Hacienda, may indicate that a bank believes in the company's prospects because it has loaned money at less than the prevailing rate.

It is readily apparent that the flow of public information about companies is restricted by two principal factors - disclosure requirements are inadequate and not enforced and the role of the independent public accountant has not yet been adequately defined.

1. Existing Disclosure Requirements

(a) Role of the Ministry of Finance

Responsibility for internal financing and regulation of the securities markets is concentrated in the Department of Financial Policy of the Ministry of Finance. This Department is also responsible for (1) external financing, (including relations with the International Monetary Fund and the World Bank); (2) financing entities (including banks) and (3) insurance companies.

As of January 1973, the Office of Internal Financing, which had the entire staff responsibility for enforcing the existing regulation of the securities markets, consisted of seven professionals including the Subdirector for Internal Financing. Within the office two persons are assigned to qualification of brokers and one each to issues of bonds, qualification of bonds for savings banks, mutual funds and closed-end investment companies, the stock exchanges and other

29/ Spain does not have a separate Securities Law. Instead, its Code of Commerce gives the government the power to establish stock exchanges and authorize their operations (Article 65) and to determine what items will be the subject of dealing on them (Article 67). Under the Code public stock and securities, and securities issued by private or legally constituted companies or enterprises may not be included in "official quotations" unless dealing in them has been authorized. Nor may stocks or securities of companies which are not inscribed in the Mercantile Register be included or of those companies which have not been issued in accordance with the Code or special laws. (Article 72) Article 73 permits regulations to fix everything concerning the internal regime of the stock exchange and the government to fix the brokers' commission scale. Articles 95 and 96 respectively, set forth specific obligations of brokers and restrictions on their activities.

30/ This does not include the Bank of Spain which we understand is under the direct supervision of the Minister of Finance.

qualified securities markets. In addition, the Department of Financial Policy includes a newly created unit which inspects investment companies and the stock exchanges, a four man economic research department, a lawyer and administrative personnel. With the exception of investment companies, however, this Department does not administer any program of required disclosures.

(b) Exchange Reporting Requirements

Spain does not have a requirement that companies issue any kind of prospectus or report to investors when they expand their capitalization through the issuance of new shares. However, Chapter V of the Stock Market Regulations (Articles 26 and 27) requires comprehensive disclosures and documentation to be provided with an application for listing. As a consequence, the corporate public disclosure program, to the extent it exists, is administered by the Exchanges.

A listing application must include a description of the nature, nominal value and class of security to be listed, numeration and form and period of amortization. Among the documents required are a notarized up-to-date copy of the company's constitution, by-laws, the annual reports, balance sheets, profit and loss statements. The current balance sheet is required to be certified by a Chartered Accountant. In addition, Article 28 gives the Stock Exchange's Board of Governors the power to require whatever other documents appear necessary to establish a sound basis for its decision on admitting the stock to official quotation and its suitability for free trading on the stock exchange. For securities of companies with previous issues admitted to quotation, Article 29 requires that a dossier of admission be brought up-to-date through an examination which includes its legal, financial and economic situation. Moreover, Article 32 permits the Board of Governors of the Exchange to establish

minimum conditions with respect to corporate capital, number of securities, number of shareholders in proportion to corporate capital and distribution of dividends and distributable profits.

Article 47 of the Stock Exchange Regulations requires all companies admitted to official quotation to submit to the Exchange an Annual Report and various financial statements certified by a Chartered Accountant. Additional information to better inform the public may be required under Article 44. If an issuer fails to comply with the obligations to provide information required under the regulations, the Exchanges and Board of Governors after notice to the Ministry of Finance may temporarily suspend or exclude from official quotation all the securities issued by the infringing party. Enforcement of these requirements is irregular, however, and, as a consequence they are often ignored.

(c) Company Reports to Shareholders

At present there is no requirement that shareholders receive annual or periodic reports and no control over the reports that are sent.

(d) The Role of Investment Companies

The growth and development of investment companies has resulted indirectly in improved disclosure on the part of many issuers. In the words of one financial analyst, "There has been a revolution in the securities market since the first mutual funds appeared." The investment companies' financial analysts talk in a technical way to corporations and have created greater interest in financial statements. The chief financial officer of a listed company which successfully issued new shares at a premium with the aid of investment companies stated that as a consequence of investment company interest in his company's shares "every year the annual report gets better."

2. The Independent Auditor

It is axiomatic that the primary responsibility for the adequacy and accuracy of financial information reported to the exchanges and to the government (in the case of investment companies) and disseminated among investors must rest on management. Nevertheless, an objective analysis and verification of that information by an independent third party will help to inspire public confidence in the information provided and tend to encourage public investment in the securities markets. The present method is far short of this. Independent verification of financial information is now attained through the election of ^{31/}two independent shareholders to audit a company's financial statements. Perhaps the "two shareholder system" was a practical approach when life and business were simpler and companies were smaller and owned by closely-knit groups, but it does not seem adequate to meet the need for independent verification of the financial statements of the large, complex corporations or of their widely dispersed groups of stockholders.

C. Developing the Primary Market and Encouraging its Use.

To a large extent, access to the Spanish securities markets is artificially restrained by a combination of factors which tend to encourage the businessman to seek capital for expansion through means other than the issuance of common stock.

I. The Corporate Income Tax

To the extent it is desired to avoid income taxes by the maintenance of separate books and records for tax reporting purposes, it may be more difficult to interest industrialists in the securities

^{31/} There is also a procedure for selection of a public accountant if 10 percent of the shareholders do not agree on the two shareholders. However, this is rarely used.

markets and compliance with applicable public disclosure requirements. This factor, particularly when combined with the natural reluctance of a businessman to publish information about his business, which may be necessary for investors but also helpful to his competitors, can make public financing an unattractive way to raise capital. Even assuming a businessman has nothing to hide, he will still weigh the impact of the tax structure in deciding whether or not to sell shares to the public. If, on the one hand, the company can borrow large sums from a bank or other private lender interest payments will be a deductible expense. On the other hand, if the company issues additional shares it will be taxed on profits before payment of dividends and stockholders also will be taxed on the dividends they receive.^{32/}

These are considerations which bear directly on the critical decision of whether or not to raise capital through the securities markets. If the immediate disadvantages outweigh the longer term benefits of selling shares to the public, then the markets will be deprived of stock, the public will lose what might be worthwhile investment opportunities and ultimately, to the extent that a broad-based securities market could provide an important basis for economic expansion, industrial development may be retarded. Consequently, fiscal policy strongly influences how the securities markets will develop and its effects upon the securities market should be taken into account in formulating overall tax and economic strategy.

2. Issuance of Shares at Par Value

Perhaps the most significant factor which may deter a businessman from raising capital through the securities markets is the practice of

^{32/} If listing involves conversion from a limited liability company to a corporation S.A. the transfer taxes and brokerage (notarization) fees involved will also be a factor which the businessman will consider.

issuing shares at par value with subscription rights to purchase additional shares at par. This is an inefficient and expensive method of raising capital which also contributes to the narrowness of the markets.

The most frequent explanation for the practice is that an issue at market (i.e., "con prima") simply would not sell. Shareholders find rights offerings attractive because the market value of the stock is usually considerably in excess of the subscription price. This means that rights may be sold at a good profit. Moreover, in contrast to dividends, that profit is not subject to taxation. The investing public has come to regard the issuance of rights as an indication of the issuer's strength and future prospects. They assume that issuers will have the earnings to sustain their dividends even with the new shares. In fact, because the investing public has come to expect and demand new issues at par and to look forward to the issuance of rights, listed companies come under pressure to expand their capitalization whether or not they need the additional capital.

This situation should be changed. Expansion of capitalization is a decision which should rest on its economic merits not on the basis of shareholder demands for rights at par value. Further, issuing new shares at par value instead of at market is poor financial policy. From the viewpoint of the company trying to raise capital it is wasteful and expensive. If the company's stock is selling at a premium in the market the shareholders, rather than the company, receive the premium.

Issuance of rights under this system contributes to the narrowness of the markets in two ways. First, it is so expensive that it may discourage businessmen from using the markets to raise capital. Second, and perhaps more important, because the large majority of shareholders hold on to their rights to preserve their interest in the company, it perpetuates

concentration of holdings.

Previous efforts to re-educate the public with respect to the problems involved in issuing shares at par value have not been very successful.^{33/} One reason for that lack of success may be that stocks are quoted in terms of percentages of par value rather than in pesetas^{34/} and dividends are reported without respect to shares issued. If stock prices were reported in pesetas, investors would have a clearer idea of how market values are affected when shares are issued at par. Similarly, if dividends and earnings were reported in per share terms, it would also help the public to understand what happens when shares are issued at par instead of at market value.

3. The Absence of Financial Intermediaries

Another impediment to raising capital through the securities markets has been the scarcity of underwriters and other financial intermediaries to assist in bringing securities to market. There is no category of financial institution in Spain whose principal activity and source of revenue is the distribution of securities to the public. This situation creates problems for everyone who is concerned with the securities business. If a privately held company wishes to raise capital or if a listed company wants to expand its capitalization there are very few places, other than the banks, where it can obtain professional know-how or financing. Owing to the absence of investment banking firms which have an interest in underwriting new companies and the necessary

^{33/} After allowing for the minimal increase in paid-in-capital, issues at par are like stock dividends. Unless there is an increase in the net worth of the company, they merely amount to the issuance of more shares.

^{34/} Article 148 of the Stock Exchange Regulations provides that in general, the prices of securities should be expressed in percentage terms, unless for given reasons the Boards of Government agree to indicate them in pesetas per security.

expertise and capital to perform this function, it can be particularly difficult for small companies to obtain financing by issuing their shares to public investors.

In the last few years, especially with the advent of the investment companies, some progress has been made in furnishing the kind of services necessary for bringing securities to the market. Because investment companies are obligated to invest 90% of their assets and possibilities for investment were limited, they have provided initiatives for the expansion of capital. They have persuaded a few important firms to issue new shares, in some cases at market value. To do this one or two investment companies, working with the issuer purchased rights and distributed them to other investment companies and then, for a short period, purchased stock to help maintain the market price. In a sense they served as underwriters. Much more remains to be done to develop a sound broad-based underwriting capability. What is needed are private investment bankers who devote at least a significant, if not all of their activity to financing, underwriting and distributing securities.

D. Conclusions and Recommendations

Improved and expanded disclosure should be the foundation of a broadened public participation in the securities markets. Publication and dissemination of more financial information about Spanish companies, coupled with public confidence that such information can be relied upon, could start a self-generating cycle. In this context, the issuance of shares at a premium could become more acceptable; company owners

and managers should begin to see the securities markets as a more practical means of raising capital than they are today, leading, in turn, to a greater demand for the services of intermediaries to help to bring securities to the market; and, as confidence that the markets can work rises, companies will have greater incentive to continually upgrade their disclosures which should help to broaden and strengthen the markets.

I. Disclosure

This cycle must start with the furnishing of investment information. The government is in the best position to develop the total effort to obtain and disseminate the financial information and other material needed.

(a) Tighter Enforcement of Existing Exchange Reporting Rules

(1) This is an area where self-regulation can be highly effective but only if the Exchange Rules, which already require the filing of annual reports, are rigorously enforced. Failure to file a required report within a prescribed period should result in an immediate audit or investigation by qualified exchange staff members or by qualified independent auditors and in meaningful sanctions, such as temporary suspension from trading or exclusion from official quotation.

^{35/} Article 48 of the Exchange Regulations provides for such steps.

In addition, stock exchange rules should be expanded to specify the circumstances when it would be necessary to file more current reports: for example, the loss of a substantial contract, the development of a significant new product, the sale of a substantial portion of the assets or a significant corporate merger or acquisition.

(2) To assure that an Exchange enforces its own rules the Ministry should have a staff sufficient to maintain close contact with the Exchange and to review exchange procedures and rules and exchange compliance with its own rules and those of the Ministry. In particular, the Ministry should assure itself that the Exchanges requires that issuers comply with Article 47 of the Stock Exchange Regulations which requires an Annual Report, balance sheet, profit and loss statement and the application of the results of each completed financial year to be filed within two months from the date of their approval and certified by a Chartered Accountant. The Ministry should also have at its disposal a range of sanctions applicable to the Exchanges to assure that they deal with violations of their rules.

(3) Even if the reports filed with an Exchange have been examined by independent outside auditors they should be reviewed for completeness by qualified members of the Exchange staff. If a report appears inadequate, the Exchange should make an appropriate inquiry with a view to determining whether the security should be suspended from trading or delisted.

(4) The Exchanges should take the lead in improving reporting requirements. There are many ways to accomplish this on a gradual basis. Stronger reporting requirements could be applied first to all companies over a certain size or to those with the largest numbers of stockholders. Initially, the largest companies or those with the largest numbers of stockholders might find it easier to comply with such requirements. Another approach would be to make the requirements applicable to all companies which listed after a certain date. Over a period of time as the markets for the stock of such reporting companies improve, reflecting the quality of information available, it should encourage other companies to list.

(b) A Comprehensive Reporting System

^{36/}(1) The Ministry should require listed or publicly-held companies to report to their shareholders as well as to the Ministry of Finance and the exchanges. Reports to the Ministry should be more comprehensive and more frequent than reports to shareholders. Reports to shareholders can be more basic, drawing upon certain key information required in government reports. Reports to shareholders should be made at least annually.

(2) The Ministry should spell-out disclosure and other requirements for registration of securities which would be a prerequisite to the public offer and sale of such securities. If an issuer fails to provide the disclosures specified in the manner required by the government none of its securities should be permitted to be offered to the public. The information already required to accompany an application for listing under Stock Exchange Regulations - annual reports, balance sheets, profit and loss accounts, and the application of the results of the

^{36/} Consideration should be given to subjecting unlisted companies with more than a specified number of shareholders - for example, 100 - to reporting requirements similar to those applicable to listed companies.

company for the past year - all as approved by the company and certified by a chartered accountant, provides the starting point for such disclosure.^{37/}

One approach which has worked successfully in the United States and other countries is the requirement that companies publish a prospectus when they issue new shares. Such a prospectus, which includes financial statements, is a comprehensive description of the company, its operations, properties, management as well as of the stock being issued.^{38/} It is reviewed by the staff of the SEC for completeness and conformity to disclosure requirements

37/ Article 47, Stock Exchange Regulations.

38/ Among other things, in the United States such a prospectus must include:

- (1) information about the distributor's compensation and the plan of distribution;
- (2) how the company plans to use the proceeds of the issue;
- (3) the capital structure of the company;
- (4) a summary of earnings for the company or for the company and its subsidiaries consolidated, or both as appropriate for each of the last five fiscal years or for the life of the company if less.
- (5) organization of companies and description of control by parent companies, if any;
- (6) the business done and intended to be done by the company and the general development of that business during the past five years;
- (7) the location and general character of the principal plants, mines and other materially important physical properties of the registrant and its subsidiaries including a description of any encumbrances on such property;
- (8) any material non-routine legal proceedings to which the company or any of its subsidiaries is a party;
- (9) if capital stock is being issued -- dividend rights, voting rights, liquidation rights, pre-emptive rights, conversion rights, redemption provisions, sinking fund provisions, liability to further calls or assessments; for long term debt and other securities similar detailed descriptions of investors rights are required;
- (10) descriptions of remuneration of directors and officers, of any options to purchase securities from the company or any of its subsidiaries and of the interests of management in any material transactions.

Companies must also file additional information with the SEC as part of their "registration statement" when they offer new shares to the public.

and is "cleared" by the SEC as to the adequacy of the disclosure.

However, the SEC does not pass upon the investment merits of securities.

(3) Consideration should be given to subjecting special types of issuers such as banks, financial conglomerates and multi-national issuers or their affiliates to special reporting requirements as circumstances require.

(4) All corporate issuers should be required to maintain books and records in a place where they are easily accessible to designated government or exchange inspectors for a designated period and in a specified manner. Consideration should also be given to requiring that shareholders who own a specified minimum amount of stock be permitted to review an issuer's books if Spanish law does not already provide for such rights.

(5) The feasibility of developing a program requiring the distribution of proxy materials should be explored further. The primary reason for a system of proxy solicitation is to provide for shareholder democracy. For this to be effective the materials which accompany the proxy should provide sufficient disclosure to permit shareholders to intelligently exercise their proxy rights. Moreover, the solicitation of proxies for an annual meeting provides an excellent means of channeling information to shareholders and to the investing public especially where there is widespread public ownership. Even for companies where ownership is highly concentrated, proxy solicitation materials can provide an effective method of broadening investor interest. Such materials could be filed with the Ministry and made available by it through its public files or the press and news media.

Requiring disclosure of transactions in proxy materials can also strengthen public confidence by protecting investors from abusive practices.

Disclosure, in and of itself, generally has a significant prophylactic effect. If management has a question about the fairness or wisdom of a transaction, it might decide to forego the transaction if it would have to be fully disclosed in its proxy statement.^{39/} Moreover, the proxy statement will provide investors with information with which to pursue any remedies if management completes the transaction.

(c) Inspection Program

It is imperative that the government have maximum flexibility to develop means to detect non-compliance and to impose effective sanctions on violators.^{40/}

(1) A regular inspection program may not be necessary for all types of issuers. However the Ministry of Finance should have the authority to move quickly when any issuer is delinquent in meeting reporting requirements or when information reported indicates a reason for action. This means having authority and capability to inspect an issuer's books and to require the immediate production of all relevant books and records from the issuer, its officers, directors and employees, as well as from others.

^{39/} Such a situation might include the sale of property to a corporation by an insider at a price substantially in excess of his cost shortly after acquiring the property or the diversion of a corporate opportunity to an insider.

^{40/} The inspection program which accompanied the development of investment companies sets a pattern for the kind of disclosure and investor protection which can be obtained through a vigorous regulatory program. Under this program the fund and the Ministry each name an accountant to inspect the investment company. All of the fund's documentation is placed at the inspectors' disposal. They must verify fund transactions and confirm its accounts. Accountants are chosen from a preferred list and are paid by the investment company. Violations discovered by the inspectors may be met with serious consequences, fines of between 10,000 and 1 million pesetas and removal of board members. For serious violations, a fund may lose its tax benefits, i.e., freedom from capital gains taxes.

(2) The Ministry or its designated inspectors should be able to take testimony from officers, directors and employees of issuers as well as from any others (including financial institutions) which have information relevant to its inquiry.

(3) The officers and directors of companies required to file documents with the government and the exchanges, and even the lawyers and accountants who prepare or examine such documents, should have sufficient resources to satisfy any liabilities to investors resulting from non-compliance with any registration or reporting requirements adopted. One means of accomplishing this would be for the Ministry to have authority to require that such persons be bonded and to set bond limits.

(4) Sanctions for serious violations should include fines and consideration might be given to providing a means whereby non-complying officers and directors could be removed from office. As an ultimate sanction, the securities of non-complying issuers could either be removed from the Mercantile Register or withdrawn from quotation for a specified period.

(d) Information Disclosed to Banks

Companies which seek loans from banks are required by them to disclose comprehensive financial and other information. In some cases, before making a loan the bank will send two or three of its people to the company to review its operations. The relationship between the company and the bank has been regarded as confidential, at least in the sense that information disclosed is not available outside the bank.

However, such information circulates freely within the bank. The chief of the New Issues and Investment Advice Department of one of Spain's largest banks indicated that his department receives and exchanges information with other departments of the bank - credit, foreign, economic. The reports he receives include production, sales, balance sheet, profits and cash flow. Thus, a wide variety of confidential information is at the disposal of the bank's advisory department. After being analyzed and digested it may be sold to private clients in the form of investment advice or used to attract clients to the bank. To this extent, such information may already pass into the public domain. But, because the banks dominate the securities markets, the opportunity for special advantage prior to such dissemination is great. Serious consideration should be given to how to deal with this situation - either by limiting the use of such information within the banks or by requiring the banks or the companies to which they make loans to file with the Ministry of Finance certain of the basic financial reports of the company, including Balance Sheets and Statements of Profits and Losses, on which such loans are based, and any modification and corrections made by the bank.

(e) Disclosure of Portfolio Holdings

In a heavily institutionalized market where a few, large institutions such as banks and investment companies either hold or have investment discretion or investment decision-making power over a large portion of the outstanding stock of a listed company, information about holdings and transactions of such institutions may be as important as information about the companies. With broader public participation the situation may change but the fact now is that a few institutions can dominate the market in a particular stock. This information might be an important consideration for an investor and this is an area which may require further study. Perhaps institutions should be required to disclose their holdings and transactions of portfolio stocks and stocks of clients over which they exercise investment management authority. Another alternative might be to eventually limit the amount of shares of a particular company that an institution can own or exercise management authority over or, perhaps even limit the transactions in a security that an institution can place at a particular market session or over a specified time period.

2. Dissemination of Information

Reporting to the Ministry of Finance does not complete the disclosure process. Information should be disseminated to the public through a combination of Ministry action and requirements placed upon issuers and securities market professionals.

(a) Prospectus Distribution

Any consideration of a program which would require all issuers of securities to publish prospectuses describing the security and summarizing the company's operations should also consider the

requirement that such prospectuses be distributed to purchasers of such securities when they are originally issued. For example, in the United States such a prospectus would be required to be distributed to purchasers of subscription rights prior to consummation of the transactions.

(b) Dissemination of Information Collected by the Ministry of Finance

Public knowledge that the Ministry is developing a comprehensive program for strengthening the securities markets and protecting investors should stimulate public confidence - itself an important prerequisite for broad-based public investor participation in the markets. Such knowledge could be disseminated by the distribution of information and the publication of articles and news stories about the efforts of the Ministry to strengthen the capital markets. Similarly, publication of a daily calendar of corporate reports filed and regular distribution of information about any action taken by the Ministry whether routine or unusual - should also help to build investor confidence by emphasizing the Ministry's interest in the securities markets. Continual publication of summaries and reports both by the Ministry and the exchanges will also help to stimulate interest and confidence.

The Ministry might consider maintaining regional offices for internal financing in Barcelona and Balbao or smaller branch offices in other commercial centers in addition to its offices in Madrid. These offices could assist in inspections and investigations and make available financial reports and other current information filed by issuers and exchanges. An expanded regional presence should tend to stimulate interest among investors throughout the country.

3. Development of the Accounting Profession

An integral part of any disclosure system is a means of assuring that financial information is dependable, that the data is presented fairly in accordance with generally accepted accounting standards. This can be achieved by requiring that an independent public accountant express his opinion, based upon an examination of the financial statements in accordance with generally accepted auditing standards, that the financial statements present fairly the financial position and results of operations in conformity with generally accepted accounting principles applied on a consistent basis. The independence of the auditor is designed to assure the detached objectivity and skill of a knowledgeable professional not connected with ^{41/}management.

- ^{41/} The question of the independence of an auditor will always be one of fact to be determined in the light of all pertinent circumstances in a given case. The Ministry may wish to reserve to itself the role of final arbiter in determining independence in a particular situation. However, the minimal guidelines for what constitutes independence could be set by the Ministry in cooperation with the accounting profession, the exchanges and other interested parties. Among the factors it may wish to take into account in any guidelines in this area are:
- (1) Absence of managerial responsibility. The accountant should not become, or appear to become so identified with the client's management to be indistinguishable from it.
 - (2) An accountant cannot objectively audit books and records which he has maintained for a client. He should not be placed in the position of evaluating and attesting to his own record-keeping.
 - (3) The accountant should not have any direct or indirect financial interest in a client. This would include the situation where fees for an audit or other professional service remain unpaid over an extended period of time and become material in relation to the current audit fee.
 - (4) Family relationships: Where the family relationship existing between an accountant or member of his firm and the client is such that, because of the strong bond which is customary among family members, an outside party could reasonably question the accountant's impartial examination he may not be considered independent.
 - (5) Occupations with conflicting interests. Certain concurrent occupations of the auditor involve relationships with clients which jeopardize the auditors' objectivity. These would include acting as counsel for or actively engaging in direct competition with the client in a commercial enterprise.

Spain has made a start toward reporting and independent auditing requirements in its regulation of investment companies and mutual funds. However, this is only a beginning. There is a need for many more qualified accountants and auditors in the country. They must develop the experience, background and even the size to complete a sophisticated audit of a large industrial enterprise. Further a uniform auditing system, generally accepted accounting principles and uniform industry reporting requirements do not yet exist in Spain. Nor is there a requirement for immediate disclosure of material changes in a company's business.

Fortunately, the need for accounting standards has been recognized and a General Accounting Plan has been developed by the "Commission Central de Planificacion Contable" and approved by the government. The development of the accounting profession and continual upgrading of accounting standards should receive a high priority. It is an essential part of the program to promote disclosure and strengthen the markets.

(a) Detailed recommendations for uniform industry reporting requirements and a uniform auditing standards are beyond the scope of this document, but work on them should proceed directly, perhaps in cooperation with professional societies and other interested parties. One helpful reference for such a project would be the SEC's Regulation S-X. This is a series of rules promulgated the SEC which state the requirements applicable to the form and content of financial statements required to be filed with the SEC under the U. S. securities laws.

(b) The government should have the authority to impose sanctions against accountants and other professionals who fail to meet standards provided. Such sanctions could range from citations and fines to barring violators from practice before the government or from examining any documents to be filed with the government.

(c) More independent accountants will be needed in order to provide the auditing capability and dependable information the securities markets require. To encourage the development of the accounting profession and other professions necessary to the operation of the securities markets the government should foster educational programs and curriculum changes in the universities in order to specifically cover the securities markets, corporate laws, finance and auditing. Students should be encouraged to follow such a program with the potential for responsible and well-paying positions in public accounting firms, other parts of the private sector and in the government and at the Exchanges.

4. Financial Advisory Services

Clearly, one goal of the regulatory program should be to broaden the sources of investment information by promoting and developing a system which produces a constant stream of information which can be digested and analyzed by a variety of qualified professionals. This information should be relayed to the public through many channels in a relatively simple comprehensive form.

As more financial and other information about companies becomes available it will become feasible to achieve this goal. Individuals could be encouraged to organize private investment counseling and advisory services, to publish market letters and financial analyses. In addition, brokers, if permitted to associate, would have the capacity to provide such services or could be required to provide them. Exchanges could be required to publish summaries of data from their files, and financial publications, the press, other news media and economists could be encouraged to publish news of financial developments and even some financial analyses. To the fullest extent, dissemination of information and analyses should be encouraged.

At the same time it might also be well to explore the feasibility of establishing minimum qualification standards for those who would act in this capacity. Brokers are already subject to rigorous tests. Others who wish to provide advisory services might be subject to licensing based upon professional training and examinations or encouraged to develop their own professional codes of conduct.

5. Fiscal Considerations

Application of the tax laws can strongly influence the decision of whether or not to list a company's stock and thus directly affect the development of the securities markets. For this reason, implications for the securities markets should be taken into account in developing fiscal policy. However, we realize that these must be weighed against competing social and economic considerations. This area is beyond the scope of this report and no recommendations on the kind of fiscal program necessary to aid

in the development of the securities market are offered. We merely point out that the options available to create positive incentives or eliminate inhibitions to listing include:

1. Lowering corporate taxes for listed companies;
2. Lowering or eliminating taxes on dividends for listed companies;
3. Reducing transfer taxes in connection with new listings;
4. Instituting tax forgiveness for newly listed companies;
5. Increasing enforcement of the tax laws to assure that the desire

to avoid taxes does not influence the decision whether or not to sell shares to the public. To the extent that this could be accomplished it would make the choice between expanding operations privately or through the securities markets hinge upon the economic merits of each type of financing rather than on the extraneous factor of maintaining secret operations.

6. Discouraging Issuance of Shares at Par Value

Serious consideration should also be given to changing the existing system of subscription rights. Although the premium which investors receive on the disposition of subscription rights - and the tax treatment of the gain derived from sale of rights - constitute a principal incentive for investment in securities, the existing system is extremely disadvantageous to publicly held companies.

The issuance of shares at par value is an expensive way to raise capital through the securities markets. Whenever a company issues additional securities, any premium in the market price of the securities over their par value accrues to the benefit of the investors rather than to the issuing company. This system also contributes to the narrowness of the markets because it perpetuates the concentration of holdings. Because the underlying purpose of developing the capital

^{42/} Brazil has recently developed a comprehensive system of fiscal incentives which may be of interest in this respect. See David M. Trubek; Law, Planning and the Development of the Brazilian Capital Markets, NYU Graduate School of Business Administration Bulletin, April, 1971.

markets in the first place is to facilitate the channeling of funds to companies which require financing, it seems important this system be re-examined in the light of the present policy of the Ministry of Finance to further the development of the capital markets.

There are a number of ways to discourage or to end this practice.

1. The quickest way would be to tax shareholders on all or a portion of the amount of any premiums involved. Such taxes could be imposed either on the sale of the rights or upon their conversion into stock at par value.

2. Another way would be to attempt to reeducate the public. Such a reeducational effort would be substantially aided if stock values were required to be shown in all official exchange publications in terms of pesetas rather than as percentage of par value.^{43/} At present the continuous focus on the relationship of prices to par value gives an undue emphasis to this basically meaningless figure and distorts the real value - the amount of pesetas which will be paid or received when a share is bought or sold. If share values were shown in terms of pesetas and dividends were shown in pesetas per share, the public would have a clearer idea of the effects of issuing shares at par instead and at market value. Here is another area where changes could be made gradually. First, by publishing quotes simultaneously in percentages and pesetas and then by dropping the percentages.

^{43/} Cf. Article 148 of the Stock Exchange Regulations which, as a general matter, requires securities prices to be expressed in percentage terms, unless for given reasons the Boards of Governors agrees to indicate them in pesetas per security. If this regulation prevents expression of prices in pesetas consideration should be given to amending it.

3. A third possibility could be to require an increasing percentage of the premium to be included as part of the offering price over a period of time.

7. Financial Intermediaries

Financial intermediaries - underwriters, private investment bankers, skilled professional analysts - are needed to provide the financial assistance and technical acumen required to distribute shares to the public. Banks already provide some of these services, and mutual funds, in an indirect way, have helped to bring some companies to the market. A few independent consultants and advisory firms are now beginning to provide these services. But the need for them will increase sharply as disclosure and regulatory requirements are strengthened and the markets become more active and attractive. If and when brokers are permitted to associate they can be expected to enter this field if stock exchange rules are amended to allow them to do so. Further encouragement to become underwriters could be provided through direct fiscal incentives such as advantageous tax treatment of underwriting profits and reduced transaction taxes in connection with original issues and stabilizing transactions.

8. The Regulatory Capability of the Ministry of Finance

The development of a viable program designed to improve the functioning of the securities markets and a broadened public participation depends to a large degree upon the assumption of significant self-regulatory responsibility by the Exchanges and voluntary activity

by issuers, banks, brokers, and professionals. Nevertheless, the Ministry of Finance must be the galvanizing force behind reform and improvement. Its role will be to develop an appropriate regulatory framework and also to prod others into necessary action. To meet this responsibility, it is imperative that the Ministry be provided with an adequate staff.

Although the Ministry is able to draw upon the services of accountants and lawyers in addition to its staff clearly its relatively small staff must be significantly expanded if it is to keep abreast of the growth of the securities markets much less meet the challenge of a program such as that outlined in this report.

As is recommended in Part III, above, a large part of our program may be accomplished by the exchanges themselves through an expanded program of self-regulation. However, to be fully effective, self-regulation depends upon an outside authority, the government, assuring that the exchanges enforce their own rules and upon the government ultimately being able to change those rules after consultation with the exchange if it feels that improvements are necessary. With the recent establishment of a unit in the Office of Financial Policy to inspect the exchanges and investment companies, a start has already been made in this direction.



PART V

GENERAL OBSERVATIONS.

A. Development of a Central Market

In Part III it is suggested that the volume of trading at the present time does not appear to justify the substantial costs involved in developing a central market system. Such a system might bring only marginal benefits within the foreseeable future. Nevertheless, assuming a significant growth in the securities markets, a centralized system should be an important long-term goal for Spain both because of the efficiencies it could mean and because of the depth and liquidity it could add to the market. Steps should be taken now to plan for this goal before listings increase and any great expansion of trading volume occurs. Inauguration of such a program while market development is still at a fairly early stage would involve much less dislocation and would place the markets in a better position ultimately to unite. Therefore, particular attention should be paid to those recommendations in this report which would tend to integrate the markets.

One of the principal recommendations contained in Part III is that serious consideration should be given to permitting brokers to associate with others to form brokerage firms. The implications for the development of a unified central market of permitting brokers from different exchanges to associate with each other could be immense. Efficiency and competition could lead such combined brokerage firms to introduce modern communications networks and other electronic technology to link their offices in various cities and to provide improved customer facilities as indicated

previously.^{44/} Support for greater consolidation of the exchanges could be expected to increase as brokers from different exchanges unify their operations.

Another intermediate step which might help to knit the exchanges together would be to provide greater opportunities and incentives for the corredores to bring their customer's trades to the exchanges. One way to accomplish this would be for the corredores to follow the example of the banks and put operators on the floors of the exchanges who would represent their interests. Instead of being atomized as they are at present, this step would give the corredores greater market leverage. With their orders consolidated, they might achieve better executions. Theoretically, at least, this could make them more competitive and enable them to attract more customers.

At present, the corredores are reluctant to use the exchanges. If they do, they must share the brokerage commission with an exchange member.

^{44/} It should improve clearing and back office services, lead to brokers providing advisory and underwriting services and a specialist system which, through the use of the broker's own capital, could contribute significantly to the stability and orderliness of the markets.

In addition, using the exchange now tends to weaken their relationship with their customers because it is the exchange members who issue the poliza. If exchange commission rates were raised and corredores were entitled to receive a larger percentage of such enlarged commissions, perhaps they would have greater incentives to bring their customers' transactions to the exchange and this would stimulate greater regional participation in them. An alternative to this recommendation would be for the corredores to establish correspondent relationships with exchange brokerage firms under which they would be assured of receiving a larger portion of the fee on customer trades referred to that firm by them. This would give corredores a greater identity of interest with the brokers and make it economically attractive for them to channel orders to the exchange.

A further step toward the integration of the markets would be to permit the corredores to become members of the same brokerage firms as the exchange brokers. In a sense, this could flow naturally from permitting brokers to associate and raising incentives to build up exchange business since, as a competitive matter, it may be expected that some firms will consider opening regional offices in the smaller cities.

Action taken with respect to the principal recommendation in Part II, that a committee study the feasibility of immobilizing the certificate in a central depository should have strong bearing on other steps for consolidation of market operations. If certificates are immobilized in a central depository only one clearing house system will be necessary.

Part II recommends that studies be made of consolidating clearing houses into one system and exchange processing operations into another. Savings from the elimination of duplication should be considerable. However, meaningful savings should be attainable even without consolidation of exchanges. Neither a single electronic data processing operation for the clearing houses nor a consolidated data processing operation in one location requires the exchanges to consolidate.

As to consolidation, it should be noted that integration and consolidation of the markets need not result in abandonment of major exchange facilities. A single market can exist with two trading floors if an instantaneous communications system is set up.^{45/} Because of the expense involved in creating such a system it is not recommended at this time. This matter should be the subject of further study by exchange and government officials and perhaps by others such as banks, investment companies and major issuers who have a stake in the efficiency of the markets.

B. Implications of Bank Power

In a healthy regulatory environment responsibility accompanies power. In the Spanish securities markets, however, the banks exert great power without concomitant responsibility. They are not held accountable for the effects of their activities on the securities markets generally and the exchanges in particular. This report suggests a number of steps for dealing with this anomaly. Banks would play

^{45/} In the United States the Pacific Coast Stock Exchange consists of two facilities, one in Los Angeles and the other in San Francisco, 500 miles away.

a leading role in the creation and operation of a central depository, but that depository should be subject to direct governmental regulation by the department responsible for market operations and thus the depository would be directly accountable for delays in liquidations or other malfunctions.

With regard to bank powers over the exchanges, two approaches were considered. On the one hand, as suggested in Part III, banks could be brought into the exchanges as owners of brokerage firms and made directly responsible under exchange rules. On the other hand, banks could be precluded from association with brokerage firms and exchange membership. The report recommended placing responsibility on the banks because of the enormous financial resources they would bring to the exchange and because realistically it seems impossible, regardless of all the regulatory efforts that might be devised, to significantly curtail the banks' tremendous power and influence over the markets. However, in theory, it might be preferable to limit the banks' influence.

It is imperative, in any event, if bank ownership of brokerage firms is permitted, that steps be taken to diminish conflicts of interest under the present system, to build up incentives for other brokers to concentrate on exchange related activities and to increase the number of such brokers who derive their principal income from market activities. The objective of such a program would be to reduce the dependency of the markets and the brokers on the banks.

Even if it is determined that banks should not be permitted to own brokerage firms, certain of their market related activities should be subject to direct regulation. At a minimum banks should be required to keep records of their own securities business and transactions. The records should include the date any order is received by a bank and should indicate the type of instructions given with respect to execution (e.g., whether a limit price was included or whether execution was to be at market). The government should have the right to inspect those records and should do so regularly. Sanctions should be spelled out to assure compliance with the record keeping requirements and to prevent rationing and interpositioning by the bank at a price which is less advantageous to its customers.

Transactions by bank affiliates in the stock of the bank should be reported to the government and reviewed to prevent manipulation. Consideration should also be given to requiring banks to report transactions in stocks in which the orders placed by a particular bank and its affiliates account for a stated percentage of trading. The government should have regulatory power to assure that such banks and their affiliates or any broker or other person trading for his own account as a professional in the markets does so in a way that contributes to the orderliness of the markets. Such regulatory power should include the authority to prevent trading on the exchange floor by such persons for their own accounts or for discretionary accounts as may be appropriate in the public interest and for the protection of investors. The government should also have the authority to restrict dealings so far as practicable, to those necessary to permit such persons to maintain a fair and orderly market.

While it is true that banks occupy sensitive positions in the securities markets, their resources and expertise also provide a great potential for meeting the needs of those markets. The contribution of their abilities and strengths could be an integral part of the success of any program for the improvement of the securities markets. This undertaking will require the cooperation not only of the banks, but of the exchanges and brokers and all of the companies whose stocks are traded as well. The problems of securities markets do not lend themselves to quick solutions. Hopefully, however, this report will help to set the direction with which a firm start can be made.

APPENDIX A

Tentative Summary of the Main Problems
in the Spanish Securities Markets

Prepared by

José Vilarasau
Director General of Financial
Policy
Ministry of Finance



*El Director General
de
Política Financiera*

A-1

Madrid, October, 19, 1972.

Mr. Allan S. Mostoff,
Associate Director
Securities and Exchange Commission,
WASHINGTON, D.C. 20549

Dear Mr. Mostoff,

I am sending you a note on the problems that I think your analysis should cover. Obviously, this is only a tentative list to be completed during the preliminary contacts of our - teams.

Enclosed you will find also a leaflet describing the main features of the Spanish securities market.

Sincerely,

José Vilarasau Salat.

MAIN PROBLEMS IN SPANISH SECURITIES MARKET

1. Settlement of transactions

It is the more urgent technical problem to solve in the Spanish market.

In the Madrid Stock Exchange, in ten years, the nominal volume of transactions has been multiplied by four and the admissions to official quotation have been **quintupled**. The securities nominal value has remained practically invariable.

In spite of measures taken by companies and Stock Exchanges to reduce it (multiple bonds, settlement services, etc.), the problem remains and the final solution has been postponed.

The problem becomes greater because of two facts:

- The obligatory intervention of a public agent in any securities transaction, meaning in practice that all kinds of securities are registered bonds.
- The transactions in banks securities represent in Madrid stock exchange approximately a 50 per 100 of total transactions, and this kind of securities are all registered, in accordance to legal precept.

2. A narrow market

In Madrid Stock Exchange the nominal value of transactions represents the following percentages upon the nominal value of securities admitted to official quotation:

Public bonds	1,8 per 100
Private bonds	2,2 per 100
Shares	2,1 per 100
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Total	2,1 per 100

In other Stocks Exchanges, these percentages are substantially lower.

It must be said that there is not a real market in private bonds because almost all issues are qualified to be acquired by institutional investors (savings banks, Social Security institutions, etc.) forced to buy them in order to cover officially imposed reserves and coefficients. Most of the transactions actually made are due to portfolio adjustments of these institutions, or to dealings in unqualified bonds.

About shares, in Madrid Stock Exchange, approximately a 10 per 100 of companies whose shares are quoted represent three-quarters of the total shares transactions. On the other hand, there are several important companies whose shares are not quoted in the Stock Exchange.

Institutional investors own nearly a 15 per 100 of quoted shares and a 25,2 per 100 of shares and private bonds issued. They hold also an 89,5 per 100 of public bonds.

The relatively scarce volume of operations in the Stock Exchange is probably due mainly to the nature of the securities investment in Spain. However, it would be interesting to investigate if there are other institutional problems such as legal or customary checks to the portfolio adjustment of institutional investors,

excessive cost of the transactions, fiscal inducements to delay the sale of securities, etc., which aggravate the situation.

A problem related to the narrowness of the market is the difficulty in defining a quotation which is not too erratic and, on the other hand, does not depend on the dealers' or financial authorities' personal criteria. So, a further field of inquiry should be the market procedures to fix quotations, the convenience or not of dealing through four regular markets (Madrid, Barcelona, Valencia, Bilbao) and a number of authorized dealers operating out of them, the possibility of pooling in the market most of the over-the-counter transactions, etc.

3. Centralization and decentralization of markets

A major problem due to the multiplication of markets is the different regulations of securities transactions in each market. Securities officially quoted in a Stock Exchange can be unofficially dealt in other stock exchange, without observing the established rules about making or changing quotation prices (minimum volume of operations to change it, maximum day-to-day changes and so on).

4. Nature and functions of the securities market dealers

Both the Stock Exchange brokers and the licensed dealers not working in a place with Stock Exchange perform a number of different functions in the mercantile trade, being most in the nature of a public notary than an investment adviser or market intermediary. It is felt that the diversity of their functions, coupled with some legal limitations to their securities business, has somewhat distracted them of the organization and improvement of the securities market; the existing vacuum with regard to securities advice and management is being filled by the commercial

banks and several private entities (dependent or not of the banks), both of which are not subject to any kind of control in this respect. However, the Stock Exchanges themselves are totally managed and controlled by the licensed brokers.

It would be interesting to have an evaluation of the actual performance of the dealers, the possibilities to improve it in order to activate the securities market, and the convenience of extending the basis of the directory of the Stock Exchange, reflecting the transformations operated by the market and the role played by the institutional investors and the business community.

APPENDIX B

Persons Interviewed

(A Partial List)

Ministry of Finance

Sr. Juan Rovira Tarazona	Undersecretary of Finance
Sr. José Vilarasau	General Director Financial Policy
Sr. Antonio Rua	Assistant Director
Sr. Raimundo Foveda	Chief of Research Department
Sr. Joaquín Pulido	Chief of Stock Exchanges Division
Sr. Dionisio Martínez	Fiscal Law Specialist

Madrid Stock Exchange

Sr. Pedro Rodríguez Ponga	President
Sr. Antonio Sanz de Bremond	Vice President
Sr. Jaime Aguilar	Broker
Sr. Adolfo Fries	Broker
Sr. Javier Oyarzabel	Broker and Dealings Manager
Sr. Manuel De La Concha	Broker and Clearing Manager

Bank of Spain

Sr. Angel Rojo	General Director Research Department
Sr. Martínez Mendez	
Sr. Antonio Sanchez Pedreiraño	

Bank Urquijo

Sr. Francisco Ruiz Jarabo	Vice Director, Chief Securities Division
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Bank of Bilbao

Sr. Jose Manuel Meñoz Cortés	Subdirector
Sr. Joaquin Cayuela Verges	
Sr. Jose Luis Eadiola Vigo	
Sr. Fermin Lacanda	

Banco Español de Crédito

Sr. Jorge Brosa Palau	Director General
Sr. Felix Muelas Medrano	Director of Foreign Department
Sr. José Antonio Suárez F.-Equia	Director General
Sr. Julian Tiemblo	Associate General Manager
Sr. Fernando Montesino de Sobrino	Director for International Financial Relations

Hispanibec, S.A. - Crecinco

Sr. Joaquin del Castillo Montalvo	Member of the Board
Sr. Alejandro Uriarte Picó	Director Of Investments
Sr. Jorge Camio	General Manager
Sr. Castillo Serfige	

Spanish Federation of Savings Banks (Ahorrofond)

Sr. Marcelino Poo	General Vice Director
Sr. Eusebio Morales	Financial Analyst

University of Madrid

Sr. José Maria de la Cuesta	Professor of Commercial Law
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Banif, S.A.

Sr. Juan Antonio Ruiz de Alda	Member of the Board
Sr. Carlos de la Cruz	Managing Director

Compañía Telefónica

Sr. Luis Garcia Velarde	Financial Manager
Sr. Fernando Asin	

Gestinbao-Gesbancaya

Sr. Eduardo de Aguirre Alonso-Allende	Financial Director
Sr. Félix Herrero Suazo	Secretary General
Sr. Alvaro G. de la Rasilla y Pineda	Subdirector
Sr. Dupla	

Corredores de Comercio

Sr. Joaquín Maldonado Almenar	President
Sr. Avelino Moya Torres	Vice President
Sr. Ernesto Machin Sanchez	Corredor

Asland Cement Co.

Sr. Joaquín Zuerras Abizanda	Director of Finance
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Catalun Gas & Electric Company S.A.

Sr. José Cervera Bardera	Director General
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Cataluna - Occidente Insurance Corp.

Sr. Jesus Serra	General Manager
Sr. Javier Villavecchia de Delás	Director General

Bank Mas Sardá

Sr. José Maria Mas-Sardá Sells	President
Sr. Juan Sallent Rosich	Director Securities Dept.

Inversiones Mobiliarias de Cajas de Ahorros

Sr. Enrique Casany Cortada	Director General
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Industrial Bank of Cataluna

Sr. Enrique Bonmati	Director of Public Relations
Sr. Amadeu Juan Gomez Borsa	
Sr. Constantino Gomez Tuarez	

Gesfondo S.A.

Sr. Ramon Trias Fargas	Member of Board
Sr. Jorge Petit Fontseré	Director General
Sr. Ramon DeOlano Moliner	Subdirector of Investments
Sr. Jesús Lladó F-Urrutia	Counsel

Barcelona Stock Exchange

Sr. Javier Garçon	President
Sr. Javier Ribó Ruís	Broker
Sr. Francisco Fernandez Flores	Broker
Sra. M ^a Angeles Vallve Ribera	Broker
Sr. Jorge Planasdemunt	Secretary General

Tobanca

Sr. Maximo Fernandez	Counselor
Sr. Carlos Grau Petit	Director

Saeco

Sr. Saturnino Anfosó Borrell	Director General
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Motor Ibérica

Sr. Blanco