

**RETAIL BANKING SECTOR INQUIRY
PRELIMINARY REPORT II
CONSULTATION FEEDBACK FORM**

Name of company:

Caixa d'Estalvis i de Pensions de Barcelona (hereinafter "la Caixa")

1. INTRODUCTION AND STRUCTURE OF THE RESPONSES

Caixa d'Estalvis i de Pensions de Barcelona (hereinafter, "la Caixa") welcomes the opportunity to submit its comments on the issues submitted for consultation by the European Commission in its *Interim Report II Current Accounts and Related Services* (hereinafter, the "Interim Report") under a sector inquiry on retail banking initiated by the European Commission under Article 17 of Regulation 1/2003.

"la Caixa" is the third largest financial entity and the leading savings bank in Spain. It provides all types of banking services (universal bank) to both households and small and medium enterprises. "la Caixa"'s offer is multi-channel, combining a major network of branches with other channels, such as Internet, ATM or telephone. "la Caixa" had 5,053 branches at the end of 2005, the most extensive network in the Spanish financial system. Its workforce now numbers 25,254 employees, 11,768 more than ten years ago, making "la Caixa" one of the biggest job creators in Spain. 2005 saw the celebration of the installation of automatic teller number 7,000 and, at the end of 2005, the network of self-service terminals included 7,208 machines. In addition, the Internet channel through *Línea Abierta* (www.laCaixa.es) is the leading service in the on-line banking market, with 3.7 million registered customers, 1.6 million of which are active users (up 26%), who conducted 641 million transactions in 2005, a 59% increase¹. In 2005, the number of customers totaled 9.6 million, 452,100 more than in 2004².

"la Caixa"'s responses to the questions submitted to consultation have been structured in the following manner: Section 2 contains some preliminary and general comments on the Interim Report. Section 3 deals specifically with the Spanish market for retail banking services, with express references to the questions submitted to public consultation. Section 4 contains information relating to credit registries and payment systems also with express references to the questions submitted to public consultation. Finally, Section 5 contains the conclusions drawn by "la Caixa" on the different legal and economic questions raised.

2. PRELIMINARY COMMENTS ON THE COMMISSION'S INTERIM REPORT

2.1. Statistical considerations of the Commission Interim Report

"la Caixa" believes that the statistical considerations contained in the Interim Report are appropriate for an initial study of the market. Nevertheless, we are of the opinion that if conclusions are going to be based on such statistical considerations, the same must be further refined. The reasons are the following:

Firstly, the **data base** used has serious homogeneity problems –not only among countries, but also among banking entities within a given country. This makes it more difficult to compare data. The methodology used, based on surveys with a certain

¹ The figures related to on-line banking almost double the second internet bank in Spain (ING Direct).

² For further information, see

<http://www.lacaixa.comunicacions.com/se/igia.php?idioma=eng&any=2005>

leeway in setting the parameters – such as the way the relevant retail banking market is defined or how certain commissions are computed for products – may give way to erroneous interpretations or associations of data.

Secondly, the **indicators that were constructed** and later used to make econometric analyses may not be adequate to achieve the desired results. The following are some examples of the problems they suffer:

- (i) The measure of **efficiency** used (cost-to income ratio) is basically an indicator of profitability which includes price effects: given that gross income is influenced by the interest rate level the ratio pick up effects other than efficiency in costs. The economic literature provides various approaches which have attempted to overcome this problem (such as the estimation of cost functions or the use of non-parametric methods).
- (ii) The **mobility** indicator, based on the overall mobility of current accounts (openings + closings), does not always reflect the switch from one entity to another, since closing one account does not necessarily imply that another account is opened in another banking entity. This is especially true in countries in which every customer has more than one current account. Similarly, it is of note that in certain countries, such as Spain, there is a high ratio of bank accounts abandoned due to the fact that the abandonment of bank accounts is not penalized.
- (iii) The degree of cross-selling is measured as the total number of products owned by a customer in a given entity. Thus, the magnitude of the indicator depends both on the active policies of the entities and on the different financial needs of the consumer (reflecting as well the country's degree of financial development).

Finally, the **statistical analysis** provided has some weaknesses because it is based on econometric relationships which only take into account univariate regressions and simple correlations.

As an example, Page 80 of the Interim Report presents two univariate regressions, in an attempt to identify the determinants for profitability. Market share is the only variable used to explain profits and the efficiency ratio respectively. Even though the only significant coefficient is that for the first regression (market share-profit), the Interim Report concludes: *“The relative size of a bank, measured by market share, has a statistically significant relationship with profit. Market share also has a negative but non-statistically significant relationship with the cost-income ratio. This could support the hypothesis that banks with larger market shares, although not necessarily more efficient, were able to obtain larger profits by exerting market power.”* The conclusion, despite being qualified later by the Commission, is entirely questionable on the basis of the analysis made. The estimated indicators are biased: the regression suffers from the omission of relevant variables, so that the coefficient of the market share variable may be picking up the effect that other variables, such as the efficiency level, have on profit. An analysis of the determinants for profitability would require an adequate comparison of the efficiency hypothesis (redefining, as has been said, the way in which this variable has been measured and econometrically

estimating a system of behavior equations that properly models the competition between entities).

To conclude, “la Caixa” is of the opinion that the statistical considerations included in the Interim Report are appropriate for an initial study of the retail banking market but that if any conclusions are going to be based on such statistical data, then such data must be further refined.

2.2. Market fragmentation within the EU retail banking market.

The European Commission, in view of the importance of the retail banking sector, has decided to carry out an investigation with the purpose of determining whether or not certain practices require antitrust action. The fact that the characteristics of this particular sector vary from country to country is considered by the Commission a hint that anticompetitive practices might be taking place.

In “la Caixa”’s opinion, the reasons for market fragmentation in Europe’s retail banking sector are mainly legislative, structural, or even cultural in nature:

(i) Legislative reasons. From a legislative point of view, it is noteworthy that there are still certain differences amongst the different Member States. These include the fact that legislation concerning the following matters may vary from country to country: (i) taxation of different savings products, (ii) consumer protection and transparency, (iii) permits and authorizations required by financial entities to carry out certain activities (e.g., insurance activities), and (iv) remuneration of certain products and/or services.

In each particular case, taking into consideration the requirements of demand and the very specific nature of each service or product, the legislator of each Member State has provided each particular product or service with a specific legal framework. Furthermore, the laws generally establish the different legal frameworks bearing in mind the welfare of retail banking consumers. Thus, it cannot be denied that regional and national legislations may vary substantially among the different Member States³.

The fact that such differences amongst Member States are due to the characteristics of demand for such products and services has even been confirmed by the Spanish Competition Authority and the European Commission in cases relating to this particular market, in which the relevant geographic market has been defined as being national or even regional due to the characteristics of demand and the offer and characteristics of the relevant product⁴.

³ This has also been pointed out by the Commission on Page 57 of the Interim Report.

⁴ Commission decisions COMP.IV/M.1616 “Antonio de Sommer Champalimaud/Banco Santander Central Hispanoamericano”, COMP.IV/M.1089 “Paribas Belgique/Paribas Nederland”, COMP.IV/M.1029 “Merita/Nordbanken”, COMP.IV/M.850 “Fortis/Meespierson”, COMP.IV/M.873 “Bank Austria/Creditanstalt”, and decisions from the Spanish Competition Court nums. C51/00 “Cajas Navarras”, C43/99 “Caixa Vigo/Caixa Ourense/Caixa Pontevedra”, C47/99 “BBV/Argentaria”, C39/99 “Banco Santander/Banco Central Hispanoamericano” and from the Spanish Competition Service nums. N-06053 “Banco Sabadell/Banco Urquijo” and N-03077 “Banco Sabadell/Banco Atlántico”.

Nevertheless, it is to be noted that the lack of harmonisation or, in other words, the respect for “local preferences,” might be justifiable in terms of economic welfare despite the fact that with such differences something might be lost as far as economies of scale are concerned. Such lack of harmonisation or respect for “local preferences” might be justifiable provided that such local differences are not used as a discriminatory or protectionist measure. Thus, failure to achieve full harmonisation is required since the legislative differences amongst Member States are the response to the differing consumer demands in each Member State.

(ii) Structural reasons. Market fragmentation may also be due to reasons of a structural nature. The various types of financial institutions, the level of development of financial entities and the products and/or services being offered are different from one country to another. Thus, market fragmentation is also due to the different surrounding macroeconomic and microeconomic situations of each Member State.

Regarding the above, it is of note that savings banks may have played a different role in each particular Member State. For instance, as far as Spain is concerned, Spanish savings banks have played a very important and positive role in the development of the Spanish financial system as a whole. Not only have they fought strongly against the phenomenon of financial exclusion, but they have also played a major role in extending services and in creating a highly competitive environment in the Spanish financial system. It is to remark the statement included in the report prepared by the International Monetary Fund regarding Spanish saving banks⁵ which reads as follows:

"The savings banks have been a major force in extending services and in creating a highly competitive environment in the Spanish financial system. They have close ties with the communities and they support social, cultural, and educational projects. Savings banks have endeavoured to keep close to their customer base and have successfully adapted to the liberalization of the Spanish financial sector. They have a large network of branches and a strong regional identity, and since 1980 have steadily increased their market share of customer deposits and total credit to the private sector—which is concentrated in lending to individuals and to small- and medium-size enterprises—to account for more than one-half of the system in 2005. Savings banks have built a strong capital base over the years and the system has suffered no systemic crisis."

Likewise, it is to remember that the liberalization process of the Spanish financial system which started in the end of the decade of the 70s ended up with a serious crisis of the Spanish financial system during years running from 1978 to 1985. Before such a situation, the Bank of Spain was obliged to adopt urgent measures, amongst which, it included the creation of a deposit guarantee fund (hereinafter, the “DGF”). While the activities of the DGF in relation to commercial banks was of utmost importance to overcome the crisis, the activities of the DGF in relation to saving banks was more discrete, in line with the small effects of the crisis on saving banks.

⁵ INTERNATIONAL MONETARY FUND (Monetary and Financial Systems Department); *Financial Sector Assessment Program. Spain: Technical note on regulation, supervision and governance of the Spanish Cajas [Saving Banks]*; May 2006.

(iii) Cultural reasons. Likewise, from country to country, there might be cultural differences which affect demand for the different retail banking products and/or services. For instance, access to housing may differ from one Member State to another, which in turn affects the greater or lesser demand for mortgages. Likewise, in some countries consumers, when selecting retail banking products and/or services, might prefer the physical presence of persons, whereas in other countries consumers might prefer to contract retail banking services from home or office – telephone, the Internet, etc.

2.3. Varying rates of profitability and income in retail banking amongst the Member States

The Commission comments that there are varying rates of profitability and income in retail banking in the different Member States.

Regarding the reasons that might justify the different levels of profitability and income in retail banking in the different Member States, the following should be pointed out:

(i) Differences in interest rates in the EU Member States. There are still cross-border differences in various types of deposit and lending interest rates that are offered and charged by euro-area monetary financial institutions to households and non-financial corporations. Despite the convergence that has taken place in the euro area over the last several years, similar types of interest rates still vary from one country to another.

As indicated by the European Central Bank⁶, several factors contribute to the dispersion. One factor may be the remaining product heterogeneity, which could be a reflection of differences in national commercial conventions and practices, as well as in regulatory and fiscal arrangements. Other factors such as differences in credit risk dispersion and market structure, also contribute to such differences.

(ii) Different legislations in the Member States. As mentioned in Section 2.2 above, there are still certain differences amongst the legislations of the different Member States.

With regard to legislation on remuneration of products, it may be pointed out that “la Caixa” has always had a positive attitude towards assuring consumers a remuneration of the products and services they contract. A significant example is Case C-442/02 (*Caixabank vs. France*), where the European Court of Justice ruled in October 2004 that France could not ban interest-bearing current accounts in that that would constitute an obstacle to freedom of establishment.

(iii) Heterogeneity in the products and/or services compared. To make a proper comparison of the levels of profitability and income with regard to the different products and/or services offered, it is of crucial importance that the products and/or services being compared are similar. This is so because several quality levels of

⁶ Report “*Differences in MFI Interest Rates across the Euro Area Countries*” which can be found in the “Publications” section of the European Central Bank’s website <http://www.ecb.int/pub>.

products and/or services may actually be offered under a common commercial name. Otherwise, the results of the comparison are questionable. In other words, the services and or products compared might differ from one country to another (for instance, the specific services included, the time frame within which the particular service is offered, a value-added service in one country may be regarded as standard in other countries, etc.) and thus, the conclusions obtained with regard to their profitability might not be very accurate.

(iv) The conditions of each retail banking market. For cultural reasons, in some countries there might be high demand for a particular product and/or service whilst in other countries the demand for such a product and/or service might be moderate or even low. A clear example is the demand for mortgages, which will obviously depend on the different approaches that consumers have to access to housing. Accordingly, some products might be more profitable than others, influencing thereby the existing differences between entities of the different Member States as far as their profitability and income are concerned.

(v) Role played by regulators. The role that each regulator plays in the market may differ from one Member State to another. For instance, as far as Spain is concerned, financial entities are forbidden from charging any commission for depositing money in a bank account, including when such deposit is made by a person who is not a client of such entity. Obviously, any transfer of funds involves certain costs because it involves manual handling, but the fact that Spanish banks cannot charge for such services may affect the profitability of Spanish banks vis-à-vis banks in another country.

(vi) Different levels of efficiency of the banking service providers. The efficiency of retail banking service providers may be different from one country to another, and this in turn affects their level of profitability and income.

In light of the above and to conclude, varying rates of profitability and income rates of retail banking services across Europe might be due to all of the following factors: (i) differences in interest rates in the EU Member States, (ii) different legislations in the Member States, (iii) heterogeneity of the products and/or services compared, (iv) the conditions of each retail banking market, (v) role played by regulators and (vi) different levels of efficiency of the banking service providers.

3. SPANISH MARKET FOR RETAIL BANKING

3.1 The importance of proximity in the Spanish market for retail banking

The retail banking business is, by definition, a proximity business. Despite the significant technological effort that has been made until now, the relationship between customer and bank remains a fundamental competitive factor due to the trust that derives from proximity.

This main feature of the retail banking business in general is even more important in the Spanish case: Spain shows a unique model of banking structure in Europe. It not only has the largest network of branches (42,073 by the end of 2005) but also the

greatest density (11.5 branches per every 10,000 inhabitants over 16 years-old, according to the last reports of the Bank of Spain).

Saving banks contributed to this circumstance. After the withdrawal of the legal impediment that banned savings banks from expanding out of their territory of origin in 1989, they have weaved a banking model of their own (nowadays, the 46 savings banks operating in Spain have 22,444 branches). An important aspect to highlight is that the geographic expansion of savings banks took place at the very moment where new technologies were being implemented on a general basis. As a result, the expansion was carried out with reduced staff per branch, and thus, with an average office of small size (today the average number of staff is 4.2 employees per branch).

With a model based on many branches of small size, banking coverage is given in all regions, even in those with a lower income rate, which guarantees the access to a high level of banking services in the whole territory.

In this regard, it is indisputable the role played by savings banks which, having a calling for retail service for all social groups and geographic regions, have practically eliminated the financial exclusion phenomena. This aspect merits special attention, mainly due to the interest that the topic of financial exclusion has had in countries like the United Kingdom (savings banks disappeared from this country many years ago). Some studies entrusted by the British government, like the one known as Cruickshank Report⁷, have brought about the existence of a growing mass of population that is being excluded from the financial system. With regard to the financial exclusion phenomena and the efforts made by “la Caixa” against such phenomena, please see Section 3.2.1 below.

As a consequence, the importance of having a large network of branches, in order to successfully compete in the Spanish retail banking market, could be considered as a “natural entry barrier” and not as an anticompetitive tool. In the contrary, multi-channel offering (branches, online banking, telephone banking, ATMs) is of increased importance and has been pushed especially by all “traditional” financial institutions with a wide branch network. Moreover, the last years has seen an important entrance or “pure” online banks. Interestingly, however, there has been a recent trend towards continued branch opening, even by “pure online bank” players.

3.2. Spain’s mobility of bank customers is remarkably high

The Interim Report itself recognizes that Spain’s mobility of bank customers is remarkably high and ranges over 14% well above the EU average⁸. Spanish consumers do not suffer high switching costs when deciding to change service provider because of all of the reasons explained below:

⁷ “Competition in UK banking: A report to the Chancellor of the Exchequer” that can be consulted in the web page of the HM Treasury.

⁸ Page 100 of the Interim Report.

3.2.1. High Price Transparency in the Spanish market for retail banking. Unique case within the European Union

Financial entities operating in Spain within the retail banking market have a considerable amount of obligations to comply with to assure price transparency vis-à-vis their customers. Probably, the case of Spain is unique within the European Union and is one of the countries with greatest price transparency.

Amongst other obligations aimed to assure price transparency, financial entities operating in Spain have to comply with the following obligations:

(i) Financial entities are obliged, for registration purposes, to report to the Bank of Spain and to the Spanish Securities and Exchange Commission (“CNMV”), prior to their implementation, the maximum amount of commissions and expenses that they shall charge their customers for the products or services offered. Once the financial entity has communicated such commissions and expenses, the financial entity is not able to charge higher commissions or fees than the ones communicated or charge for concepts not included in such a communication⁹. If the relevant financial entity then decides to change its commissions and fees, such financial entity will have to communicate once again the new commissions and fees to be applied and justify to the Bank of Spain any eventual increase of such fees and commissions.

In some cases, although it is not legally provided, the Bank of Spain may inform financial entities of its opposition to certain commissions or charges, mainly on the basis that they are excessive or cannot be deemed a consideration for a real service.

With the information received from the financial entities, the Bank of Spain then publishes in its webpage the different services rendered by the financial entities as well as the maximum prices applied for the same¹⁰. As a consequence thereof, customers can easily compare the prices applied by the different financial entities.

The above obligations do not only affect individual products and/or services, but also products and/or services offered as a bundle.

(ii) Financial entities must communicate to the Bank of Spain on a monthly basis the average interest rates applied for certain transactions carried out in Spain.

With this information, the Bank of Spain publishes and makes available to the public in its webpage interest rate references or indexes¹¹.

(iii) Financial entities must have, in each and all of the branches which are opened to the public, a poster fixed permanently and in a place which attracts the attention of the public containing amongst others, the commissions applied for the provision of

⁹ Obligation that arises from the Order of December 12, 1989, of the Ministry of Finance and Economy regarding interest rates and commissions, rules on behavior, information to customers and publicity of credit institutions and the Spanish Act 9/1999 that implements Directive EC/97/5. These documents can be found at: <http://www.bde.es/clientebanca/derechos/normas/normas.htm>.

¹⁰ See at <http://www.bde.es/tipos/comisiones.htm>

¹¹ Obligation that arises from Circular 8/90, of September 7, of the Bank of Spain regarding credit institutions, transparency of the transactions and protection of the clientele.

services of subsequent performance, the preferential interest rate applied as well as the interest rate applicable in case of overdraft¹².

(iv) Any publicity made by credit institutions regarding transactions, services or financing products is subject to the prior approval of the Bank of Spain provided such publicity contains information regarding prices and conditions applicable to the same. This prior approval guarantees that any publicity is transparent and clear to the public¹³. Otherwise, the publicity would not be authorized by the Bank of Spain.

Each and all of the above obligations above indicated assure a high level of price transparency for customers enabling them to easily compare the prices applied by the different service providers and helping them to adopt the decision on whether to change service provider or not.

With regard to the above, “la Caixa” wants to point out that the level of obligations regarding price transparency is perhaps too burdensome for financial entities and that the objective of such provisions (that is, to assure price transparency) could nevertheless be achieved with fewer obligations imposed on financial entities, increasing thereby the efficiency of Spanish entities as well as competition on prices among them.

From “la Caixa”’s point of view, it might be advisable to consider the eventual lessening of or leniency with the indicated obligations and, more in particular with regard to, the obligation indicated in paragraph (i) above that consists in the obligation to communicate to the Bank of Spain and to the CNMV and file the maximum amount of fees and commissions to be charged to customers. This is so because Spain is the sole country with such an obligation within all the European Union. Furthermore, such price transparency measure only affects the maximum amount of fees and commissions to be applied but not the commissions and fees effectively applied to customers and, on the financial entities’ perspective, such obligation considerably restricts their freedom when deciding the fees and commissions to be applied to its customers and consequently it may negatively affect the Spanish entities ability to compete on prices, specially when time is of essence in the design of marketing strategies.

Furthermore, the Interim Report remarks the customers’ perceptions of pricing complexity¹⁴. With regard to such supposed complexity, “la Caixa” wants to point out that it has incurred in efforts and investments to facilitate customers the understanding of the information that it is provided to them. Amongst others, it is to remark the program launched by “la Caixa” targeted to foreigners from developing countries to help them understand, not only the products and services offered and its pricing policy, but also the financial system as a whole. “la Caixa” has always fought against the financial exclusion phenomena assuring that all social groups and geographic regions have access to the financial system. Apart from specific programs aimed to determined groups, “la Caixa” also makes sure that amongst all of its employees

¹² Obligation that arises from Circular 8/90, of September 7, of the Bank of Spain regarding credit institutions, transparency of the transactions and protection of the clientele.

¹³ Obligation that arises from Circular 8/90, of September 7, of the Bank of Spain regarding credit institutions, transparency of the transactions and protection of the clientele.

¹⁴ Page 95 of the Interim Report

(including the ones working in its branches), there is a good representation of people from abroad to make sure that they can speak and understand different languages. Likewise, home banking services and services through ATM are offered in several languages to make sure that no customer encounters itself with a language problem.

3.2.2. Lack of Information Asymmetry in the Spanish market for retail banking

In its Interim Report¹⁵, the Commission considers that a banking relationship often results in a better understanding by the bank of the credit quality of its customers and that this information may be lost when a customer switches banks. As a consequence thereof, low credit risk customers are pooled together with higher credit risk customers when changing bank and consequently, they are charged with higher interest rates.

“la Caixa” believes that in Spain such information asymmetry does not exist because of the existence of three (3) different data basis with information on financial solvency and which any financial entity can have easy access to. For further details regarding the credit registries existing in Spain, see Section 4.1 below.

Thus, “la Caixa” considers that in Spain it is unnecessary to implement a portable credit record or credit history to be issued by the financial entities. This kind of measure would only increase the formal obligations already imposed to financial entities operating in Spain, impose larger costs on operators and delay the current time limits to switch from one service provider to another one.

3.2.3. No administrative burdens

In general terms, one can say that in Spain customers do not suffer administrative burden when changing service provider. In this regard, “la Caixa” wants to remark the following: (i) in Spain it is generally the new service provider who, free of cost, offers the new customer the service of informing all interested parties about the new bank account details of the recently acquired client or even carrying out all formalities before the relevant Social Security authorities as far as pensions are concerned. This free of cost services liberates the customers of a high administrative burden; (ii) in Spain the abandonment of bank accounts is generally not penalized which in turn makes that some customers do not close their bank accounts with their former banks and (iii) many of the formalities that the customers may have to do to change service provider can now be made through electronic means without the consumer having to physically go to the bank’s branch to do such formalities.

Consequently, “la Caixa” considers that the measures proposed by the Commission in its Interim Report¹⁶ consisting in (i) switching regulations which would require banks to observe certain procedures and deadlines when transferring a customer’s account details to a new bank or (ii) switching codes to be agreed between banks delivered through industry self-regulation rather than rules set by the regulator, are unnecessary. The adoption of such measures would increase the administrative burden of Spanish banks and hamper their efficiency.

¹⁵ Page 94 of the Interim Report.

¹⁶ Page 116 of the Interim Report.

3.2.4. Limited closing charges

With regard to closing charges being considered as a switching cost for customers when changing service provider, “la Caixa” would like to remark that, in general terms, Spanish financial entities do not apply any penalty for the closing of a bank account.

Likewise, the abandonment of bank accounts in Spain is not penalized. Several decisions of the Bank of Spain have forbidden Spanish entities from charging commissions to bank accounts with an outstanding balance of 0€ Such prohibition has resulted in a high ratio of bank accounts abandoned but which in turn generate a cost for the financial entity.

Furthermore, Spain is one of the sole countries within the European Union where customers have the possibility to subrogate within mortgages with reduced costs - formalities as per public notaries and property registries have a discount of 75% or 90% and a maximum bank commission for early cancellation of 0.5% of the pending capital-, increasing thereby the mobility of customers.¹⁷

3.2.5 Cross Selling, Bundling and Tying cannot be considered anticompetitive

Similarly, banking practices such as “cross-selling”, “bundling” or “tying” should not be considered anticompetitive practices in general terms. Indeed, the different price policies observed are consequence of different business models and orientation towards different types of customer. They generate a profit for the banking entity but also represent a value-added to the customer who benefits from a service that fits better to his/her preferences. Thus, the price policies observed are the consequence of the diversity on the demand-side.

On the offer-side, the existence of scope economies (that may be achieved by offering a wide range of products and services) justifies this practice. Scope economies are the consequence of the bank’s own nature due to the joint offering of the whole range of services throughout its entire branch-network (in a way that the cost of the joint production is lower than the cost of products produced separately).

In the Interim Report¹⁸, the Commission considers that in some cases bundling might reduce price transparency since bundling might make it difficult for the customer to compare the prices of its current bank with those of its competitors. As commented in Section 3.2.1 above, Spain is one of the countries within the EU with the highest level of price transparency. The obligations imposed to financial entities regarding price transparency do not only affect individual products and/or services, but also products and/or services offered as a bundle.

To conclude, Spain is one of the countries with the highest level of customer mobility and this is due to (i) high price transparency, (ii) lack of information asymmetry and (iii) no administrative burdens nor closing charges. Likewise, practices such as cross

¹⁷ Spanish Act 2/1994 on Mortgages and Royal Decree-Law 2/2003 on Economic Incentives.

¹⁸ Page 96 of the Interim Report.

selling, bundling and tying benefit both the financial entity and the customer, without price transparency being affected. One can not ask for higher levels of customer mobility since at the end it is the choice of the own customer who has all the elements to freely change service provider.

4. CREDIT REGISTRIES AND PAYMENT SYSTEMS ARE NOT A BARRIER TO ENTRY IN THE SPANISH RETAIL BANKING MARKET

4.1. Credit registries and barriers to entry in the Spanish retail banking market.

The Commission recognizes that credit data share can have some positive effects and that empirical evidence suggests that greater availability of credit data can improve the performance of the retail banking market¹⁹. However, in the Commission's view, credit information sharing can also lead to foreclosure problems in the market, for example when members of a credit bureau refuse to admit potential entrants, or where such an entry is granted on a discriminatory basis.

In this regard, "la Caixa"'s view is that credit information sharing in the Spanish market can not lead to foreclosure problems in the market. This is so because in Spain there are currently three (3) different credit registries to share data on financial solvency and in relation to which any new entrant can have access to on a non discriminatory basis.

The existing registries are the following: (i) *Registro de Aceptaciones Impagadas* (RAI); (ii) ASNEF-EQUIFAX and (iii) *Central de Información de Riesgos del Banco de España* (CIRBE). While the RAI and the ASNFEX-EQUIFAX are registries privately owned, the third one, that is CIRBE, is managed by the Spanish Central Bank. The coexistence of privately owned and managed registries and a registry managed by the central bank is unique within the European Union.

The Spanish Competition Court has given an individual exemption to the agreement by virtue of which the credit registry ASNEF-EQUIFAX was created²⁰. When granting the individual exemption to such an agreement, amongst other conditions, the Competition Court required that the credit registry be opened to third parties on a non discriminatory basis. Furthermore, it is to remark that following a request for a preliminary ruling made by the Spanish Supreme Court to the European Court of Justice, last June 29, 2006 the Advocate General Mr. L.A. Geelhoed ruled that the ASNEF-EQUIFAX credit registry did not infringe article 81 of the EC Treaty provided the members operating the registry determine their behavior autonomously, including the conditions to be applied to their customers²¹.

¹⁹ Page 150 of the Interim Report.

²⁰ On November 3, 1999 the Spanish Competition Authority authorized the agreement by virtue of which the credit registry ASNEF-EQUIFAX was created for a period of five years (*Expte. A 239/98, Crédito Asnef-Equifax*). On June 18, 2004, the Competition Authority renewed such an exemption for an additional period of five years (*Expte. A 33/1992*).

²¹ Conclusions of the Advocate General in Case C-238/05 *ASNEF-EQUIFAX, Servicios de Información sobre Solvencia y Crédito, S.L. y Administración del Estado contra Asociación de Usuarios de Servicios Bancarios (AUSBANC)* dated June 29, 2006

With regard to RAI and following a decision from the Spanish Competition Court on February 2, 2005 declaring the current text of the agreement on the functioning of the registry contrary to Spanish competition rules²², decision which was confirmed by the National Court (*Audiencia Nacional*) on July 4, 2005²³, the association of banks, saving banks and cooperatives which manage the registry RAI have decided to abide the decision of the Spanish Competition Court and has opened the registry to third parties. Thus, such registry is now also opened to third parties on a non discriminatory basis.

In light of the above, it is to remark that as far as Spain is concerned, data sharing through credit registries can not be considered as a barrier to entry into the Spanish retail banking market since there are currently three credit registries to which newcomers can have easy access to. Likewise and following the relevant decisions of the Spanish Competition Court, both credit registries (RAI and ASNEF-EQUIFAX) now comply with competition rules.

4.2. Payment systems

4.2.1. Introduction to the Spanish retail payment system and its functioning

The Spanish retail payment system is the *Sistema Nacional de Compensación Electrónica* or SNCE. The SNCE was created in 1990 as one of the Spanish bodies for the automatic interchange, clearing and settlement of payment transactions between different retail banks in Spain. Although it is nowadays managed by Sociedad Española de Sistemas de Pagos or SESP—a private corporation whose shareholders are retail banking entities- the Bank of Spain still has the power to approve its rules and monitor the whole functioning of the system.

The majority of retail banking entities acting in Spain are members of the SNCE because this system is more rapid and efficient than other existing systems as regards payment transactions (communication of data, clearing and settlement).

Alternatively or cumulatively to the SNCE, there are pan-European systems for international transactions as well as a number of bilateral agreements between retail banks which are not members to the same payment system.²⁴ Despite the fact of existing alternatives to the SNCE, it can not be denied that operating within the system lowers the risks involved and thus, it is important for entities wishing to operate in Spain to have access to the SNCE.

The SNCE has two types of members: (i) **direct or associated members** and (ii) **indirect or represented members**. Indirect members are represented in the SNCE by a direct member who transmits the orders that it receives from the indirect member/s that it represents and assumes the responsibility for the settlement of the payment made by its represented member/s. Thus, to participate within the system, such indirect members must enter into a representation agreement with their elected direct

²² Decision of the Spanish Competition Court Expte. A 335/03, RAI/CCI dated February 8, 2005.

²³ Decision of the National Court n° 729/2002 dated July 4, 2005.

²⁴ It is to note that according to the data published by the Spanish Central Bank, 44.35% of the total transactions in 2005 which amounted to 75.51% in terms of value, was not processed through the SNCE but directly by banks (including “on-us” transactions and bilateral agreements).

or associated member. SESP does not intervene or participate in the representation agreements that indirect members and direct members may enter into. Thus, the direct member and the indirect member are free to decide on the content and conditions of their particular agreement. New comers wishing to participate in the system can freely choose their preferred representative.

Currently there are 24 direct or associated members. Direct or associated members must be shareholders of SESP and their participation within the corporate capital of SESP is proportional to their level of activity within the system.

¿How does a financial entity become a direct or associate member of the system? Admission of new members must be approved by the Board of Directors of SESP which shall only refuse the entrance of new direct members in the case the relevant applicable criteria is not met. In this regard, it is to note that to become a direct member of the system the interested financial entity must achieve at least 0.5% of the total volume of transactions of the system. This is so without prejudice of the nationality of the interested financial entity and irrespective of whether such financial entity has a physical presence in Spain. Hence, the possibility of becoming a direct or associated member of the system depends on an objective, transparent and non-discriminatory criteria. Likewise, such criteria was initially established by the Bank of Spain.²⁵ One fact that merits special attention is that although the Bank of Spain has assigned the management of the SNCE to SESP, the Bank of Spain continues to exercise a supervisory role.

With regard to the threshold of the 0.5%, “la Caixa” would like to point out that such a threshold is not restrictive but that it is a consequence of the system being bilateral. The system would become unworkable if the number of direct participants is too high. That is, that the 0.5% is a technical and operational requirement needed for the proper functioning of the system. Furthermore, the existing rules do not prevent financial entities from entering into pooling or collaboration agreements to accumulate their individual volumes of transactions within the system to reach the above indicated threshold of 0.5%.

Finally, “la Caixa” considers that the current system to become a direct or associated member of the SESP fosters competition within the retail banking market as far as those financial entities wishing to become so will be encourage to increase their retail activity up to such an extent as to reach the threshold of 0.5% of the total volume of transactions carried out within the system.

SNCE not constituting a barrier to entry into the Spanish market is evidenced by the large number of foreign banks (both EU and non EU based) that operate in Spain and which compete vigorously with Spanish entities²⁶.

²⁵ Rules regarding the functioning of the SNCE contained in Circular nº 8/1988 of the Spanish Central Bank

²⁶ To verify the number of foreign entities operating in Spain please see the webpage of the SESP: <http://www.sesp.info/sncepar.pdf>.

4.2.2. System of fees charged by SESP.

Within the system, there are three (3) different types of fees that SESP charges to its members. These are the following:

Joining Fee: The current joining fee amounts to 12,000€ for direct or associated members and 1,200€ for indirect or represented members. Hence, the joining fee paid by direct or associated members is considerably higher than the one charged to indirect or represented members. By paying such a moderate joining fee, newcomers are capable of benefiting from the entire system without compensating associated members for the enormous historical amounts invested in the creation and maintenance of the entire system, thus jeopardizing the associate members' capacity to compete. Contrary to that, in other European countries, the joining fees established to access the system assure that associated members are compensated for the historical investments made in the system. This does not seem to be the case in Spain.

Annual Fee: For year 2005, the annual fee applied to direct or associated members amounted to 50,000€ while the annual fee charged to indirect or represented members amounted to 750€ per year. Once again, the amount to be paid by direct or associated members is considerably higher than the amount to be paid by indirect or represented members.

Per Transaction Fee: Per transaction fees range from 0.0003€ to 0.0012€ and are only charged to direct or associated members. Direct or associated members can obtain volume discounts on per transaction fees depending on the total volume of transactions carried out within the system. Per transaction fees are never charged to indirect members. Nevertheless, direct members may agree with their represented indirect members the reimbursement of part of the per transaction fees paid to SESP. Without prejudice to the above and as it has been indicated above, SESP does not intervene at all in such agreements nor has any influence on the same.

Indirect members have a strong bargaining power vis-à-vis direct members of the system. On the one hand, they can choose amongst 24 entities as to which one of them shall represent them within the system. On the other hand, direct members are interested in entering into the most representation agreements as possible as far as all the transactions of their represented entities are attributed to them and this shall favor them to obtain greater volume discounts.

In light of the above, "la Caixa" considers that the current fee structure applied by the SESP grants a more favorable treatment to indirect participants (i.e. new comers) than if compared to direct or associated members (i.e. incumbent banks). It even prejudices associated members since the joining fees to access the system do not compensate the historical investments made by the associated members. Thus, access to the SNCE can not be considered as a barrier to entry in the market but all to the contrary: the current system grants a more advantageous treatment to newcomers.

In fact, certain associated members have decided to become indirect members because of the more favorable treatment granted to indirect members by the SESP rules.

4.2.3. Interchange Fees

As a preliminary comment, “la Caixa” wants to remark that interchange fees are agreed on a bilateral basis by the associated members of the SESP and that SESP does not intervene in calculating their amount or in the discussions between the banks to the bilateral agreements or in the implementation of the same. Likewise, the Bank of Spain, when the SNCE was created, installed a set-by-default system.

The amount of interchange fees effectively applied by financial entities has decreased over time. Likewise, Spanish interchange fees applied by default (that is, those applied in the absence of bilaterally agreed fees between banks) are not any more broken down in ranges (for instance, varying depending on the sector involved or the value of the transaction). Furthermore, interchange fees do remunerate banks for certain services rendered which involved certain costs for the banks. The default interchange fees have been set up taking into account the costs involved in the transactions and thus they are cost-oriented. This is shown by the fact that fully automatic STP transactions bear a moderate fee.

With regard to this subject matter, “la Caixa”’s view is that interchange fees should not pose a problem from a competition law point of view when they are agreed on a bilateral basis and when the fees applied by default are cost-oriented. At the end, they remunerate the banks for certain costs suffered for the rendering of the services. In addition to the above, interchange fees should not pose a problem in those markets which are highly competitive. If the market is highly competitive, banks will have to absorb the interchange fees and not pass them unto their clients. Spanish market for retail banking is highly competitive and there is a strong vigorous competition between banks. Nowadays there are certain entities which do not charge any commission to their customers for transmitting or receiving funds nor for cashing checks. A clear example is “la Caixa” which does not charge any commission to its customers for receiving funds nor for transferring amounts such as salaries or pensions.

4.2.4. Commissions

The Interim Report indicates that market participants had highlighted three problems concerning access to clearing and settlement facilities.

4.2.4.1 Commissions as a percentage of the value of the transaction.

On customers’ charges for payments, market participants alleged that Spanish banks are alone in the EU in charging payment fees as a percentage of the value of the transaction. They alleged that such fees were disproportionate to transaction costs and created uncertainty regarding the level of payment fees. Likewise, they consider that charging payment fees as a percentage of the value of the transaction poses a problem concerning access to clearing and settlement facilities.

In this respect, “la Caixa” would like to point out the following:

- (i) Greater risks assumed by Spanish entities.** Charging fees as a percentage of the value of the transaction is justified as far as the risks assumed by Spanish entities are greater than the risks assumed by entities of

other European countries. Although the costs for settling and clearing a transaction are the same independently of the value of the transaction, it is important to remark that there are certain costs which are linked to monitoring the risks involved in bank transfers. Spanish entities have additional obligations and, as a consequence thereof, additional risks and responsibilities.

On the one hand and following the criteria established by the Bank of Spain in several resolutions²⁷, the bank of the beneficiary must verify the identity of the beneficiary and, in case of discrepancy between the name of the beneficiary and the bank account indicated in the order of transfer, the beneficiary payment service provider must transfer the funds to the person indicated in the order of transfer and, if such person does not hold a bank account in such entity, then the bank must return the funds to the originator payment service provider. The criterion established by the Bank of Spain has also been confirmed by the Spanish Supreme's Court²⁸ as well as by a regional court²⁹.

As seen above, the current Spanish regime goes further than that established in Directive 97/5/CE, of the European Parliament and the Council, of January 27, 1997 on cross border transfers, as far as the obligations of the bank of the receiver is concerned. Furthermore, it seems that other European countries such as the United Kingdom, Germany and The Netherlands have adopted a different approach. While those countries have not regulated the obligation of the beneficiary's bank to verify the identity of the beneficiary, it can be said that entities in the United Kingdom, Germany and The Netherlands are exonerated from such an obligation.

Likewise, it is to note that both Article 8 of the UNCITRAL's Model Law on International Credit Transfers (hereinafter, "Model Law") as well as Article 4.A of the Uniform Commercial Code of the U.S.A. (hereinafter, "UCC") have exempted the bank of the beneficiary of an international credit transfer of the obligation to identify the beneficiary of a credit transfer. The aim of those provisions is to reduce the costs involved in bank transfers since the same shall only be based in standardized numerical codes.

As far as the Model Law is concerned, its Articles 8.5, 10.3 and 10.4, when dealing with the bank of the beneficiary's obligations, they do not establish the obligation of the bank to verify the identity of the beneficiary of the funds. Thus, the bank shall either follow the name of the beneficiary or the numerical code of the bank account and, in no event, shall be liable for the eventual losses and damages caused in case of an error. Nevertheless, if such bank detects a discrepancy between the name of the beneficiary and the holder of the account, the bank shall suspend the transaction and obtain more information from the bank originator of the transfer of funds.

As far as Article 4.A of the UCC is concerned, it is to note that the same does not impose on the bank of the beneficiary the obligation to verify the identity

²⁷ Amongst others, Resolution 1110/00 *Colonya-Caixa D'Estalvis de Pollensa*, Resolution 548/01 *Bilbao Vizcaya Argentaria*.

²⁸ Supreme Court's decision dated November 14, 1987 (RJ 1987/9987)

²⁹ Decision of the Provincial Court of Castellón dated May 13, 2000 (JUR 2002/159423)

of the beneficiary. Nevertheless, under Article 4.A of the UCC, the numerical code prevails over the name of the beneficiary. Thus if the bank discovers a discrepancy, it shall obtain instructions from the originator. If it does not discover the discrepancy, then to avoid incurring in any discrepancy, it shall execute the transaction following the numerical code. As a consequence thereof and to avoid incurring in responsibilities, banks shall always follow the numerical code included in the order of transfer of funds.

On the other hand and following a decision of the Spanish Supreme Court³⁰, in case of fraud, the bank is the responsible one. Although this case law was first developed in cases of checks, the decision of the Supreme Court before indicated has applied the same doctrine in cases of transfer funds.

In light of the above, the greater the amount of the transaction is, the greater the risk is.

(ii) Limited effects. Despite Spanish entities charging commissions as a percentage of the value of the transaction, at the end, the total amounts charged for such concept is probably lesser than the amounts that would have been charged if a fixed amount of commissions would have been in place. This is so because (i) many entities do not currently charge any commission to their customers neither for transmitting or receiving funds nor for cashing checks (for instance, “la Caixa” does not charge any commission to its customers for receiving funds nor for transferring amounts such as salaries or pensions) and (ii) as a result of the negotiations with the client, a flat fee is very often applied (specially with companies).

Furthermore, several Spanish entities, including “la Caixa”, offer packs to its customers containing a certain number of transfers of funds free of cost.

To conclude, one can say that charging commissions as a percentage of the transaction is justified as far as Spanish entities assume greater risks if compared to other EU countries (general obligation to verify identify of the beneficiary). Likewise and although the possibility of charging a commission on the value of the transaction exists, in practice and as a result of the negotiations with the customer and because of the vigorous competition within the market, a flat commission is applied or even no commission at all. Thus, in light of the above, the implementation of a flat fee would have negative consequences if compared to the existing regime on fees per value of the transaction.

4.2.4.2. Shared Commissions.

Market participants also alleged that “*the recently privatized clearing system was seeking to set up a shared commissions system among banks which would allow them to charge customers on received transfers. Concerns were expressed that this arrangement would suppress price competition for clearing services and harm consumers*”.

³⁰ Supreme Court’s decision dated July 15, 1988 (RJ 1988/5717)

To the best knowledge of “la Caixa”, SESP has never sought to set up a system of shared commissions amongst banks which would allow them to charge customers on received transfers. As indicated above, SESP only manages the clearing and settlement system but does not intervene in the relationships of its members and their customers not in the representation agreements between direct and indirect members.

Nevertheless and as far as shares commissions are concerned, it is to remark that the Proposal for a Directive of the European Parliament and of the Council on Payment Services in the Internal Market³¹ (hereinafter, the “New Legal Framework Directive”) in its Para. 26 of the Preamble already recognizes that a system of shared commissions is the most efficient system. In this sense, Para. 26 of the Preamble reads as follows:

“With regard to fees, experience has shown that the sharing of fees between payer and payee is the most efficient system since it facilitates the straight-through processing of payments. Provision should therefore be made for fees to be levied directly on the payer and the payee by their respective payment service provider.”

Likewise, Article 57 of the New Legal Framework Directive reads as follows:

“Where a payment transaction is carried out solely in the currency of a Member State and not involve any currency exchanges and where the service providers of both the payer and the payee are located in the Community, Member States shall require that any fees be levied directly on the payer and the payee by their respective payment service provider, and that they each bear their own fees”.

Thus, it is surprising that the fact of certain banks having announced to start charging their customers for received funds, decisions probably adopted in view of the legal framework to be implemented by the New Legal Framework Directive, raises the concerns of the market participants as well as the Commission.

4.2.4.3 *Inter-bank fees applied to larger transactions.*

Market participants believed that interchange fees applied to larger transactions (over 3,000€) were disproportionate to the processing costs and ultimately pushed up prices for consumers. Likewise, such inter-bank fees for larger transactions could hamper access to clearing and settlement facilities.

With regard to the above, “la Caixa” understands that there must have been an erroneous interpretation either by the market participants or by the Commission when drawing up these conclusions.

Transactions above 3,000€ and transactions below 3,000€ are completely different transactions. Transactions above the limit of 3,000€ are processed through a different

³¹ Proposal for a Directive of the European Parliament and of the Council on Payment Services in the Internal Market and amending Directives 97/7/EC, 2000/12/EC and 2002/65/EC, dated December 1, 2005 / 2005/0245 (COD).

circuit which requires greater control and supervision and which involves greater costs. Contrary to that, transactions below the limit of the 3,000€ are processed through a different circuit which involves lesser costs. Thus, the commissions for there later transactions are inferior.

Thus, the differences in commissions between transactions above or below the limit of the 3,000€ are justified from a costs' perspective.

5. CONCLUSIONS

- Although the statistical data included in the Interim Report is a good point of departure for an initial study of the retail banking market, such data must be further refined and completed prior to drawing any conclusions from the same.
- Market fragmentation within the EU retail banking market is due to reasons of a legislative, structural and even cultural nature. Thus, market fragmentation does not necessarily involve the existence of anti-competitive practices.

Amongst the reasons of a structural nature, it is to remark the different role played by saving banks in the financial systems of each Member State. In this regard, Spanish savings banks have played a very important and positive role in the development of the Spanish financial system as a whole. They have fought strongly not only against the phenomenon of financial exclusion, but they have also played a major role in extending services and in creating a highly competitive environment in the Spanish financial system. Furthermore, during the Spanish financial crisis running from 1978 to 1985, it is of note that the activities of the DGF with regard to saving banks were discrete if compared to the activities in which the DGF engaged with regard to commercial banks.

- Varying rates of profitability and income rates of retail banking services across Europe might be due to all of the following factors: (i) differences in interest rates in the EU Member States, (ii) different legislations in the Member States, (iii) heterogeneity of the products and/or services compared, (iv) the conditions of each retail banking market, (v) different role played by the regulators of each Member State and (vi) the different levels of efficiency of the banking service providers.

Spain is one of the countries with the highest level of customer mobility and this is due to (i) high price transparency, (ii) lack of information asymmetry and (iii) no administrative burdens and limited closing charges. Likewise, practices such as cross selling, bundling and tying benefit both the financial entity and the customer, without price transparency being affected.

- It might be advisable to consider the eventual lessening of or leniency with the obligation imposed on Spanish financial entities to report the maximum amount of fees and commissions to be charged to customers to the Bank of Spain and to the CNMV and file such tariffs since (i) Spain is the only country with such an obligation within all the European Union and (ii) from the financial entities' perspective, it may negatively affect the Spanish entities ability to compete on prices, specially when time is of essence in the design of marketing strategies.

- Data sharing through credit registries can not be considered as a barrier to entry into the Spanish retail banking market since there are currently three credit registries to which newcomers can have easy access to, including a credit registry managed by the Bank of Spain.

- Likewise, access to the SNCE can not be seen either as a barrier to entry to the Spanish market because the access system depends on an objective, transparent and non-discriminatory criteria initially established by the Bank of Spain. Furthermore and although the Bank of Spain has assigned the management of the SNCE to SESP, the Bank of Spain continues to exercise a supervisory role.

The current fee structure applied by the SESP grants a more favorable treatment to indirect participants (i.e. new comers) than to direct or associated members (i.e. incumbent banks). The current fee structure even prejudices associated members since the joining fees to access the system do not compensate the historical investments made by the associated members.

- Interchange fees should not pose a problem from a competition law point of view when they are agreed on a bilateral basis and when the fees applied by default are cost-oriented. At the end, they remunerate the banks for certain costs suffered for the rendering of the services. Additionally, the role played by interchange fees raises no concerns in markets which are highly competitive like the Spanish one.

- Charging commissions as a percentage of the transaction is justified as far as Spanish entities have more obligations and assume greater risks if compared to the entities of other EU countries (such as the obligation to identify the beneficiary of the transfer of funds). Likewise and although the possibility of charging a commission on the value of the transaction exists, in practice and as a result of the negotiations with the customer and because of the vigorous competition within the market, a flat commission is applied or even no commission at all. Implementation of a flat fee would have negative consequences if compared to the existing regime on fees per value of the transaction.

- The New Legal Framework Directive recognizes that a system of shared commissions is the most efficient system and specifically foresees the same in its Article 57. Thus, “la Caixa” does not comprehend the reaction of market participants and of the Commission to the fact of certain Spanish banks, and not the SESP, announcing to start applying shared commissions.

- Transactions above or below the threshold of 3,000€ are different types of transactions. Transactions below 3,000€ are processed through a faster circuit and involve lesser costs than transactions over the threshold of 3,000€. Thus, the differences in commissions between transactions above or below the limit of the 3,000€ are justified from a costs’ perspective.
