DECISIONS

COUNCIL IMPLEMENTING DECISION

of 9 October 2012

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

(2012/658/EU)

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 [2], the Commission, together with the International Monetary Fund (IMF) and in liaison with the European Central Bank (ECB), has conducted the fifth review of the Portuguese authorities' progress on the implementation of the agreed measures under the economic and financial adjustment programme (Programme) as well as of their effectiveness and economic and social impact.

(2) The rebalancing of the Portuguese economy is taking place at a faster-than-expected pace. The second quarter of 2012 brought a substantial quarter-on-quarter real gross domestic product (GDP) contraction of 1,2 % following a flat first quarter. For the year as a whole, the projected pace of the economic recession remains unchanged at – 3 %. The current account deficit is declining more rapidly than anticipated, falling to 3 % of GDP in 2012 from nearly 10 % just two years ago. This adjustment is taking place on the back of well-performing exports and a rapid fall in imports. Looking forward, economic activity will be affected by a diminishing stimulus from external demand and the impact of further budgetary consolidation. Consequently, GDP growth has been revised downward by about 1 percentage point in both 2013 and 2014 to around – 1 % and + 1 %.

(3) In spite of a rigorous budget implementation on the expenditure side, data until July point to a budgetary gap of 1¾ % of GDP in 2012 compared with the budget plans. While the faster-than-projected adjustment from domestic demand to exports is welcome, it impacts on budgetary execution in two ways. First, employment-intensive domestic sectors, such as construction, are affected most negatively and the resulting higher unemployment weighs on social security budgets. Second, the tax-intensity of production and consumption is falling, leading to noticeable revenue shortfalls. The growth composition effect on revenue is compounded by intra-category shifts away from higher-taxed items such as consumer durables towards lower-taxed items of daily consumption. Also, the weakness in direct taxation is exacerbated by negative bracket creep as falling incomes are taxed at lower rates and tax revenue on profits shrink. By contrast, expenditure has overall developed according to plans, with higher-than-budgeted savings on compensation for employees. Budgetary execution is also benefitting from lower-than-expected interest payments and the reprogramming of Union Structural Funds. Although some one-off factors could reduce the gap to about ¾ % of GDP in 2012, a large carry-over into 2013 and 2014 of approximately 1½ % of GDP would remain, making the fiscal programme targets over 2012-2014 unattainable.

(4) In view of the large revenue shortfalls and the more subdued growth outlook, the deficit targets haven been adjusted to 5,0 % of GDP in 2012, 4,5 % in 2013 and 2,5 % of GDP in 2014. As the fiscal gap is assessed to be essentially outside the control of the government, a revision of the targets to accommodate part of the shortfall seems appropriate. Even under the revised targets, significant consolidation efforts of 3 % and 1¾ % of GDP will be necessary in 2013 and 2014 respectively. In order to maintain the credibility of the Programme, some degree of front-loading of the adjustment is warranted.

(5) A range of structural spending and revenue measures underpin the revised fiscal targets. Measures worth ¼ % of GDP should still be taken in 2012 in order to reach the target of 5 % of GDP. This includes, inter alia, spending freezes and a frontloading of some of the measures planned for 2013. For 2013, consolidation measures amounting to 3 % of GDP should be incorporated in the budget in order to achieve the target of

[1] OJ L 118, 12.5.2010, p. 1.
[2] OJ L 159, 17.6.2011, p. 88.

4,5 % of GDP. These include a further decrease in the wage bill mainly through the reduction of the number of public employees, a reduction in intermediate consumption, a cut in social transfers, a further rationalisation in the health sector, reduced spending on capital formation, as well as revenue increases achieved via a reform of the personal income tax simplifying the tax structure, broadening the base by eliminating some tax benefits, increasing the average tax rate while improving progressivity, broadening the corporate income tax base by eliminating interest deductibility, raising excise taxes and changing property taxation. For 2014, a comprehensive expenditure review has been initiated with a view to identifying spending cuts (of EUR 4 billion over two years) in order to reach a budget deficit of 2,5 % of GDP.

(6) Instruments to control government expenses are being put in place. The new commitment control system is being implemented but full compliance needs to be ensured so as to avoid a further build-up of new arrears. Budgetary fragmentation should be reduced and costly inefficiencies are being tackled across a broad range. This includes containing losses of State-owned enterprises (SOEs), renegotiating public-private partnerships (PPP) and pushing for further savings in the health sector.

(7) Under the Commission's current projections for nominal GDP growth (– 1,0 % in 2011, – 2,7 % in 2012, 0,3 % in 2013 and 2,2 % in 2014) and the revised fiscal targets, the path for the debt-to-GDP ratio is expected as follows: 107,8 % in 2011, 119,1 % in 2012, 123,7 % in 2013 and 123,6 % in 2014. The debt-to-GDP ratio would therefore be stabilised at below 124 % and be placed on a declining path in 2014, assuming further progress in the reduction of the deficit. Debt dynamics are affected by several below-the-line operations, including sizeable acquisitions of financial assets, in particular for possible bank recapitalisation and financing to SOEs and differences between accrued and cash interest payments.

(8) The liquidity and the solvency conditions of the banking system have improved since the fourth review, reflecting the ongoing deleveraging, the exceptional liquidity support provided by the Eurosystem, and a capital augmentation worth over EUR 7 billion. Banks presented their updated funding and capital plans (4th edition). Albeit slightly less optimistic on deposits growth, all banks foresee to meet the indicative loan-to-deposit target of 120 % by 2014. Overall, the implementation of the Memorandum of Understanding on Specific Economic Policy Conditionality (Memorandum of Understanding) on the financial sector part is proceeding in accordance with the envisaged objectives to preserve financial stability. Efforts are still needed in some banks to meet the end of the year target for 2012 of the Banco de Portugal of a Core Tier 1 ratio of 10 %.

(9) Progress in the implementation of reforms to raise competitiveness, employment and the growth potential is broadly satisfactory. The revised Labour Code entered into force in August 2012. Further important reforms in the area of severance payment and collective bargaining are planned by the end of September 2012. The Portuguese Government has recently adopted a number of active labour market policies aimed at improving the functioning of public employment services, supporting employment creation, strengthening activation and offering more effective training opportunities. The judiciary reforms in the areas of civil procedure and court organisation, which will speed up civil and commercial litigation and unclog the court system, are progressing well. Steps have been taken to improve the framework for the recognition of professional qualifications with the adoption of amendments to the law transposing Directive 2005/36/EC of the European Parliament and of the Council of 7 September 2005 on the recognition of professional qualifications [1] and with the adoption by the Portuguese Government of a law proposal aimed at improving the functioning of highly regulated professions. Work on the implementation of Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market [2] has advanced at a steady pace as regards sector-specific legislation, with the adoption of the remaining necessary sector-specific legislative amendments expected by the end of 2012. Further efforts in the implementation of the Zero Authorisation initiative and the set-up of the Point of Single Contact provided for in Directive 2006/123/EC are essential to reduce the administrative burden. With a view to facilitating access to finance to small and medium-sized enterprises (SMEs), the Portuguese Government is committed to adopt, if necessary, a number of additional initiatives, including mechanisms to strengthen the export orientation of SMEs.

(10) Building on the independent report on the main national regulator authorities, Portugal will prepare a framework law that protects the public interest and promotes market efficiency. The framework law shall guarantee the regulators' independence and financial, administrative and

[1] OJ L 255, 30.9.2005, p. 22.
[2] OJ L 376, 27.12.2006, p. 36.

management autonomy to exercise their responsibilities, in full compliance with Union law. The framework law shall also contribute towards the effectiveness of the Competition Authority in enforcing competition rules, thereby supporting and complementing the effect of the recently adopted Competition Law.

(11) The fifth update of the Memorandum of Understanding includes a full section on promoting a business-friendly licensing environment which provides a more detailed calendar and specific milestones in the revision of some important legal regimes such as environment and territorial planning, industrial, commercial and tourism licensing.

(12) In the light of these developments, Implementing Decision 2011/344/EU should be amended,

HAS ADOPTED THIS DECISION:

Article 1

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

(1) paragraphs 3 and 4 are replaced by the following:

‘3. The general government deficit shall not exceed 5,9 % of GDP in 2011, 5,0 % in 2012, 4,5 % of GDP in 2013 and 2,5 % of GDP in 2014 in line with the revised excessive deficit procedure requirements. For the calculation of this deficit, the possible budgetary costs of bank support measures in the context of the Portuguese Government’s financial sector strategy shall not be taken into account. Consolidation shall be achieved by means of high-quality permanent measures and minimising the impact of consolidation on vulnerable groups.

4. Portugal shall adopt the measures specified in paragraphs 5 to 8 before the end of the indicated year, with exact deadlines for the years 2011-2014 being specified in the Memorandum of Understanding. Portugal shall stand ready to take additional consolidation measures to reduce the deficit to below 3 % of GDP by 2014 in case of deviations from targets.’;

(2) paragraphs 6 to 9 are replaced by the following:

‘6. Portugal shall adopt the following measures during 2012, in line with specifications in the Memorandum of Understanding:

(a) the general government deficit shall not exceed 5,0 % of GDP in 2012. Portugal shall continue to closely monitor fiscal developments and implement further policy adjustments to achieve the 2012 target. To this effect, Portugal shall freeze some of the 2012 budget appropriations for investment projects not yet initiated; increase stamp duties on high value properties; raise tax rates on investment income; frontload some of the 2013 budget measures affecting social benefits; implement additional measures generating savings in intermediate consumption and raising other revenues in order to secure the deficit target for 2012;

(b) Portugal shall aim to reduce expenditure in 2012 by at least EUR 6,8 billion including by reducing public sector wages and employment; making cuts in pensions; carrying out a comprehensive reorganisation of the central administration, eliminating redundancies and other inefficiencies; reducing transfers to SOEs; reorganising and reducing the number of municipalities and parishes; making cuts in education and health; lowering transfers to regional and local authorities; and reducing capital expenditure and other expenditure as set out in the Programme;

(c) on the revenue side, Portugal shall implement revenue measures of at least EUR 3 billion, including by broadening VAT bases through the reduction of exemptions and the rearranging of the lists of goods and services subject to reduced, intermediate and higher rates; increasing excise taxes; broadening the corporate and personal income tax bases by reducing tax deductions and special regimes; ensuring the convergence of personal income tax deductions applied to pensions and labour income; and changing property taxation by substantially reducing exemptions. These measures shall be complemented by action to fight tax evasion, fraud and informality;

(d) Portugal shall continue adopting 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 the reporting and monitoring of public finances and reinforce budgetary execution rules and procedures. The Portuguese Government shall apply the strategy for the validation and settlement of arrears and step up the implementation of the commitment control law to prevent the creation of new arrears. Portugal shall implement the new legal and institutional PPPs framework. No PPP shall be launched until the new framework is fully effective. Based on a study prepared by an international auditing firm, Portugal shall develop a detailed strategic plan, in full compliance with applicable Union law including public procurement law, with a view to obtaining substantial fiscal gains, while minimising the debt burden and ensuring sustainable reduction of government liabilities. Portugal shall adopt a law to regulate the creation and the functioning of SOEs at central, regional and local levels;

(e) Portugal shall apply the new legislation to reorganise and significantly reduce the number of local government entities. These changes shall come into effect by the beginning of the next local election cycle. In addition, Portugal shall enhance efforts to streamline the public sector by reducing entities and improving task sharing at all levels of government;

(f) Portugal shall deepen the reform of the revenue administration by reinforcing the links between the Autoridade Tributária e Aduaneira and the revenue collection units of the Social Security, reducing the number of municipal offices and addressing remaining bottlenecks in the tax appeal system;

(g) Portugal shall implement the financial arrangement with the RAM;

(h) Portugal shall adopt measures to improve the efficiency and sustainability of SOEs at central, regional and local level. Portugal shall explore options in order to manage the heavy debt load of SOEs, including Parpública, and to ensure improved conditions for market financing. Portugal shall aim to reach operational balance at sector level by the end of 2012;

(i) Portugal shall continue implementing the privatisation programme. The direct sale of Caixa Geral de Depósitos' (CGD) insurance arm, Caixa Seguros, is ongoing;

(j) the Portuguese Government shall submit draft legislation to the Portuguese Parliament to align severance payments with the Union average of 8 to 12 days per year of work and to create a compensation fund for severance payments;

(k) Portugal shall promote wage developments consistent with the objectives of fostering job creation and improving firms' competitiveness with a view to correcting macroeconomic imbalances. Over the Programme period, any increase in minimum wages shall take place only if justified by economic and labour market developments. Measures shall be taken to address weaknesses in the current wage bargaining schemes, including legislation to redefine the criteria and modalities of the extension of collective agreements and to facilitate firm-level agreements. Until then, collective agreements shall not be extended;

(l) Portugal shall continue to improve the effectiveness of its active labour market policies in line with the results of the assessment report and the action plan to improve the functioning of the public employment services;

(m) Portugal shall implement the measures set out in its action plans to improve the quality of secondary and vocational education and training;

(n) the functioning of the judicial system shall be improved by implementing the measures proposed under the Judicial Reform Map and by applying targeted measures to progressively eliminate the court backlog and to foster alternative dispute resolution;

(o) Portugal shall continue opening up its economy to competition. The Portuguese Government shall take the necessary measures to ensure that obstacles to free movement of capital will not be created by their action and, in particular, that the Portuguese State or any public body does not conclude, in a shareholder capacity, agreements which may hinder the free movement of capital or influence the management control of companies. The functioning of professional services shall be fostered by improving the framework for recognition of professional qualifications and by eliminating unnecessary restrictions on regulated professions. In construction and real estate activities, Portugal shall make the requirements for cross-border providers less burdensome and review obstacles to the establishment of service providers;

(p) the competition and regulatory framework shall be improved. Portugal shall reinforce the independence, autonomy and governance of the main national regulatory authorities; implement the Competition Law with a view to improving the speed and effectiveness of the 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;

(q) in the energy sector, Portugal shall take measures to facilitate market entry and promote the establishment of the Iberian gas market and shall take further steps towards fully transposing the Third EU Energy Package. To ensure the independence and autonomy and powers of the national regulatory authority provided for in the Third EU Energy Package, Portugal shall adopt the new regulators' by-laws, as agreed in July 2012 with the Commission, the ECB and the IMF, by the third quarter of 2012, and shall ensure that they are effective before the end of 2012 in time for the liberalisation of the electricity and gas market. Portugal shall take measures to review the support and compensation schemes for the production of electricity. Portugal shall take measures to reduce excessive rents and eliminate the tariff debt by 2020, focusing on compensation schemes for power guarantee, special regime (renewables — excluding those granted under tender mechanisms — and cogeneration), and the ordinary regime (CMECs and CAEs);

(r) in other network industries, in particular transport, telecommunications and postal services, Portugal shall adopt additional measures to promote competition and flexibility;

(s) Portugal shall adopt a number of measures with a view to increase the efficiency of the licensing schemes for territorial planning, industrial and commercial licensing and tourism. In addition, the Portuguese Government shall analyse and fast-track applications for the licensing of planned investment projects which are left unresolved or undecided for more than 12 months;

(t) Portugal shall prepare an action plan with measures to facilitate access to finance and to export markets for companies, in particular for SMEs.

7. Portugal shall adopt the following measures during 2013, in line with specifications in the Memorandum of Understanding:

(a) the general government deficit shall not exceed 4,5 % of GDP in 2013. The 2013 budget shall include permanent consolidation measures of at least 3 % of GDP aiming at reducing the general government deficit within the timeframe referred to in paragraph 3. The Portuguese Government shall explore ways to increase the weight of expediture reduction in the overall consolidation package for 2013 in order to ensure a medium-term growth-friendly fiscal adjustment tilted towards the expenditure side. The Portuguese Government shall use contingency measures in the course of 2013 in case of slippages given possible implementation risks;

(b) the 2013 budget shall include revenue measures such as reforming the personal income tax by simplifying the tax structure, broadening the tax base through the elimination of some tax benefits and increasing the average tax rate while improving progressivity; broadening the corporate income tax base, increasing investment income tax rate; increasing excise taxes and introducing changes in property taxation;

(c) on the expenditure side, the 2013 budget shall identify measures such as lowering expenditure in the central administration, education, health and social benefits; streamlining public and private social transfers and subsidies; reducing transfers to local and regional authorities; reducing the wage bill by decreasing permanent and temporary staff and reducing overtime pay; and lowering operational and capital expenditures by SOEs;

(d) Portugal shall complete the elimination of the court backlog;

(e) Portugal shall improve the business environment by reducing administrative burden through the extension of simplification reforms [Points of Single Contact (PSC) and “Zero Authorisation” projects] to all sectors of the economy. In particular, Portugal shall adapt the content and the information available at the PSC to ensure compliance with Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market (*) and with Directive 2005/36/EC of the European Parliament and of the Council of 7 September 2005 on the recognition of professional qualifications (**). Portugal shall alleviate the credit constraints of SMEs, including through the implementation of Directive 2011/7/EU of the European Parliament and of the Council of 16 February 2011 on combating late payment in commercial transactions (***);

(f) Portugal shall adapt the content and the information available at the PSC in respect of the rules applicable to the 44 specific sectors that were amended to ensure compliance with Directive 2006/123/EC, and shall adapt the content and information available at the PSC in respect of the rules applicable to the 13 specific sectors that were amended to ensure compliance with Directive 2005/36/EC;

(g) Portugal shall continue implementing its privatisation programme, which shall be expanded to include additional companies and assets to the ones identified in the Memorandum of Understanding for sale or concession in 2013.

8. The general government deficit shall not exceed 2,5 % of GDP in 2014. To achieve this objective, Portugal shall apply a thorough expenditure-reducing plan worth approximately EUR 4 billion over 2014-2015. A comprehensive expenditure review to fully specify the additional sources of savings shall be carried out for the sixth review and measures shall be fully specified by February 2013. The fiscal consolidation plans for 2014-2015 shall be fully defined in the 2013 Stability Programme.

9. With a view to restoring confidence in the financial sector, Portugal shall aim to maintain an adequate level of capital in 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 so that financial stability is preserved. In particular, Portugal shall:

(a) advise banks to strengthen their collateral buffers on a sustainable basis;

(b) ensure that banks reach the Programme target of the Core Tier 1 ratio of 10 % at the latest by the end of 2012;

(c) ensure a balanced and orderly deleveraging of the banking sector, which remains critical in permanently eliminating funding imbalances. Banks’ funding plans aim at reducing the loan-to-deposit ratio to an indicative value of approximately 120 % in 2014 and reducing the reliance on Eurosystem funding in the medium-term. Those funding plans shall be reviewed quarterly;

(d) continue to streamline the State-owned CGD;

(e) optimise the process for recovering the assets transferred from BPN to the three State-owned special purpose vehicles through the outsourcing to a professional third party of the management of the assets, with a mandate to gradually recover the assets over time. The Portuguese Government shall select the party managing the credits through a competitive bidding process and include adequate incentives to maximise the recoveries and minimise operational costs into the mandate. The Portuguese Government shall ensure timely disposition of the subsidiaries and the assets in the other two State-owned special purpose vehicles;

(f) on the basis of the set of preliminary proposals to encourage the diversification of financing alternatives to the corporate sector presented, develop and evaluate the different options put forward with a view to setting priorities. The Portuguese Government shall assess the effectiveness of Union-compatible government-sponsored export credit insurance schemes with a view to taking appropriate measures to promote exports;

(g) ensure the initial and periodical funding arrangements for the Resolution Fund in two steps, first by the approval of a decree-law on the banks' contributions to the Resolution Fund by November 2012, and secondly by the approval of a supervisory notice on the specific periodic contributions by banks one month later; adopt the supervisory notices on recovery plans by the end of October 2012; adopt the regulation on resolution plans by the end of November 2012; and adopt the rules applicable to setting-up and operation of bridge banks in line with Union competition rules by the end of October 2012. Priority shall 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 and implement an action plan to raise public awareness of the restructuring tools.

(*) OJ L 376, 27.12.2006, p. 36.
(**) OJ L 255, 30.9.2005, p. 22.
(***) OJ L 48, 23.2.2011, p. 1.';

(3) the following paragraph is added:

'10. In order to ensure the smooth implementation of the Programme's conditionality, and to help to correct imbalances in a sustainable way, the Commission shall provide continued advice and guidance on fiscal, financial market and structural reforms. Within the framework of the assistance to be provided to Portugal, together with the IMF and in liaison with the ECB, the Commission shall periodically review the effectiveness and economic and social impact of the agreed measures, and shall recommend necessary corrections with a view to enhancing growth and job creation, securing the necessary fiscal consolidation and minimising harmful social impacts, particularly on the most vulnerable parts of Portuguese society.'.

Article 2

This Decision is addressed to the Portuguese Republic.

Done at Luxembourg, 9 October 2012.

For the Council

The President

V. SHIARLY