



PORTUGUESE REPUBLIC

MINISTRY OF FINANCE AND PUBLIC ADMINISTRATION

OFFICE OF THE MINISTER OF STATE AND FINANCE

INITIATIVES FOR STRENGTHENING FINANCIAL STABILITY

12 October 2008

As recently emphasized by the International Monetary Fund, the Portuguese financial system is fundamentally sound and has been resilient to the turbulence in financial markets. However, it is currently being subject to a substantial external shock, due to severe liquidity restrictions in international financial and money markets.

Financial stability is a key factor in ensuring the regular financing of households and firms, in particular SMEs. The Portuguese Government is, thus, determined to use all means to guarantee financial stability and reiterates that all deposits of the Portuguese people in all banks established in Portugal are guaranteed.

The Government approved today an Initiative to strengthen financial stability, by improving conditions for credit institutions' access to liquidity in financial markets (Annex 1). Based on granting State guarantees for the financing of credit institutions, up to a maximum value of 20 billion euros, this Initiative:

- (i) Enhances the confidence in the domestic financial system;
- (ii) Permits timely intervention adapted to market conditions;
- (iii) Is temporary, remaining effective only while market conditions have not returned to normal;
- (iv) Safeguards the interest of depositors and taxpayers;
- (v) Allows the shareholders and managers of banks to be held accountable whenever necessary and fosters the adoption of good corporate governance principles, in accordance with best international practices;
- (vi) Safeguards the interests of the market in general and a level playing field among competitors, in particular.



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The Government has also approved, in detail, the package of measures of last week's Council of Ministers (Annex 2), which includes measures to strengthen market agents' information and disclosure obligations to both their clients and supervisory authorities.

In the field of guaranteeing bank deposits, the value covered by the Bank Deposits Guarantee Fund and the Mutual Agricultural Credit Guarantee Fund is raised from EUR 25 000 to EUR 100 000. Moreover, the term for reimbursing deposits is significantly reduced.

The approval of these measures occurs in a context of similar initiatives in other Member States of the European Union, and meets the commitments undertaken by the Ecofin Council on 7 October last. The Government remains committed to joint action in Europe, which may imply the adoption of additional measures deemed necessary.

The intention in adopting today's Initiative is not for the State to serve as a substitute for market mechanisms, namely in relation to the provision of liquidity, but rather to support institutions' access to market mechanisms.

The Government, in addition to the measures approved today, remains attentive and stands ready to adopt the mechanisms deemed necessary to facilitate financial institutions' access to liquidity, to strengthen their financial capacity and soundness and, consequently, to guarantee financial stability in Portugal. Accordingly, the financial system will continue to ensure the normal financing of the economic activity and, simultaneously, the savings of the Portuguese people deposited in any bank operating in Portugal are guaranteed.

The Government will maintain a flexible framework, in both the adoption of additional measures that may prove to be necessary and in swiftness in the implementation of the decisions taken today.



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Annex 1

INITIATIVE FOR STRENGTHENING FINANCIAL STABILITY

State Guarantees for the Financing of Credit Institutions

12 October 2008

1. Summary

In the context of initiatives that are being adopted in the European Union and aiming to strengthen the financial system stability, the access to liquidity and the financial capacity of credit institutions, the State creates a special scheme for granting guarantees to credit institutions with registered office in Portugal.

This instrument is intended to guarantee the renewal of credit institutions' financing operations, in order to ensure the regular financing of the economic activity at a time of severe turbulence in international financial markets.

This instrument is conditional, temporary and applied under commercial terms.

Besides this instrument, other ones deemed necessary to strengthen the financial soundness of credit institutions may be adopted.

2. Total value of guarantees

Guarantees of the State up to a maximum value of 20 billion euros may be awarded under this Initiative.

3. General guarantee access conditions

The award of guarantees is governed by the following principles:

- i. The guarantees are provided under adequate commercial conditions, considering, in particular, the assessment of the institution's risk and, as such, fees are charged and adequate coverage by good quality assets is required.



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- ii. The State may revise the fees while the guarantee remains effective, when market conditions change significantly.
- iii. Credit institutions granted guarantees are monitored by the State in liaison with the Portuguese Central Bank.
- iv. In the event that a guarantee is activated, the State will require the beneficiaries to reimburse the due amount, notwithstanding the adoption of adequate alternative measures, including the conversion of the credit into share capital, upon consultation with the Portuguese Central Bank.

4. Entity responsible for the decision to award and manage guarantees

The Government will approve the general conditions for awarding guarantees (overall policy) and the respective sum, as well as the set of principles governing their award.

The decision to award guarantees and their continuous monitoring is undertaken by the Ministry of Finance, in collaboration with the Portuguese Central Bank, via an active and swift process as required by current conditions.

5. Implementation

All credit institutions with registered office in Portugal are eligible to benefit from this Initiative and can apply forthwith for the provision of the State's guarantee under current legislation. The Government will immediately submit the legislative proposals required to implement this Initiative to the Portuguese Parliament.

6. Duration

This Initiative is temporary. It remains in force only while normal market conditions are not restored, applying only to guarantees to be issued before 31 December 2009, at the latest.



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7. Financing

The State will set up a Fund that will be capitalised through the issuance of public debt securities, in order to cover the risk of activation of the guarantees provided and to finance other measures that may be taken to strengthen credit institutions' financial soundness.

The sum held by the Fund on the Initiative's winding up, whether due to the funds being unused or resulting from reimbursements by credit institutions, as well as the fees paid by such institutions for the provision of the guarantees, will be used to repay the public debt that was issued.



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Annex 2

INITIATIVES TO REINFORCE THE FINANCIAL SYSTEM STABILITY

Coordination in Supervision, Transparency and Disclosure of Information

02 October 2008

The Portuguese Council of Ministers approved a set of measures to reinforce the effectiveness of financial supervision and financial stability, in close articulation with the National Council of Financial Supervisors.

These measures are fully in line with the EU policy response - which underlies the roadmap for action taken in response for the financial turmoil - namely, by improving transparency and valuation of financial products, strengthening prudential regulation and making markets function better.

In this context, the Portuguese initiatives cover 4 main areas of policy response:

I. Improve transparency and information duties

- a) Financial institutions must provide information to their supervisors on the nature and extent of risks incurred in relation to the activities and instruments; on the risk management practices of relevance to their activities, and on valuation methods for financial instruments and related disclosures, especially when markets are no longer active;
- b) Financial institutions must provide full and clear information to investors on structured financial products, in order to guarantee that investors have all relevant information on the characteristics and riskiness of these products;
- c) Concerning consumption loans, credit institutions shall provide their clients full and clear information on the terms of the loan contract, including information on the total cost of the loan, before the contract signature.
- d) The rules on financial products advertising are reinforced, especially in what structured financial products are concerned. In this specific case, a previous authorization from the supervisor is now required;



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- e) Financial institutions and public companies must provide information on their equity holdings in companies with their head-offices situated in a non-EU country;
- f) Financial institutions, state-owned firms and public companies must release a statement of their policy on directors' remuneration, which must be included on the agenda of the shareholders' general meeting and submitted to a vote. The statement should include, among others, information on the total annual remuneration of individual directors, the shares or rights to share options granted to them and the criteria used to compute the variable remuneration (including mechanisms which guarantee an upper limit to the variable remuneration, when firms' performance is worse than expected).

II. Review of the sanctions regime in both criminal and administrative infractions

This review aims to:

- Adapt the sanctions regime to the current characteristics of the financial sector
- Strengthen the sanctions regime punishment and dissuasion effects
- Promote the arrangement of the fines frames and the procedural tools in the three financial sectors, which had remained unchanged since the 90s.

In this context, the following measures are going to be implemented:

- a) Update of the criminal frames - that are raised from 3 to 5 years - and of the fines amounts - that are raised up to a maximum of €5.000.000;
- b) To punish harshly the cases where the duty violation leads to a quantitatively large benefit, if the double of that economic benefit exceeds that amount, besides losing the economic benefit itself, the maximum fine increases;
- c) The administrative infractions related to the violation of duties of information, and of constitution or contribution for mandatory guarantee schemes are now considered "very serious ones";
- d) The introduction of the summary proceeding in the banking and in the insurance, reinsurance and pension fund sectors, that allows to haste the sanctions intervention of the supervisory authorities, in an large number of less seriousness offences;



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e) The advertising system of the condemnatory decisions in administrative infraction proceeding applies now to the banking and the insurance, reinsurance and pension fund sectors.

III. Reinforcement of the responsibility of individual agents and collective bodies

The rules, according to which collective bodies are responsible for offences committed by members of their boards and by holders of executive, supervisory or managerial posts acting in the performance of their functions, become more comprehensive.

IV. Reinforce the coordinated action of financial supervisors

a) The role of the National Council of Financial Supervisors (CNSF) - which consists of the three supervisory authorities of the Portuguese financial system - in the coordination of overall financial supervision is reinforced. The CNSF should assess and evaluate the events that may affect financial stability, and guarantee regular sharing of information among the three supervisors;

b) The sharing of relevant information on financial stability between the CNSF and the Ministry of Finance is strengthened.

Finally, in order to improve banks' liquidity risk management, the decree-law that establishes the legal requirements for granting credit for the effects of securitisation and regulates the constitution and functioning of securitisation funds, securitisation firms and the management companies of those funds was modified, in order to remove some obstacles in the renegotiation of credit contract terms.