



BANKING & FINANCE | Law no. 4/2012 establishing measures for the reinforcement of the financial solidity of banking institutions

Within the framework of the measures to be adopted for the implementation of the Financial and Economic Assistance Program for Portugal, the new Law no. 4/2012, of January 11 (hereinafter, the “Law”), amending Law no. 63-A/2008, of November 24, enters today into force, with an aim to establish the reinforcement of the financial solidity of banking institutions and to contribute to the strengthening of their levels of Core Tier 1 capital.

One of the more visible measures provided by the new Law is the extension of its scope of application in relation to the former regime, expressly including banking institutions established in Portugal which are not public limited corporations, as well as savings banks (*caixas económicas*) and, especially, the *Caixa Central de Crédito Agrícola Mútuo*, as beneficiaries of capitalization transactions.

With the purpose of encouraging the stability of the financial system and the protection of depositaries, public intervention for the capitalization of these institutions tends to assume a voluntary (generally through the filing of an application by the relevant banking institution with the Bank of Portugal), transitory (it shall last for a maximum period of five years) and subsidiary nature (it shall operate as an extraordinary measure against other investment alternatives, such as, for instance, injections of capital by private shareholders, be they Portuguese or foreign). Together with public intervention, the Law provides the mechanisms applicable to public divestment, taking place once the maintenance of adequate Core Tier 1 capital levels is ensured, which is to be verified by the Bank of Portugal and to be performed in accordance with market conditions and to preserve the appropriate payment and security of the capital invested, always taking into account the aims of financial stability.

The preferential methods provided by the Law to the capitalization process are the purchase by the State of the credit institution’s shares (or, if the institution is not a public limited company, other securities representative of its capital) or an increase in capital of the credit institution, whereby the purchased shares by public investment are automatically converted into a new class of “special shares”.

This new class of “special shares” does not provide the State, in a first stage of capitalization which cannot exceed the period of five years, with the right of overcome or control the relevant institution, as well as with the voting rights concerning matters resolved by qualified majority. Throughout this stage, “special shares” grant the State a right to a primary dividend, the application of the available amounts above the own funds of the relevant institution being mandatory with regard to the payment of the State’s intervention.

However, this new Law innovates by establishing a new stage of the capitalization process, reinforcing the State’s powers regarding the relevant banking institution where a materially relevant breach of the capitalization plan occurs. At this stage, the Law provides the State with the free exercise of all voting rights related with its social participation in the relevant institution, as well as the power to nominate the members of both the board of directors and the supervisory board who may represent the State to the extent of its participation, the right to the primary dividend being preserved. During this second stage, the distributable profits are allocated to State divestment.

The legal framework laid out in this Law, in an extremely difficult state of affairs brought about by the atmosphere of economic and financial instability, allows for an adequate and proportional balancing of the interests of all parties involved, permitting the defense of the public interest, on one hand, whilst respecting the legal autonomy of the credit institutions and the rights of their shareholders.

