International Monetary Fund

Portugal and the IMF

Press Release:
IMF Completes Eighth and Ninth Reviews Under an EFF Arrangement with Portugal, Approves €1.91 Billion Disbursement
November 8, 2013

Portugal: Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding

October 24, 2013

The following item is a Letter of Intent of the government of Portugal, which describes the policies that Portugal intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Portugal, is being made available on the IMF website by agreement with the member as a service to users of the IMF website.

Country's Policy Intentions Documents

E-Mail Notification
Subscribe or Modify your subscription

Portugal: Letter of Intent

Lisbon, October 24, 2013

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, DC 20431

Dear Ms. Lagarde:

1. The attached Memorandum of Economic and Financial Policies (MEFP) describes the progress made in recent months toward the objectives laid out in our program supported by the Extended Arrangement. It also updates previous MEFPs and highlights the policy steps to be taken in the months ahead.

2. We have made further progress toward the program objectives. Some delays generated by the political situation and government reshuffling over the summer, as well as new adverse rulings by the Constitutional Court on spending measures and labor reforms have been dealt with. The end-June deficit and performance criteria were met. All but one of the six structural benchmarks initially planned for the June-October period were also met, with the last one expected to be completed by end-October.

3. The macroeconomic outlook has recently improved. Growth and employment in the second quarter turned out to be better than expected, with sequential real GDP growth turning positive and unemployment falling, signaling that output may have bottomed out. Nonetheless, headwinds from private sector deleveraging and fiscal consolidation will remain significant. Though most structural reforms envisaged in the program are now in place, and are beginning to have an impact, we remain strongly committed to further reforms aimed at bolstering price and cost competitiveness and setting the basis for a strong and durable recovery. In this regard, significant steps are underway to further improve the dynamism and efficiency of the labor and product market, reduce costs for exporters, and further improve our business environment.

4. We are committed to achieving our fiscal objectives. This year's deficit target (5½ percent of GDP) is within reach, as we have tightened budget execution and taken exceptional measures to offset budget overruns earlier in the year and non-tax revenue shortfalls, some of them due to exceptional factors. As a prior action for completion of this review, we have submitted to Parliament a 2014 budget that aims at a general government deficit of 4 percent of GDP, as well as some of the necessary supporting legislation. The draft budget is, to a large extent, underpinned by the public sector reforms identified in the context of the 2013 PER, ensuring a consolidation strongly tilted towards permanent measures to reduce expenditure. Fiscal consolidation will continue in 2015, with a targeted deficit of 2½ percent of GDP.

5. We are committed to preserving financial sector stability and supporting a balanced and orderly balance sheet deleveraging in the economy. While the capital and liquidity conditions of the banking system remain adequate, Banco de Portugal (BdP) continues to vigilantly supervise the banking system in view of the challenging operating environment. Moreover, to facilitate the ongoing balance sheet adjustment, we are renewing our efforts to promote adequate funding conditions for the most productive and innovative segments of the economy, while ensuring prompt restructuring of viable firms in financial difficulties.

6. On the basis of the strength of the policies outlined in this letter, and in light of our performance under the program, we request the completion of the combined eighth and ninth reviews under the Extended Arrangement, as well as a waiver of applicability for the end-September deficit and debt performance criteria.

7. We remain confident that the policies described in the current and previous MEFPs are adequate to achieve the objectives under the program. We stand ready to take additional measures should they be needed to meet the objectives of the economic program and will consult with the IMF, the European Commission, and the ECB, in advance of any necessary revisions to the policies contained in this letter and attached Memorandum.

8. This letter is copied to Messrs. Dijsselbloem, Rehn, and Draghi.

Sincerely yours,

/s/	/s/	/s/
Paulo Portas	Maria Luís Albuquerque	Carlos da Silva Costa
Deputy Prime Minister	Minister of State and Finance	Governor of the Banco de Portugal

Attachments: 1. Memorandum of Economic and Financial Policies (MEFP)
2. Technical Memorandum of Understanding (TMU)

Attachment I. Portugal: Memorandum of Economic and Financial Policies

October 24, 2013

Macroeconomic Outlook

1. **Activity.** The near-term economic outlook has improved since the seventh review. First, output and employment surprised on the upside in the second quarter, with real GDP expanding (by 1.1 percent quarter-over-quarter) for the first time since late 2010 and the unemployment rate declining to 16.4 percent from 17.7 percent. Second, recent high frequency indicators point to some stabilization in activity and confidence. In light of this, we now expect the economy to contract by 1.8 percent in 2013, compared to 2.3 percent at the time of the seventh review, with the revision reflecting mainly a less negative contribution from domestic demand and strong growth of exports of goods and services, which however is largely offset by an upward revision of imports. Accordingly, the projected 2013 unemployment rate has been revised down from 18.2 to 17.4 percent. Output is expected to remain broadly flat for the rest of the year, and to pick up gradually during the course of 2014—consistent with growth of some 0.8 percent for the year as a whole and unemployment peaking at 17.7 percent—underpinned by a gradual pick-up in investment, conditioned on the continued alleviation of uncertainty and a sustained improvement in confidence. Reflecting still weak domestic demand, we expect headline inflation to average around 0.6 percent this year. Notwithstanding the improved near-term outlook, uncertainties remain as the drag of private sector deleveraging and fiscal consolidation on growth could turn out to be stronger than expected.

2. **External adjustment.** The current account balance has continued to adjust at a faster pace than envisaged previously. It is now projected to turn into a surplus of about 1 percent of GDP this year (compared to an expected 0.3 percent of GDP at the time of the seventh review) and remain at that level next year, bringing the cumulative adjustment since 2009 to some 12 percent of GDP. The revision is largely driven by higher exports—including tourism receipts that increased by 8 percent in January through July. Strong demand from non-EU trading partners and an improvement in Portugal's export market shares in most markets continue to underpin robust export growth. In the short term, weaker demand from trading partners remains the main downside risk to these projections. Although most structural reforms envisaged in the program are now in place and are beginning to have an impact, maintaining robust export growth over the medium term will require continued improvement in external competitiveness.

Fiscal Policy

3. **2013 Budget Execution.** While the end-June quantitative performance criteria on the general government cash balance and debt were met, we need to overcome a number of budgetary challenges. Overall, we expect to meet our annual deficit target (5½ percent of GDP, excluding the BANIF recapitalization costs of 0.4 percent of GDP), but with an unfavorable net carry-over from

the 2013 budget execution to 2014 of some 0.4 percent of GDP and the need to rebuild a budgetary reserve (0.3 percent of GDP). Specifically:

- Budgetary overruns and revenue shortfalls totaling about 0.8 percent of GDP reflect a combination of one-off factors (0.2 percent of GDP) stemming from a shortfall in the reprogrammed EU funds and delays in the planned port concession, as well as pressures (0.6 percent of GDP) from increased contributions to the EU budget, the transfer to Greece of the income from the Greek bond holdings in Banco de Portugal's investment portfolio (consistent with the Eurogroup agreement), shortfalls in contributions to the public pension scheme, and overruns in wages and intermediate consumption. In addition, despite efforts to apply the commitment control law, slippages in the health sector are causing a net accumulation of arrears in SOE hospitals (some €300 million year-to-date).

- Nevertheless, the use of the provisional budget allocation (0.3 percent of GDP), the reduction in funds available to the line ministries (0.1 percent of GDP), and recourse to a one-off tax and social security contribution debt recovery scheme (0.4 percent of GDP) should offset these deviations.

Under these assumptions, underlying structural primary adjustment would reach nearly 0.5 percent of GDP.

4. **Fiscal path for 2014-15.** We remain committed to achieving our 2014 deficit target of 4 percent of GDP in 2014—consistent with a structural primary adjustment of 1 percent of GDP. To achieve these objectives while arresting the accumulation of domestic arrears, measures of around 2.3 percent of GDP will be needed in 2014. Most of these measures have been drawn from the public expenditure review (PER—see below). We have submitted the Budget Law to Parliament on October 15 as a *prior action* for the completion of this review. Fiscal consolidation will continue in 2015, with a targeted structural primary adjustment of about 1 percent of GDP.

5. **Public Expenditure Review (PER).** We modified the package of expenditure reforms initially identified in the context of the PER to reflect consultations with social partners as well as the recent developments, including an adverse Constitutional Court ruling. The reforms are proceeding. The expected yield of the PER package is now €3.1 billion (net of reduced income taxes and social contribution collections) or €2.9 billion when including the upfront costs of mutual agreements terminations in 2014. There was a rebalancing of the package toward sector-specific measures. Savings will be generated mainly by limiting outlays on the public wage bill and pensions—which account for over two-thirds of primary spending and where Portugal spends more in comparison to peer countries—as well as sector-specific reforms, with a view to increase equity and efficiency in the provision of social transfers and public services. The underlying reforms are organized around three main pillars: (i) a wage bill reform, (ii) a pension reform, and (iii) sector-specific savings.

a. ***PER—wage bill reform.*** The overall objective of the wage bill reform (0.9 billion in net savings) will be to (i) reduce the size of the public sector workforce—addressing excessive employment in particular sub-sectors—while tilting its composition toward high-skilled and

better-trained civil servants; (ii) ensure convergence of the public sector work rules and regulations toward private sector legal regimes (including regarding working hours, working time arrangements, and holiday entitlements); (iii) increase beneficiaries' contributions to ensure self-sustainability of public sector health subsystem; and (iv) simplify the remuneration policy by implementing a single wage scale and streamlining the wage supplement scale. The reduction in the workforce will be achieved through a combination of policies, including lower replacement of retirees, voluntary separations (scheme launched on September 1), and use of the redesigned mobility pool. The increase in working hours to 40-hours per week will also help, while generating efficiency gains more broadly. The current status of the various legislative changes needed to implement these reforms is as follows :

i. The Law aligning the working hours of the public sector to the 40 hours in force in the private sector was already approved. It is now under consideration by the Constitutional Court.

ii. Following the consultations with social partners, the new draft public administration labor law—aiming at aligning current public employment regime to the private sector rules, including for working hours and holiday time—will be submitted to Parliament by end-October (*structural benchmark*).

iii. The draft law on the redesigned mobility pool was also submitted and approved by Parliament, but subsequently deemed unconstitutional by the Constitutional Court and returned to Parliament for amendments. We have redesigned the scheme and the revised draft law now awaits parliamentary approval.

iv. The single wage scale reform and the reduction to the wage supplements will be made effective by January 1, 2014, implemented through a budget provision (*prior action*). A report on a more comprehensive reform of wage supplements is expected by end-December.

b. ***PER—pension reform.*** A pension reform is expected to generate 0.6 billion of net savings. It is based on equity principles with preservation of minimum socially-acceptable income levels, thus protecting those who earn the lowest pensions. Specifically, the reform takes into consideration the need to reduce the current differences between the civil servants' regime and the general social security regime, aiming at enhancing the fairness of the overall pension system. Moreover, while reforms implemented over the past two decades have contributed to long-term sustainability, the amount of pension benefit payments for which the government is currently liable makes the system excessively costly under the current circumstances reassessing the need to take into account demographic developments. Accordingly, the reform is based on three main elements: (i) an effective increase by one-year in the statutory retirement age to 66 years—implemented by adjusting the demographic sustainability factor (*prior action*); (ii) aligning the rules and benefits of the public sector pension funds, CGA, to the general pension regime by changing one of the replacement rate parameters from about 90 to about 80 percent for all applicable beneficiaries, while avoiding double penalization of CGA

beneficiaries, with a pension below €5,030, with the CES contribution *(structural benchmark*), and (iii) means testing survivors' pensions of both CGA and the general pension regime, in cases where these accumulate with other pensions. Each of these reforms is implemented through modifications to the relevant laws. The necessary legislative proposals have been submitted to Parliament.

c. ***Sector-specific expenditure savings.*** Other savings under the PER (1.65 billion of net savings) are generated through a combination of sector-specific reforms, which mainly include intermediate consumption cuts and targeted nonrenewals of fixed-term contracts. Additional cutbacks in SOE and PPP expenditure are generated through further negotiation and operational restructuring. In the education sector for example, rationalization of the school network and a convergence of the key indicators, namely class size, towards peer levels are at the core of our reforms. In the health sector, savings come from further restructuring of the hospital network.

6. **Additional measures.** Due to the negative carryover from the 2013 budget execution and upward expenditure pressures, the PER measures need to be complemented by permanent measures amounting to €0.6 billion (0.4 percent of GDP) to achieve the budget deficit of 4.0 percent in 2014. These include new revenue measures (on company cars, online gambling, diesel passenger cars, alcohol and tobacco, banking, and media spectrum), a reduction of fiscal benefits for pension and real estate funds and a special levy on the energy sector (with revenues in excess of €100 million to be used to reduce the electricity tariff deficit). A number of one-off operations (including port concessions, sales of excess oil reserves, and a transfer from the CTT health fund) adding to €0.4 billion (0.2 percent of GDP) will also contribute to achieving our deficit target, more than offsetting the one-off upfront costs related to the mutual agreements for termination of public sector employment contracts (by about 0.1 percent of GDP).

7. **Legal safeguards.** To mitigate legal risks from future potential Constitutional Court rulings, we will continue to respect the following principles. First, expenditure reforms will be designed with the principle of public/private sector and intergenerational equity in mind as well as the need to address the sustainability of social security systems. Second, legislation underpinning the expenditure reforms will be duly justified on compliance with the fiscal sustainability rules in the recently-ratified European Fiscal Compact, which now ranks higher than ordinary legislation. Third, the government will rely as much as possible on general laws—rather than on one-year budget laws—consistent with the structural nature of the reforms. This also allows the possibility of prior constitutional review of the said laws, thus permitting early reaction on the part of the government in case these reforms raise constitutional issues.

8. **Debt Path.** Under the programmed fiscal path, gross debt is set to peak at close to 128 percent of GDP in 2013 (or at about 122 percent of GDP net of IGCP's projected deposits in 2014). The increase in the debt peak vis-à-vis the seventh review is explained by the suspension of the transfer of the State's CGD shares to Parpública, by the postponement of the reallocation of the Social Security portfolio from foreign assets to government securities, now scheduled to be completed by end-2014, and by a higher projected Treasury cash balance at end-2013.

9. **CIT Reform.** We have launched a far-reaching reform of the Portuguese corporate income tax (CIT) regime aimed at boosting investment and growth. The reform committee presented in July 2013 its recommendations. They consist in simplifying the CIT regime through a broadening of the tax base, the gradual lowering of the rate, the reduction of multiple surcharges, and the rationalization of the incentive schemes. The report also focuses on steps enhancing legal stability, lowering compliance costs, and aiming at reducing litigation. In addition, measures are proposed to improve the international competitiveness of the tax and strengthen the territorial approach, including through the adoption of a universal participation exemption regime (while respecting international standards). The reform would also envisage reducing policy-induced debt bias. It will be implemented within the existing budgetary envelope. A draft law on the CIT reform has already been submitted to Parliament.

Containing Fiscal Risks

10. **Public Financial Management.** We have made further progress in advancing our Public Financial Management reform, but controlling domestic arrears remains challenging, particularly in the health sector. Important steps have been taken in transposing the EU economic and governance fiscal framework. The process will be completed by the first quarter 2014, along with further changes to streamline budgetary procedures. In parallel, we will identify the operational changes necessary to ensure full implementation of the BFL in a draft action plan to be prepared by the eleventh review. We will publish a tax expenditure report as well as a comprehensive Fiscal Risks Report together with the Budget Law. We remain committed to reverting the accumulation of new domestic arrears, the stock of which amounted to €2.9 billion at end-July 2013. While we will proceed with a second settlement program in the health sector—in the value of €432 million—following the same procedures envisaged in the March 2012 strategy document, we are concurrently working with the enforcement authorities in order to effectively sanction public officials who do not comply with the commitment law. Moreover, we are strengthening our efforts to rein in expenditures in this sector through appropriate budgeting and ensuring effective savings measures.

11. **Revenue Administration.** We have completed the property revaluation process—with approximately 5 million properties revalued—a key measure of the 2013 budget. To bolster revenue performance in support of our medium-term fiscal objectives, we remain determined to make further progress in curbing tax evasion. Recent steps in this direction included making fully operational the new Large Taxpayer Unit and conducting successfully a VAT invoicing reform. To limit the impact of the tax and social security contribution debt recovery scheme announced in early October, we have publicly committed not to have recourse to such new schemes in the future and will tighten sanctions for criminal offenders. Looking ahead, key steps to strengthen compliance will include (i) phasing in of a modern compliance risk model, including by establishing a Risk Management Unit; (ii) strengthening PIT compliance management—the pilot projects on the High Net Wealth Individuals and the Self-employed Professionals, and strengthened control of the monthly PIT withholding information, are key instruments in this respect; and (iii) further modernizing tax litigation, building on the results obtained so far.

12. **Public Administration**. Streamlining public administration continues to be a government priority. We have made significant progress in reducing the size of the public sector, reducing the number of public employees by 6 percent since end-2011, reaching our 2-percent annual average target ahead of time. The next step in our reform agenda is the adoption of a general public administration law and other PER reforms to modernize and rationalize public administration (see paragraph 5).

13. **State-Owned Enterprises.** Despite the negative financial impact from the reinstatement of the 13th and 14th month salaries due to the Constitutional Court rulings, cost-reduction efforts and voluntary redundancy programs have moved enterprises significantly closer to operational balance. Looking ahead, we will maintain formal cost-cutting objectives for those firms still showing operating deficits, while other firms will be required to continue improving operating balances with a view to reducing debt burdens and financial costs. We also continue to manage the high debt burdens of some firms, and treasury support has remained within the envelope of budgeted transfers. To further strengthen SOE governance, the Council of Ministers approved in August a Decree-Law which concentrates all shareholder functions in the Ministry of Finance along with the creation of a dedicated Technical Unit. The law also reinforces the monitoring of SOE debt by centralizing borrowing decisions at the Debt Management Agency (IGCP). The unwinding of most derivative contracts of SOEs during 2013 also contributed to reduce significantly financial costs and risks.

14. **Privatization**. The privatization program is broadly on track, and proceeds have exceeded the initial program target. The sale of the airport operator, ANA, has now been formally completed. While preparing the changes in the legal framework for postal services, we have launched the privatization process for the postal company CTT, and expect to receive binding offers by end-2013. The sale of the airline, TAP, however, is still on hold, after the initial privatization plan fell through at end-2012 due to inadequate financial assurances by the final bidder. We are actively seeking buyers for the group as a whole and the process will be re-launched in the near future. The privatization of the rail cargo firm, CP Carga, has also been postponed with a view to maximizing market value while restoring its operating balance. We have prepared a strategic plan for the water and waste sectors, with a view to improving their efficiency, including by introducing private capital and management in the system. Binding offers for the sale of the waste management business are currently anticipated for the first quarter of 2014. Opening water concessions to private capital and management is expected to take longer. The government will further consider expanding the privatization program to include additional assets for sale or concessions.

15. **Public-Private Partnerships (PPPs).** We have taken further steps to achieve a fiscally-responsible PPP model. First, we have launched a major renegotiation of road PPPs. The objective is to generate permanent savings by rationalizing OPEX, CAPEX, and the private partner's internal rate of return. In the case of sub-concessions, savings will be generated by also reducing the scope of the relevant contracts. MoUs have now been signed with most concessionaires, offering good prospects for reaching the revised savings goal of €300 million in 2013, consistent with the supplementary budget. Second, the Ministry of Finance PPP unit is gaining a pivotal role, working

towards enhancing fiscal transparency, improving reporting on PPPs, and expanding its field of action to other sectors, namely health and security, and advising the autonomous region of Madeira. Finally, the ongoing revision of the regulatory framework for the road and rail sector is also part of the strategy to achieve sustainability in these sectors, by reducing operation, maintenance and major repair requirements in line with EU standards. This revision is to be completed by end-October.

16. **Regional and Local Governments.** The Regional and Local Finance Laws were approved by Parliament and published in September. They will improve the inter-governmental fiscal framework, notably by applying the same principles of the Budgetary Framework Law to subnational governments. Moreover, we have streamlined the organization of Parishes, significantly reducing their number. The establishment of a coordination council between the central and subnational governments is expected to enhance the exchange of information in order to support budgetary planning. The credit line to support local governments' arrears settlement is being implemented, following the necessary procedures to validate the claims. The regional government of Madeira's program with the State is broadly on track, but we will continue to closely monitor budgetary risks.

Safeguarding Financial Stability

17. **Bank supervision.** While compliance of the banking system with regulatory capital remains satisfactory, the challenging operating environment warrants continued vigilance. Against this backdrop, the BdP is pursuing various initiatives that seek to further strengthen banks' resilience, and maintain financial stability.

- *Credit Impairment Review*. Following two earlier on-site inspection programs in 2011 and 2012, the BdP has successfully completed a new credit impairment review, with the support of the participating banks' external auditors and an external consultant. The audit focused on (i) the verification of current impairment levels for a broad sample of credits, notably high-risk exposures; (ii) a follow-up of the findings identified in the original on-site inspections program related to collective impairment; and (iii) an assessment of the banks monitoring process related to the management and fair value calculation of the participation units held by the banks in restructuring funds. The limited impairment deviations identified by the review have already been addressed by the affected banks through impairment reinforcements, reflected in their end-June results. Moreover, follow-up recommendations have been issued to the banks, with all the high priority items expected to be implemented by end-December 2013.

- *Review of Restructuring Processes*. While the enhanced legal toolkit on corporate and household insolvency is now fully operational, further efforts remain necessary to promote early and effective use of the new restructuring tools. In this context, the BdP has initiated a special assessment program of banks' operational capacity in the area of loan restructuring and asset recovery, to ensure that the banking system can effectively support the balance sheet adjustment of the private sector, through timely engagement with troubled debtors before their viability is in jeopardy. The special program, which benefits from external

expertise, will evaluate the effectiveness of management processes regarding problem loans, with a special focus on early detection. The exercise will also include a broader survey of the Portuguese regulatory framework, including any remaining gaps and bottlenecks in the implementation of the new debt restructuring tools. The BdP aims to complete the special program by early November 2013.

- *Communication Strategy*. Building on experiences from the various inspection programs and to promote greater transparency on its ongoing supervisory efforts, the BdP plans to publish by mid-November minimum standards for the calculation of credit impairments, including guidance on collateral valuation. Moreover, as a follow-up to the BdP's requirements on identifying and reporting of restructured loans (Instruction No. 18/2012), banks will be required to disclose this information in their annual reports, starting in December 2013.

18. **Stress test exercise.** Banks are making progress implementing the recommendations on their stress testing methodologies and impairment projections, issued as part of the original on-site inspections program. In this context and to further enhance the rigor of the quarterly stress test exercise, the BdP has further enhanced its credit risk model used to provide methodological guidance on default probabilities to the participating banks. Moreover, the BdP is introducing a new top-down stress test to support its review of the bottom-up results. These enhancements will be included in the next round of quarterly stress tests, to be finalized in November 2013.

19. **Transition to CRD IV.** Capital requirements under the program will be set in accordance with the CRD IV package. Accordingly, as of January 1, 2014, the BdP will replace the existing targets and require banks to maintain, at a minimum, a common equity Tier 1 capital level of 7 percent, as defined in CRD IV package considering all the transitional provisions related to the definition of capital. Additional measures will also be in place to preserve banks' current capital buffers, ensuring that they remain commensurate with the challenging operating environment. The new requirements and additional measures will be included in the law transposing the CRD IV package as well as in implementation instructions from the BdP before year end. The implementation of the above framework will also need to comply with the requirements currently envisaged in the EBA Recommendation on the preservation of capital for the banks that are subject to them. We will also ensure compliance with any future regulatory initiatives at European level.

20. **BSSF.** We remain committed to providing further support to the banking sector, in the event new capital needs were to arise. While we will continue to encourage banks to seek private solutions, resources from the Bank Solvency Support Facility (BSSF) remain available to support viable banks if needed. The resources in the BSSF will solely be utilized to provide public support, if needed, to the banking system. State aid will remain subject to strict conditionality, in line with the recently amended EU state-aid rules, aimed at avoiding subsidizing private shareholders and preventing migration of private liabilities to the public sector balance sheet, while ensuring adequate lending to the real economy.

21. **Recovery and Resolution Plans.** The BdP has reviewed and issued recommendations on the recovery plans of the largest banks, and expects to receive the plans from all the other banks by

end-November 2013. Institutions for which resolution plans are mandatory have submitted the data required in the supervisory notice of December 2012, and these are currently being reviewed by the BdP. We have submitted to Parliament the necessary amendments to the recapitalization law to reflect the recent Communication from the European Commission on the Application of the State-aid Rules to Support Measures in Favor of Banks in the Context of the Financial Crisis. Moreover, we remain committed to swiftly transposing the new EU Directive on bank recovery and resolution once it has been adopted.

22. **Funding and Liquidity Conditions.** Nonstandard measures by the ECB to restore the proper transmission of monetary policy have helped ease liquidity pressures and continue to play a pivotal role in absorbing remaining funding constraints, while strengthened collateral buffers provide an important shield against potential adverse shocks. In parallel, we continue to explore with our European partners further initiatives to support funding conditions, including potential mechanisms to securitize banks' high quality mortgage and SME credit. Moreover, the new platforms recently created by the BdP for interbank secured and unsecured lending have become fully operational, supporting the functioning of the domestic interbank market.

23. **Initiatives to Promote Orderly Deleveraging.** Despite improvements in liquidity conditions, the credit situation remains challenging, especially among SMEs. In this context, banks' funding and capital plans should continue to ensure that the deleveraging process takes place in an orderly manner to achieve a stable market-based funding position, while adequate and sustainable financing is provided to the economy. To support this objective, we are stepping up our efforts to promote more efficient financing allocation to the productive segments of the economy through further enhancements to our existing government-sponsored measures, in line with EU state-aid rules, as well as the promotion of alternative private funding options for SMEs. Specifically,

- *Government-Guaranteed Credit Instruments*. We will continue to strive to improve the performance of existing government-guaranteed credit lines, in line with international best practice. On the basis of the recent external audit of the National Guarantee System (NGS), we have defined a detailed implementation plan of key policy recommendations aiming at making these schemes more efficient and minimizing risks for the State. The recommendations include (i) a review of the schemes' objectives and investment selection processes; (ii) measures to further enhance loan and guarantee pricing mechanisms in favor of end users, including through the development of competitive bidding mechanisms for the allocation of guaranteed credit to the banks, with preliminary scenarios for competitive bidding schemes to be presented and discussed by mid-November 2013; (iii) an upgrade of the NGS risk management capabilities and review of its governance structure; (iv) improved monitoring, management, and public disclosure of the State exposure to the NGS operations. We will regularly report on progress with the implementation of these measures, which are expected to be fully finalized by end-January 2014. Moreover, to support viable firms in financial difficulties, we will explore possible modalities for the provision of guaranteed credit in line with EU state aid rules, conditional on the successful completion of a corporate debt restructuring process, with an initial proposal expected by early-November. We will continue to monitor the balance sheet performance of the

firms benefiting from government-guaranteed credit lines through our newly established quarterly monitoring framework.

- *Development of SMEs Commercial Paper*. We are exploring possible changes to the regulatory environment applicable to the commercial paper market to facilitate its expansion among a wider investor base and increase the use of this alternative funding option by the corporate sector, notably SMEs. The necessary draft amendments to the existing rules are currently under discussion and are expected to be approved by the Council of Ministers by end-November.

New initiatives to facilitate credit to firms by the Ministry of Finance, Ministry of Economy, and other relevant entities will be primarily focused on streamlining and improving the efficiency of existing schemes, without creating additional burden on or posing risks to public finance. In this context, the government is conducting a stock-taking exercise aiming at streamlining and centralizing the management of EU structural funds for the 2014-2020 programming period.

24. **Central Credit Registry.** Efforts to promote information sharing, especially for SMEs, are ongoing. The BdP has recently published a new instruction requesting banks to report in the Central Credit Registry (CCR) additional loan information, including (i) as of January 2014, identification of nonperforming and restructured loans; and (ii) as of July 2014, information on government guarantees, as well as the identification of overdue and written-off loans disputed in court. Moreover, the BdP is currently finalizing a proposal for a revision of the decree law regulating the CCR to allow further enhancements, such as the inclusion of additional financial instruments. Additional efforts to permit financial institutions to access historical information on their potential new clients, subject to authorization by the Portuguese Data Protection Authority (CNPD), are in progress. In parallel, the BdP is assessing available options for reducing information asymmetry for smaller companies, taking also into consideration other available data sources, such as the Central Balance Sheet Database (CBSD).

25. **BPN SPVs.** We are implementing the strategy for managing the distressed assets from Banco Português de Negócios (BPN). Two companies have been selected through a competitive bidding process to manage the credit portfolios currently held by Parvalorem, a state-owned Special Purpose Vehicle (SPV). In parallel, the disposal of the participations and assets held by the other two state-owned SPVs is progressing. CGD’s state-guaranteed claim will be gradually settled in cash, according to the schedule agreed with the EC, ECB, and IMF staff. Any net recoveries realized on the assets will also be applied towards the settlement of CGD’s claim.

Boosting Employment, Competitiveness, and Growth

26. **Overall Reform Strategy.** The ultimate objective of our structural reform agenda is to enhance competitiveness and the business environment, so as to boost medium-term growth and job creation prospects. Significant steps have already been taken on the labor and product market fronts, where reforms have been designed to alleviate nominal rigidities, facilitate adjustment, and foster a reallocation of resources toward the tradable sector. Important steps have also been taken to reduce red tape and raise the efficiency of the judicial system. Nonetheless, we are determined to

further advance structural reforms. In light of this, we are working toward identifying unaddressed policy distortions and other potential priority reform areas.

27. **Labor Market Institutions.** Significant steps have been taken over the past couple of years to make the labor market more dynamic and efficient—including the reform of the Employment Protection Legislation, the reform of unemployment benefits and the reform of the wage-setting mechanism. A new reform of severance pay also entered into force more recently (October 1 Structural Benchmark). In light of the recent Constitutional Court ruling against legislative provisions that made it easier for firms to lay off employees in case of redundancy or unsuitability, the government's immediate priority will be to find alternative reform options that respect the ruling.. Following consultations with social partners, the alternatives will be discussed with IMF/EC/ECB staff at the time of the tenth review. Looking ahead, by end-November, we intend to enhance the activation of the unemployed by improving the role of the counseling services and by stepping up job search requirements, so as to create incentives for job seekers to accept offers and facilitate the job matching process. In view of the still extremely high unemployment, we also intend to continue to assess policy options to promote an adjustment more favorable to employment. In this context, the government will discuss at the time of the tenth review and present by end-December 2013 a report assessing policy options in three main areas: (i) ensuring more effective decentralization of wage bargaining; (ii) ensuring more wage flexibility; and (iii) study proper alignment of incentives to challenge dismissals in court.

28. **Energy.** We continue our efforts to improve the sustainability of the national electricity system. Steps have been taken in the past year to reduce excessive rents, mainly through renegotiation. The overall initial cost reduction targets were largely met, although with shortfalls for some specific measures. Nonetheless, our revised medium-term tariff debt projections (June 15 *Structural Benchmark*) clearly show strong upward pressures on the system debt, reflecting partly downward pressures on demand for electricity are generating. A number of additional measures are being considered to help reduce debt. Since we are concerned about the potential impact of large electricity price increases on competitiveness, we are investigating other options to better balance the burden of adjustment between the various stakeholders of the electricity sector, notably by eliminating remaining excess rents.

29. **Ports.** We are taking steps aimed at reducing costs for exporters. Following reductions in fees on port use (*TUP-Carga*) and a revision of the Ports Work Law, we are now seeking effective transmission of lower labor costs to end-users of port services. In particular, we will engage with concessionaires with a view to modifying existing concession contracts so as to foster price reduction. Specifically, the next steps include designing by the time of the tenth program review a strategy and a detailed timetable for measures ensuring the cost reduction and enhanced performance of both port authorities and port operators. We will also revise incentives for port operators by adopting a new performance-based model for future concessions and encourage entry of new operators. A review of the overall cost savings for exporters generated through these reforms will be conducted by December 2013.

30. **Regulation**. A framework law for the functioning of regulators was recently enacted. The law: (i) establishes a regulatory environment that protects the public interest and promotes market efficiency, (ii) guarantees the independence and financial, administrative and management autonomy of the National Regulatory Authorities in the exercise of their responsibilities, including the necessary conditions to safeguard adequate human and financial resources being able to attract and retain sufficiently qualified staff, and (iii) strengthens the role of the Competition Authority in enforcing competition rules. The corresponding amendments to the bylaws of the National Regulatory Authorities will be approved by the Government by end-November. Once the NRA framework law and follow-up bylaws and internal regulations are in place, the regulators will continue to pursue the adoption of best international regulatory practices, including by organizing international peer review exercises.

31. **Services.** Reforms in the services sector aim at eliminating entry barriers and increase competition. Significant progress has already been made in amending sector-specific legislations to align them with the Services Directive. We expect adoption by Parliament of the remaining necessary amendments—including to the Construction Law—by end-2013, and the related ordinance, ensuring appropriateness of fees linked to construction activities. The new legal framework aiming at improving the functioning of the regulated professions for which regulation involves a professional body (such as accountants, lawyers, notaries) was published earlier this year. The professional bodies' statutes are being amended accordingly for submission by the government to Parliament by yearend, including by eliminating unjustified restrictions to activity and further improving the conditions for mobility of professionals in line with EU Directives in the area of free movement of professionals.

32. **Licensing and Administrative Burden.** Tackling excessive licensing procedures, regulations and other administrative burdens—which are impeding the establishment, operation, and expansion of firms—is a government priority. Although we have faced delays in some areas due to the recent changes in the government and administrative capacity constraints, we remain strongly committed to meeting our revised timeline. Immediate priorities include: (i) adoption of the New Legal Regime on Urbanism and Building (RJUE) by the time of the tenth program review; (ii) completion of an inventory of the regulatory costs in the economy, starting with the most burdensome, on a basis of which we will devise a roadmap for a regulatory simplification; and (iii) completion of the reforms to simplify licensing procedures in the areas of tourism, commerce and industry. We will step up our efforts to make fully operational the Point of Single Contact, an e-government portal which allows administrative procedures to be done online. The new VAT cash accounting regime will also support an improvement of the business climate.

33. **Judiciary.** Most of the key judicial reforms have been successfully implemented. In particular, the new Code of Civil Procedure that entered into force on September 1, 2013 will speed up civil and enforcement proceedings. Another key legislation, the Judicial Organization Act, was adopted by Parliament in June 2013, and we have started to take steps to enable a smooth implementation by setting up a task force and adopting a wide range of implementing legislation. With respect to targeted measures to reduce the backlogged enforcement cases, an additional

179,000 enforcement cases have been cleared, bringing down the total number by about 344,000 enforcement cases since November 2011. We will publish quarterly reports on the clearance rate of enforcement court cases from the third quarter 2013 onwards (within four months after the end of the relevant quarter). We will establish the oversight body for enforcement agents and insolvency administrators (CAAJ) shortly after the entry into force of the CAAJ law, which was submitted to Parliament for approval in June 2013. The CAAJ law will enhance the supervision of enforcement agents, and thus further complement reforms implemented under the new Code of Civil Procedure and the new fee structure for enforcement agents, which entered into force on September 1, 2013 to incentivize speedier enforcement proceeding.

Table 1. Portugal: Quantitative Performance Criteria

(Billions of euros, unless otherwise indicated)

	Mar-13		Jun-13		Sep-13	Dec-13	Mar-14
	Program	Actual	Program	Actual			
1. Floor on the consolidated General Government cash balance (cumulative)	-1.9	-1.4	-6.0	-3.8	-7.3	-8.9	-1.7
2. Ceiling on accumulation of domestic arrears by the General Government (continuous indicative target) 1/	0.0	Not met	0.0	Not met	0.0	0.0	0.0
3. Ceiling on the overall stock of General Government debt	182.2	178.5	187.3	184.1	188.9	191.3	193.0
4. Ceiling on the accumulation of new external payments arrears on external debt contracted or guaranteed by the general government (continuous performance criterion)	0.0	…	0.0	…	0.0	0.0	0.0

1/ Domestic arrears for the purpose of the program increased by close to €0.4 billion in the first half of 2013, largely due to the accumulation of arrears by SOE hospitals.

Table 2. Portugal: Structural Conditionality: Seventh Review Under the EFF

	Measure	Timing	Status
Prior Actions			
1	Submit to parliament a draf 2014 budget consistent with the general government deficit target of 4 percent of GDP (MEFP ¶4-6)		Met
2	Submit to Parliament a draft Law or a budget provision to implement the single wage scale PER measure.		Met
3	Submit to Parliament a legislative proposal that increases the statutory retirement age to 66 years.		Met
Structural Benchmarks			
A. Fiscal policy			
1	Submit to Parliament a new draft public administration labor law that will aim at aligning current public employment regime to the private sector rules, including for working hours and holiday time, and termination of tenure.	July 15, 2013	Partially Met 1/
2	Submit to Parliament a draft law on the redesigned mobility pool.	End-June 2013	Met 2/
3	Submit to Parliament a legislative proposal that increases the statutory retirement age to 66 years.	July 15, 2013	Changed to prior action
4	Submit to Parliament a legislative proposal that aligns the rules and benefits of the public sector pension fund, CGA, to the general pension regime.	July 15, 2013	Met with delay
A. Strengthen financial stability			
5	Submit to Parliament amendments to the law governing banks' access to public capital.	End-January, 2013	Met
B. Enhance competitiveness and address bottlenecks to growth			
6	Enact the severance pay reform that reduces severance payments to 12 days per year for all new permanent labor contracts	October 1, 2013	Met
7	Update projections of the medium-term energy tariff debt path and identify policy options to eliminate the tariff debt by 2020 .	June 15, 2013	Met
C. Strengthen fiscal institutions and reduce fiscal risks			
8	Revise and submit to Parliament the draft regional and local public finance law.	End-Dec 2012	Met
9	Implement a full-fledged Large Taxpayer Office (LTO), to cover audit, taxpayer services, and legal functions concerning all large taxpayers, including the adoption of account managers.	End-Dec 2012	Met

Notes:

1/ The decree-law aligning working hours of the public sector to 40-hours per week as in the private sector was altready submitted and approved by the Parliament. The new draft public administration labor law will be submitted to Parliament by end-October.

2/ The draft law on the redesigned mobility pool was submitted and approved by Parliament. However, it was rejected by the Constitutional Court and has returned to Parliament for amendments.

Attachment II. Portugal: Technical Memorandum of Understanding

October 24, 2013

1. This Technical Memorandum of Understanding (TMU) sets out the understandings regarding the definitions of the indicators subject to quantitative targets (performance criteria and indicative targets), specified in the tables annexed to the Memorandum of Economic and Financial Policies. It also describes the methods to be used in assessing the Program performance and the information requirements to ensure adequate monitoring of the targets. We will consult with the EC, the ECB, and the IMF before modifying measures contained in this letter or adopting new measures that would deviate from the goals of the Program, and provide the EC, the ECB, and the IMF with the necessary information for Program monitoring.

2. For Program purposes, all foreign currency-related assets, liabilities, and flows will be evaluated at "Program exchange rates" as defined below, with the exception of the items affecting government fiscal balances, which will be measured at spot exchange rate (i.e., the rate for immediate delivery) prevailing on the date of the transaction. The Program exchange rates are those that prevailed on May 5, 2011. In particular, the exchange rates for the purposes of the Program are set €1 = 1.483 U.S. dollar, €1 = 116.8390 Japanese yen, €1.09512 = 1 SDR.

3. For reporting purposes, the MoF and BdP will employ the reporting standards and templates considered to be appropriate given the transmission of data covered by this TMU, unless otherwise stated or agreed with the EC, the ECB and the IMF.

General Government

4. **Definition.** For the purposes of the Program, the General Government, as defined in the Budget Framework Law, Law No. 91/2001 of August 20, amended by Law 22/2011 of May 20, includes**:**

- 4.1. The Central Government. This includes:
  - 4.1.1. The entities covered under the State Budget, which covers the budgets of the Central Administration, including the agencies and services that are not administratively and financially autonomous, agencies and services that are administratively and financially autonomous (*Serviços e Fundos Autónomos* – SFA).
  - 4.1.2. Other entities, including Incorporated State-owned enterprises (ISOE), or extra-budgetary funds (EBF) not part of the State Budget, but which are, under the European System of Accounts (ESA95) and ESA95 Manual on Government Deficit and Debt rules, classified by the National Statistical Institute (INE) as part of the Central Government.

- 4.2. Regional and Local Governments, that include:
    - 4.2.1. Regional Governments of Madeira and Azores and Local Governments (*Administrações Regionais and Locais*);
    - 4.2.2. Regional and local government-owned enterprises or companies, foundations, cooperatives and other agencies and institutions, which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE as Local Government.
- 4.3. Social Security Funds comprising all funds that are established in the general social security system.
- This definition of General Government also includes any new funds, or other special budgetary and extra budgetary programs or entities that may be created during the Program period to carry out operations of a fiscal nature and which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE in the correspondent subsector. The MoF will inform the EC, ECB, and IMF of the creation of any such new funds, programs, entities or operations at the time of its creation or statistical re-classification or, in the case of Regional and Local Governments, at the time the Government acknowledges its creation.
- The General Government, as measured for purposes of Program monitoring in 2013, shall not include entities nor operations (including pension funds) that are re-classified into the General Government during 2013, but shall include those reclassified in 2011-12.[1]
- The General Government, as measured for purposes of Program monitoring in 2014, shall not include entities nor operations (including pension funds) that are re-classified into the General Government during 2014, but shall include those reclassified in 2012-13.

5. **Supporting Material**

- 5.1. Data on cash balances of the State Budget will be provided to the EC, the ECB and the IMF by the MoF within three weeks after the end of the month. Data will include detailed information on revenue and expenditure items, in line with monthly reports that are published by the MoF.

[1] An operation refers to part of a legal entity that is involved in the production or delivery of goods and services—including government services provided on a nonmarket basis. As such, it does not include transactions relating to the assets or liabilities of an entity. For example, should an entity handle a number of PPPs, reclassifying only one PPP would be considered as reclassifying an operation. In contrast, taking over part of an entity's debt by the government would not qualify for the exclusion. On this issue, see also paragraph 13.

- 5.2. Data on the cash balances of the other parts of General Government as defined in paragraph 4[2] will be provided to the EC, the ECB and the IMF by the MoF within seven weeks after the end of the month. Data will include detailed information on revenue and expenditure items. Data will also include detailed information on PPP-related revenues and expenditures for those PPP reclassified within the General Government sector according to ESA 95, and called guarantees.

- 5.3. Data on domestic and external debt redemptions (securities), new domestic and external debt issuance (securities), change in the domestic and foreign currency assets and liabilities of the Central Government at the BdP and other financial institutions will be provided to the EC, the ECB, and the IMF by the BdP within 40 days after the closing of each month.

- 5.4. BdP will provide to the EC, the ECB, and the IMF detailed monthly data on the financing of the General Government, as defined in ESA95, within seven weeks after the closing of each month.

- 5.5. Data on the revenues, operating expenses, capital expenditure, remuneration of personnel, EBITDA, and number of staff will be provided for state-owned enterprises (SOEs) on a quarterly basis, within 7 weeks after the end of each quarter. Aggregate data for the SOEs within the perimeter will be provided, with company-specific information for REFER, Estradas de Portugal, Metro de Lisboa, and Metro de Porto. Furthermore data for Comboios de Portugal and Parpública (outside the perimeter) will also be provided.

Quantitative Performance Criteria, Indicative Ceilings, and Continuous Performance Criteria: Definitions and Reporting Standards

A. Floor on the Consolidated General Government Cash Balance (Performance Criterion)

6. **Definition.** The consolidated General Government cash balance (CGGCB) is defined as the sum of the cash balances of the entities covered by the State Budget, the ISOE, the Regional and Local Governments, and the Social Security Funds, and other entities and EBFs, as defined in paragraph 4. Privatization receipts will be excluded from cash receipts. In 2012 and beyond, revenues from the reclassification of pension funds into the general government will not be accounted for as cash revenues for the purpose of the calculation of the consolidated general government cash balance. In 2012-13, the cash proceeds from the sale of the ANA airport concession will be accounted for as cash expenditure-reducing transactions. The net acquisition of financial assets for policy purposes, including loans and equity participation will be recorded as cash

[2] In 2011, data exclude regional and local government-owned enterprises or companies, foundations, cooperatives and other agencies and institutions, which are, under the ESA95 and ESA95 Manual on Government Deficit and Debt rules, classified by the INE as Local Government, i.e., entities referred in paragraph 4.2.2.

expenditures, except for transactions related to the banking sector support and restructuring strategy under the Program. Called guarantees (excluding those related to the banking sector support and restructuring strategy), where entities of the General Government make cash payments on behalf of entities that are not part of the General Government, will be recorded as cash expenditures.

- 6.1. **The Cash Balance of the State Budget.** The cash balance of the State Budget will be measured from above the line, based on budget revenues (recurrent revenue plus nonrecurrent revenue, including EU revenues, minus tax refunds) minus budget expenditures of the State Budget as published monthly on the official website of the DGO of the MoF, and in line with the corresponding line items established in the State Budget. Budget expenditures will exclude amortization payments but include salaries and other payments to staff and pensions; grants to Social Security Funds, medical care and social protection; operational and other expenditure, interest payments; cash payments for military equipment procurement; and EU expenses.

- 6.2. **The Cash Balance of the Regional and Local Governments, Social Security Funds, ISOE and Other Entities or EBFs.** The cash balance of each of these parts of the General Government will be measured from above the line, based on revenues minus expenditures as it will be provided by the DGO of the MoF in the monthly General Government budget execution report (see Para 5), and in line with the corresponding line items established in their respective budgets. All entities including ISOE that prepare accrual-based financial statements will submit monthly cash flow statement in accordance with form and content specified by the MoF. The reporting by Local Government will be phased as set out in paragraph 8 below.

- 6.3. **Adjustor.** The 2013 and 2014 quarterly floors on the consolidated general government cash balance will be adjusted for the cumulative amount of arrears settled in the context of the arrears clearance strategy: (i) health sector arrears (up to €432 million), (i) local government arrears settled through the €1 billion credit facility created in May 2012, and (ii) RAM government arrears subject to concluding the agreement with the central government (up to €1.1 billion).

Other Provisions

7. For the purpose of the program, the expenditure of the central government that is monitored excludes payments related to bank support, when carried out under the program's banking sector and restructuring strategy. However, any financial operation by central government to support banks, including the issuance of guarantees or provision of liquidity, will be immediately reported to the EC, ECB, and IMF.

8. Quarterly consolidated accounts for the General Government on a cash basis will be reported for internal, EC, ECB, and IMF monitoring 7 weeks after the reference period, starting with the first quarter of 2012. The reports will be published externally starting with December 2011 data.

SOEs will be consolidated with the general government accounts starting with the first quarter 2012. The larger municipalities (defined as those with a population of 100,000 voters or more) are required to provide monthly reports under current arrangements, and their cash balance will be included in the calculation of the monthly cash General Government balance. The cash balance of the smaller municipalities, i.e. those with a population of under 100,000 voters, will be excluded until any necessary legal changes requiring them to provide monthly reports have been put in place. In this transitory period, the MoF will provide a monthly estimate of the cash balance of these smaller municipalities excluded from the General Government reports to the EC, the ECB, and the IMF.

9. **Supporting Material**

9.1. Data on cash balances of the State Government, ISOEs, Regional and Local Government and Social Security Funds will be provided to the EC, the ECB and the IMF by the MoF within seven weeks after the end of each month. The information provided will include general government net acquisitions of financial assets for policy purposes, including loans and equity participations, as well as called guarantees where entities that are part of the General Government make cash payments on behalf of entities that are not part of the General Government.

9.2. The MoF will submit quarterly data on General Government accounts determined by the INE in accordance with ESA 95 rules, showing also the main items of the transition from cash balances to the General Government balances in national accounts. The reconciliation will be accompanied by necessary explanatory materials for any indication of potential deviation of the annual general government cash target from the annual general government accrual target determined in accordance with ESA 95 rules.

B. Non-Accumulation of New Domestic Arrears by the General Government (Continuous Indicative Target)

10. **Definitions.** Commitment, liabilities, payables/creditors, and arrears can arise in respect of all types of expenditure. These include employment costs, utilities, transfer payments, interest, goods and services and capital expenditure. Commitments are explicit or implicit agreements to make payment(s) to another party in exchange for that party supplying goods and services or fulfilling other conditions. Commitments can be for specific goods and services and arise when a formal action is taken by a government agency, e.g., issuance of a purchase order or signing a contract. Commitment can also be of a continuing nature that require a series of payments over an indeterminate period of time and may or may not involve a contract, e.g. salaries, utilities, and entitlement payments. Liabilities are present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources (usually cash) embodying economic benefits or service potential. In relation to commitment, the liability arises when a third party satisfies the terms of the contract or similar arrangement. Payables/creditors are a subset of liabilities. For the purposes of the program payables/creditors exclude provisions, accrued liabilities. Arrears are a subset of payables/creditors. For the purposes of the Program domestic arrears are defined as payables/creditors (including foreigner commercial creditors), that

have remained unpaid for 90 days or more beyond any specified due date (regardless of any contractual grace period). In case no due date is specified, arrears are defined as payables/creditors that have remained unpaid for 90 days or more after the date of the invoice or contract. Data on arrears will be provided within seven weeks after the end of each month. The continuous indicative target of non-accumulation of new domestic arrears requires that the total arrears at the end of any month are not greater than the corresponding total at the end of the previous month—based on the same perimeter with respect to the entities covered. This also includes arrears that are being accumulated by the SOEs not included in the General Government.

11. **Supporting Material.** The stock of arrears will be measured through a survey. Reports on the stock of arrears of the General Government are being published monthly. The MoF will provide consistent data on monthly expenditure arrears of the General Government, as defined above. Data will be provided within seven weeks after the end of each month and will include total arrears classified by the different constituent sectors of the General Government sub-sector as defined in paragraph 4, as well as the monthly amounts of arrears cleared under the arrears clearance strategy (see paragraph 6.3).

12. **Adjustor.** In 2013 and 2014, the monthly change in the stock of arrears will be adjusted for any stock adjustment related to the arrears clearance strategy as per paragraph 6.3. This will allow monitoring the underlying flow of new arrears.

C. Ceiling on the Overall Stock of General Government Debt (Performance Criterion)

13. **Definition.** The overall stock of General Government debt will refer to the definition established by Council Regulation (EC) No 479/2009 of 25 May 2009 on the application of the Protocol on the Excessive Deficit Procedure annexed to the Treaty establishing the European Community. For the purposes of the Program, the stock of General Government debt will exclude: (i) debt contracted for bank restructuring, when carried out under the Program's banking sector support and restructuring strategy; (ii) IGCP deposits; and (iii) (from end-September 2011) the *'prepaid margin'* on all EFSF loans.

14. **Adjusters.** For 2013, the ceiling of the overall stock of General Government debt will be adjusted upward (downward) by the amount of any upward (downward) revision to the stock at end-December 2012 general government debt of EUR 204.5 billion. From 2014 onwards, the ceiling of the overall stock of General Government debt will be adjusted upward (downward) by the amount of any upward (downward) reclassification of entities or operations that affects the stock at end-December of the previous year.

15. **Supporting Material.** Quarterly data on the total stock of General Government debt as defined in paragraph 12 will be provided to the EC, ECB, and IMF by the BdP no later than 90 days after the end of each quarter, as reported to the ECB and the Eurostat. Monthly estimates will be provided to the EC, ECB and IMF by BdP no later than seven weeks after the end of each month.

D. Non-Accumulation of New External Debt Payments Arrears by the General Government (Continuous Performance Criterion)

16. **Definition.** For the purposes of the Program, the definition of debt is the same as in paragraph 12. An external debt payment arrear will be defined as a payment on debt to nonresidents, contracted or guaranteed by the general government, which has not been made within seven days after falling due (taking into account any applicable contractual grace period). The performance criterion will apply on a continuous basis throughout the Program period.

17. **Supporting Material.** Any external debt payment arrears of the General Government will be immediately reported by the MoF.

E. Bank Solvency Support Facility

18. The dedicated Bank Solvency Support Facility (BSSF) account will be maintained at the Bank of Portugal. As per previous review, resources for the BSSF will be agreed at each review and deposited in the dedicated account.

F. Overall Monitoring and Reporting Requirements

19. Performance under the Program will be monitored from data supplied to the EC, the ECB, and the IMF by the MoF and BdP. The authorities will transmit to the EC, ECB, and IMF any data revisions in a timely manner.