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2012/0176 (NLE)

Proposal for a

COUNCIL IMPLEMENTING DECISION

amending Implementing Decision 2011/344/EU on granting Union financial assistance to Portugal

EXPLANATORY MEMORANDUM

Upon a request by Portugal, the Council granted financial assistance to Portugal on 17 May 2011 (Council Implementing Decision 2011/344/EU) in support of a strong economic and reform programme aiming at restoring confidence, enabling the return of the economy to sustainable growth, and safeguarding financial stability in Portugal, the euro area and the EU.

In line with Article 3(9) of Decision 2011/344/EU, the Commission, together with the IMF and in liaison with the ECB, has conducted the fourth review to assess the progress on the implementation of the agreed measures as well as their effectiveness and economic and social impact.

Taking into account the recent economic, fiscal and financial developments and policy actions, the Commission considers that limited changes to the economic policy conditions underpinning the assistance are necessary to secure the programme's objectives, as explained in the recitals of the proposed amendments to the Council implementing Decision.

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Proposal for a

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Council Regulation (EU) No 407/2010 of 11 May 2010 establishing a European financial stabilisation mechanism[1], and in particular Article 3(2) thereof,

Having regard to the proposal from the European Commission,

Whereas:

(1) In line with Article 3(9) of Council Implementing Decision 2011/344/EU, the Commission, together with the International Monetary Fund (IMF) and in liaison with the European Central Bank (ECB), has conducted the fourth review of the authorities' progress on the implementation of the agreed measures as well as of the effectiveness and economic and social impact of the agreed measures.

(2) The review has found that compliance with the conditionality for the first quarter of 2012 was satisfactory. In 2011, the general government deficit was 4.2 per cent of GDP. The fiscal target of 4½ per cent of GDP for 2012 remains within reach. The rebalancing of the economy has continued at a swift pace and exports have outperformed expectations and more than offset weaker domestic demand. However, risks to the fiscal objectives related to the macro-economic outlook have started to materialise, with the growth composition tilting more strongly towards net exports and away from domestic demand and in view of the substantial worsening of the labour market situation. Progress in labour market reforms needs to be sustained. Severance payments will be aligned with the EU average and a fund to finance part of severance payments will be created. A proposal to revise the mechanism for extending collective agreements is under preparation. Policy efforts to support financial system stability continue. The sale of Banco Português de Negocios (BPN) has been concluded and the management of the special purpose vehicles will be optimised to maximise the recovery of the assets transferred from BPN. The early intervention, resolution and deposit insurance framework has been strenghtened and the authorities are asked to prepare the implementing measures. Product market reforms, notably in sheltered services, is essential to restore competitiveness and promote growth and employment. The government is implementing a strategy to restructure state-owned enterprises to reduce their indebtedness and to insure improved conditions for market financing. A study to assess the costs and benefits of renegotiating any public-private partnerships (PPPs) or concession contracts to reduce the government financial obligations is being prepared by an

[1] OJ L 118, 12.5.2010, p. 1.

international auditing firm. The government is committed to ensure an effective competition enforcement regime. Housing market regulations are being modernised with a view to promoting geographical mobility and the reform of the judicial system is making good progress. The privatisation programme is being implemented under the new framework law,

HAS ADOPTED THIS DECISION:

Article 1

Article 3 of Implementing Decision 2011/344/EU is hereby amended as follows:

(1) Paragraph 6 is amended as follows:

(a) point (a) is replaced by the following:

'(a) The general government deficit shall not exceed 4.5% of GDP in 2012. In addition to the measures specified in the 2012 budget and the supplementary budget approved in March, further measures, notably on the expenditure side, shall be taken to fill any possible gap in 2012.';

(b) point (d) is replaced by the following:

'(d) Portugal shall adopt measures to reinforce public finance management. Portugal shall implement the measures provided for in the new Budgetary Framework Law, including setting up a medium-term budgetary framework. The local and regional budgetary frameworks shall be considerably strengthened, in particular by aligning the respective financing laws with the requirements of the Budgetary Framework Law. Portugal shall step up reporting and monitoring of public finances and reinforce budgetary execution rules and procedures. The Portuguese Government shall implement the strategy for the validation and settlement of arrears. The strategy lays out the prioritisation criteria for paying creditors, as well as governance arrangements to ensure a fair and transparent settling process across all sectors. Portugal shall implement the new legal and institutional PPPs framework. Based on the results of a study on PPPs renegotiations, the government shall renegotiate the relevant contracts. Portugal shall adopt a law to regulate the creation and the functioning of state-owned enterprises (SOEs) at the central, regional and local levels.';

(c) point (e) is replaced by the following:

'(e) Portugal shall reorganise and significantly reduce the number of local government entities. These changes will come into effect by the beginning of the next local election cycle.';

(d) point (f) is replaced by the following:

'(f) Portugal shall modernise the revenue administration by completing the implementation of the 'Autoridade Tributária e Aduaneira', reinforcing the links with the revenue collection units of the Social Security, reducing the number of municipal offices and addressing remaining bottlenecks in the tax appeal system.';

(e) point (h) is replaced by the following:

'(h) Portugal shall adopt measures to improve the efficiency and sustainability of state-owned enterprises (SOEs) at central, regional and local level. Portugal shall implement a strategy to restructure, reduce the indebtedness of SOEs – including 'Parpública' -and to ensure improved conditions for market financing. Portugal shall implement this strategy to reach operational balance at sector level by end-2012.';

(f) point (i) is replaced by the following:

'(i) Portugal shall continue implementing the privatisation programme. The direct sale of Caixa Geral de Depositos's insurance arm (Caixa Seguros) shall take place in 2012. The privatisation process of the national air carrier (TAP), the airport operator Aeroportos de Portugal (ANA), the cargo handling subsidiary of CP (CP Carga) and of Correios de Portugal (CTT) shall start in 2012 with a view of finalising it in 2013.';

(g) point (j) is deleted;

(h) point (k) is replaced by the following:

'(k) Portugal shall submit draft legislation to the Portuguese Parliament to align severance payments with the EU average of 8-12 days per year of work and create a compensation fund for severance payments.';

(i) point (l) is deleted;

(j) point (o) is replaced by the following:

'(o) Portugal shall implement the measures set out in its action plan to improve the quality of secondary and vocational education and training.';

(k) point (p) is replaced by the following:

'(p) The functioning of the judicial system shall be improved by implementing the measures proposed under the judicial reform roadmap and by applying targeted measures to progressively eliminate court backlogs and to foster alternative dispute settlements.';

(l) point (r) is replaced by the following:

'(r) The competition and regulatory framework shall be improved. Portugal shall reinforce the independence and resources of the main national regulatory authorities; implement the competition law with a view to improving the speed and effectiveness of enforcement of competition rules; and monitor the inflow of new cases and report on the functioning of the specialised court for Competition, Regulation and Supervision.';

(m) point (u) and (v) are deleted.

(2) Paragraph 8 is replaced by the following:

'8. With a view to restoring confidence in the financial sector, Portugal shall adequately recapitalise its banking sector and ensure an orderly deleveraging process. In that regard, Portugal shall implement the strategy for the Portuguese banking sector agreed with the Commission, the ECB and the IMF a so that financial stability is preserved. In particular, Portugal shall:

(a) advise banks to strengthen their collateral buffers on a sustainable basis and monitor the issuance of the government guaranteed bank bonds, which has been authorised up to EUR 35 billion in line with Union State aid rules;

(b) ensure that banks reach the programme target of the Core Tier 1 ratio of 10 % at the latest by end-2012. The capital requirements stemming from valuing sovereign debt based on market prices according to the EU-wide recapitalisation exercise co-ordinated by the the European Banking Authority shall be met in June 2012 together with the capital implications resulting from the special on-site inspections programme and the transfer of the banks' pension funds to the State social security system. The EUR 12 billion bank solvency support facility established under the Programme should be made available if banks cannot reach the capital requirement thresholds within the deadlines set;

(c) ensure a balanced and orderly deleveraging of the banking sector, which remains critical to eliminating funding imbalances on a permanent basis. Banks' funding plans aim at a reduction in the loan-to-deposit ratio to an indicative value of around 120% by the end of the Programme and eventually a reduction of the reliance on Eurosystem funding during the duration of the Programme. These funding plans shall be reviewed quarterly;

(d) ensure that the state-owned Caixa Geral de Depósitos (CGD) is streamlined to increase the capital base of its core banking arm as needed. The sale of its insurance and health arms shall take place before end-2012, while the sale of non-strategic equity stakes is ongoing. Insofar as these needs cannot be met from internal group sources by end-June 2012, CGD shall be provided with government capital support from cash buffers outside the bank solvency support facility;

(e) optimise the process for recovering the assets transferred from BPN to the three state-owned SPVs through the outsourcing of the management of the assets to a professional third party, with a mandate to gradually recover the assets over time. Select the party managing the assets through a competitive bidding process and include proper incentives to optimize the recoveries into the mandate;

(f) complete a proposal for encouraging the diversification of financing alternatives to the corporate sector by end-July 2012;

(g) implement measures to conclude the setting-up of the Resolution Fund with a view to ensuring that it is fully operational by July 2012; to adopt the supervisory notices on recovery plans by end-July 2012 and adopt the regulation on resolution plans by end-October 2012**,** adopt the rules applicable to setting-up and operation of bridge banks in line with EU competition rules by end September 2012. Priority will be given to the review of the recovery and subsequent resolution plans of the banks that are of systemic importance;

(h) establish a framework for financial institutions to engage in out-of-court debt restructuring for households and SMEs.'

Article 2

This Decision is addressed to Portugal.

Article 3

This Decision shall be published in the *Official Journal of the European Union.*

Done at Brussels,

For the Council
The President