The Banking Regulation Review

Editor
Jan Putnis

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The Banking Regulation Review

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EDITOR'S PREFACE

Legal and regulatory areas of concern come and go in their perceived importance. It is, however, very difficult to recall any other occasion when a subject regarded by many lawyers as so obscure and arcane as international banking regulation has come to such prominence in such a short period of time.

Before the onset of the financial crisis in western economies in 2007, banking regulation was regarded by many as a discipline practised by technocrats who were, to put it politely, best left to themselves. The subject has risen up the agenda so quickly since then that few lawyers who advise financial institutions have had time to draw breath and assess the position now reached. The reality, of course, is that no final position has been reached and none is ever likely to be reached: banking regulation will continue to evolve, punctuated by bursts of activity every time there is a serious crisis to manage. What has happened is that the importance of this subject, and its rightful place amongst legal disciplines, has finally been recognised. This means that there is now great demand, from the banks themselves, but also from governments and regulators, for accessible and user-friendly explanations of the applicable rules.

The continual evolution of the rules makes any survey of banking regulation very difficult to write without risking almost immediate obsolescence. This book is an attempt to rise to that challenge and it is hoped that future editions will address the many further developments in this area that are expected to take place in the coming months and years. The book is aimed principally at lawyers and others who need access to an overview of the applicable rules in the important areas that the book covers and a commentary on recent developments. It also includes commentary on many of the areas of banking regulation that are of critical importance to the major cross-border transactions in which banks become involved.

The book illustrates the many and differing approaches that governments and banking regulators have taken to addressing what they perceive to be the problems affecting the banks that they regulate. To that extent, the lack of international coordination is a potential source of dismay amongst politicians and others who have spent so much time over the past three years trying to develop common approaches to the international challenges highlighted by the financial crisis.

It is, however, to be hoped that surveys of the kind in this book also inform the continuing debate about how to minimise the risk of a further crisis on anything like the scale that we have just seen. It will, quite literally, pay for governments to appreciate that further significant financial crises are inevitable in the future, and that the principal aim of reform should, therefore, be to minimise their likely impact, both on the lives of the millions of people who rely on banks and on local and regional economies.

It is a tribute both to the contributors and the publishers that so many leading banking and regulatory lawyers have made themselves available to write chapters for this book. I would like to thank them all for the support and encouragement that they have provided at a time when many of them have been almost overwhelmed with work on other projects emerging from the financial crisis. Many of the contributors have also been involved in initiatives designed to stabilise and reform the banking sectors in their countries. I would also like to thank Gideon Roberton and his colleagues at the publishers for their efforts in coordinating the project that this book has become, and in bringing it to fruition.

Jan Putnis
Slaughter and May
London
June 2010

Chapter 23

PORTUGAL

Pedro Cassiano Santos[*]

I INTRODUCTION

The Portuguese banking industry has been struggling since the beginning of the international crisis to avoid, as much as possible, the negative impact it might have on the health of the banks in general.

The bigger players seem to have coped reasonably well with the situation, and access to government support was kept at relatively low levels with less than €5 billion having been used under the government guarantee scheme by the banking community in general. However, two cases have blighted this ongoing effort: Banco Português de Negócios ('BPN') and Banco Privado Português ('BPP').

As far as BPP is concerned, as an investment bank with a minimum base of deposits acting primarily as a wealth manager, the stock market plunge eventually took its toll as a result of its high exposure to larger risk segments, similar to what happened to other small international banks with similar characteristics. BPP became insolvent, called for the support of the government and was temporarily kept afloat only as a result of being bailed out by a group of Portugese banks, assisted by a state guarantee. BPP finally became insolvent in April 2010 after all recovery attempts failed, and no further government support was available.

In respect of BPN, the crisis exposed a lack of capital resulting from the bank's activities that had been carried out in many segments of the economy outside the scope of 'banking'. There was a liquidity scarcity and lack of capital and the bank eventually had to be nationalised and placed under the control of a new board, appointed by the government to salvage the bank and avoid systemic collapse in the financial sector.

Nevertheless, these two seem to be isolated cases in which the crisis probably accelerated (or intensified) problems that were already in existence, forcing the adoption

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of more drastic measures that had to be implemented anyway. It is in any case fair to say that, as a whole, the financial sector in Portugal has so far held up relatively well over the past few months and hopefully the situation will now improve.

Several measures have been implemented in this crisis and liquidity scarcity scenario, both from a prudential point of view as well as regarding the requirements applicable to the conduct of banking business, but overall the Portuguese banks have shown a positive response and managed to keep up with all changes that came into play in this segment of economic activity.

II THE REGULATORY REGIME APPLICABLE TO BANKS

A credit institution qualifying as a bank, as defined in the Legal Framework of Banks and Financial Companies ('RGICSF'), is an undertaking conducting the business of receiving deposits or other repayable funds from the public and granting credit for its own account to third parties in general.

Banking activities in Portugal are governed by the RGICSF, which regulates the taking up and pursuit of banking business, banking corresponding to one of the several types of credit institutions and financial entities provided for in the law.

Banks operate in Portugal under the concept of a universal financial licence and may carry out a long list of activities such as the acceptance of deposits or other repayable funds from the public, granting credit, or any form of lending, including the granting of guarantees and other payment commitments, financial leasing and factoring. Banks having their head office in Portugal as well as branches of banks having their head offices abroad are qualified to carry on the aforementioned activities subject to Portuguese law.

Branches of banks incorporated in EU Member States may carry out in Portugal the activities listed as an Annex to European Directive 2000/12 of 20 March 2000, which the same bank would also be authorised to carry out in its home jurisdiction. These activities must be mentioned in a programme of operations when opening a branch, setting out, *inter alia*, the types of business envisaged to be conducted and the structural organisation of the branch. This programme of operations must be delivered by the relevant bank to its home jurisdiction authority and thereby notified to the Bank of Portugal ('the BoP'), which then enjoys a relatively short period to organise its host jurisdiction supervision operations.

According to the RGICSF, in respect of the activity of overseas banks not having a branch in Portugal, banks authorised in their home country to provide the services listed in the Annex to Directive 2000/12 may still carry on such activities in Portugal, even if they are not established here. As a prerequisite for the commencement of such services in Portugal, the supervisory authority of the bank's home jurisdiction must notify the BoP of the activities that the relevant institution intends to carry out, and certify that such activities are covered by the authorisation granted in the home country.

The current financial supervision system in force in Portugal is based on the coexistence of three supervisors, with responsibility for the three sectors of banking, capital markets, and insurance and pension funds; this corresponds to an organisational model in which the BoP acts as a central bank as well as the entity responsible for the supervision of banks and financial companies, focusing on the stability of the financial system, while the Portuguese Securities Market Commission ('CMVM') has the responsibility for supervising the securities market and derivative instruments as well as the activities of agents and financial intermediaries. Finally, the Portuguese Insurance Institute ('ISP') is responsible for the supervision on insurance and pension funds.

This tripartite model is expected to change in the last quarter of 2010 (possibly slipping into the year 2011), moving to a two-tier model, the so-called 'twin peaks' model, with only two autonomous and independent supervising entities. The BoP will be allocated the sole responsibility for all prudential supervision, while a new entity (resulting essentially from a merger between the CMVM and the ISP) will concentrate the competences regarding market conduct supervision. Both of these entities will have oversight of all players in the financial system, each focusing on its approach and area of expertise.

III PRUDENTIAL REGULATION

i Relationship with the prudential regulator

The BoP is currently responsible for the prudential and market conduct supervision of banks with a view to ensuring the stability, efficiency and soundness of the financial system. The BoP also enjoys the power to monitor and supervise the level of compliance with the rules of conduct and transparency requirements towards bank customers, thereby ensuring the safety of deposits and the protection of consumer interests. The powers and responsibilities of the BoP as a supervisory authority are stipulated in its Organic Law and in the RGICSF.

Banks subject to the supervision of the BoP are required to comply with prudential rules aimed at controlling risks inherent in their activities. On the one hand, these rules aim to ensure the solvency and creditworthiness of banks and, therefore, to maintain the stability of the financial system (and increase and maintain the level of trust of depositors, investors and the economic operators generally in such stability). On the other hand, they also aim to protect users (depositors and investors) against losses stemming from bad management, fraud or the bankruptcy of financial services suppliers or providers.

The RGICSF plays a central role in Portuguese prudential regulation, largely mirroring the EU Directives on financial activities. It is a set of harmonised rules covering a wide range of subjects such as the capital adequacy regime, banks and financial activities and the corresponding codes of conduct, as well as the limits on risk concentration and the rules on balance sheet consolidation and the supervision conducted on a consolidated basis. It also includes prudential rules or limits pertaining to certain non-harmonised areas that fall under the responsibility of the national authorities; for example, the provisioning framework, internal control requirements or limits that holdings banks are allow to have in fixed assets.

Most limits established in the context of prudential rules rely on the concept of own funds and the relationship and ratios that are required to be maintained with equity and quasi-equity instruments on both the asset and the liability side of the balance sheet.

In order to monitor compliance with prudential rules, the BoP analyses information reported on a systematic basis by all of those institutions subject to its supervision. This mandatory reporting is defined and specified in instructions and notices published by the BoP, which is also entitled to conduct visits and inspections on its own initiative, having unlimited access to all premises and systems for such purpose.

As far as banks acting as financial intermediaries are concerned, reference is also made to the CMVM as the relevant supervising entity for activities integrating financial intermediation and the conduct of business in capital markets generally. Supervision by the CMVM focuses on the monitoring of all products and securities that are trading or placed in organised capital markets and on the granting of licences and permits that are necessary for the professional exercise of financial intermediaries' activities, as well as on the level of compliance by these entities with market rules and the requirements for the operation of capital markets generally.

The CMVM also has the capacity to publish rules and regulations covering the relevant segments of financial activity and there are various instructions that are issued by the CMVM covering many aspects, including rules on the disclosure of information imposed on either (or both) issuers of securities and on the activities of financial intermediaries.

In its supervising capacity and within its powers, the CMVM complies with the main goals as supervising entity for the capital markets, namely, fostering the protection of investors, particularly those designated as 'not professional' or 'not qualified', by promoting efficiency, equity, security and transparency of financial markets.

ii *Management of banks*

The BoP has a key role to play as it establishes the rules governing the prevention of entry into the market of institutions that could jeopardise the stability of the financial system. The requirements for the taking up of business (also applicable to the acquisition of relevant participations in existing entities, particularly relevant when they contain an element of control or participation in the management of the relevant entity) may be broken down into three main groups, with different but interrelated goals:

- *a* suitability and professional qualification of the members of the management and auditing boards and fitness of character of shareholders – contributing to increase the efficiency of the system as a whole and maintaining the confidence of depositors and other consumers of financial services;
- *b* feasibility of the programme of operations – this relates to profitability levels that guarantee the long-term solvency of the institution as well as the safety and security of its operations; and
- *c* human, technical and financial resources that allow for adequate management and control of risks underlying financial activities – they create a minimum basis for the protection of the entities forming part of the financial sector and help prevent contagion effects and systemic risks.

The setting up of banks is subject to prior authorisation by the competent authority, which is normally the BoP except in exceptional situations where this power has been retained by the Ministry of Finance.

The establishment of a branch is initiated by supervising authority in the local jurisdiction and then communicated to the BoP, along with the information requested by the latter, which includes:

a the country in which the proposed branch is to be established;

b a programme of operations, setting out, *inter alia*, the types of business envisaged and the structural organisation of the branch;

c the address of the branch in the host country;

d the identity of those responsible for the management of the branch; and

e the scope of activity to be authorised.

When the branch originates in a non-EU Member State, the process is essentially assessed by the BoP in the same way as would apply to the creation of a local bank and the branch is required to hold allocated capital. In these cases, the capital earmarked for operations to be carried out by the branch must be sufficient to adequately cover such operations and be no less than the minimum amount required by the Portuguese law for banks of the same type.

Banks with their head offices in other EU countries may also provide services, even if those institutions are not established in Portugal, once the BoP has received the relevant information from the competent authority in their home country on the activities that the institution intends to carry on in Portugal.

In terms of decision-making policy, a general 'four eyes policy' is required to be implemented by all banks and branches operating in the country, irrespective of whether they qualify as international subsidiaries of foreign banks or local banks. Branches operating in Portugal are required to have such decision-making powers that enable them to operate in the country, but this requirement generally does not prevent them from having internal control and rules governing risk exposure and decision-making processes, as is customary in international financial groups.

Referring to the latest restrictions on remuneration of management members and employees of banking groups, reference must be made to compliance with the latest international principles and recommendations set out by the Financial Stability Board, including those published following the recent financial crisis. In this respect, the BoP has issued several recommendations to be taken in a 'comply or explain' perspective, which requires justification in a case of non-compliance by the supervised financial institution. Financial institutions should therefore adopt a remuneration policy consistent with effective management and risk control, avoiding excessive risk exposure and potential conflicts of interest, and being coherent in its objectives, values and long-term interests. Remuneration policy should be appropriate to the size, nature and complexity of the activity being carried out or developed by the bank and, in particular, with regard to the risks taken or to be taken.

Banks should adopt a clear, transparent and appropriate structure on the definition, implementation and monitoring of the remuneration policy, which objectively identifies which employees are involved in each process, as well as their roles and responsibilities. The implementation of this remuneration policy must be monitored by the parent company for its subsidiaries on an annual basis.

iii Regulatory capital

Capital requirements for banks are of prime importance for financial stability in the sense that they are intended to minimise the probability of bank failure at reasonable cost.

The role of capital requirements works at least in two ways: it provides a loss-absorption cushion for unexpected events and, if properly designed, introduces incentives for banks to limit the risk of their activities.

The Capital Requirements Directive was implemented into the Portuguese legal framework through Decree-Laws 103/2007 and 104/2007, both dated 3 April 2007. In general terms, Decree-Law 104/2007 sets out the obligations concerning the minimum level of own funds and the risk limits that banks have to comply with. According to this Decree-Law, and regarding credit risk and risk reduction of the amounts receivable in respect of all activities (except those concerning trading-book and illiquid assets that are deducted from own funds), banks must have own funds that are at all times higher than or equal to 8 per cent of the total weighted exposure risk. The total weighted exposure risk calculation methods used by Portuguese banks may be distinguished between the standardised approach or the internal ratings-based methods as specifically defined in the aforementioned legislation.

Institutions are thus obliged to comply with the regulatory capital provided therein aiming to protect themselves (and the market in general) against all their exposure. This legislation is further regulated by several notices and instructions issued by the BoP (for example, the requirements to be complied with by the banks in respect of securitisation transactions, as provided for in Notice 7/2007 of the BoP dated 18 April 2007).

Another important weapon in controlling a given bank's exposure exists in imposing limits on the concentration of exposures to a single client or group of connected clients (i.e., a group of clients so interconnected that, if one of them were to experience financial problems, the other or all of the others would be likely to encounter repayment difficulties). Specifically, the range of exposures to one client (or group of connected clients) must not exceed a given percentage of the banks' own funds.

Under the scope of prudential rules, there are also limits on holdings in other companies as well as limits on the holding of real estate assets that, whenever not used for the installation of the bank's own services, may only be held for a period of three years (extendable to five in certain situations) when they result from the enforcement of security or from other recovery measures in respect of credit exposure.

In addition, in order to avoid conflicts of interest, there are limits on loans to shareholders with qualified holdings, and loans to members of the management or supervisory bodies are prohibited (unless when for purposes specified in the law).

Decree-Law 104/2007 also establishes the rules that parent banks acting in Portugal, as well as banks controlled by parent financial companies in Portugal or in other EU Member States that are supervised on a consolidated basis by the BoP, must comply with, particularly in respect of consolidated financial positions, large exposure limits and own funds requirements.

IV CONDUCT OF BUSINESS

Banks, while conducting their business, must ensure that their clients are treated with high levels of technical competence in all the activities that they carry out, providing their business organisation with the human and material resources required to ensure appropriate conditions of quality and efficiency. We would make the following particular points:

a In respect of market conduct supervision, banks must:
- act expeditiously;
- provide information and assistance to customers;
- comply with the general regime on advertisements;
- adopt codes of conduct and disclose them to customers, including, through the bank's website; and
- impose professional secrecy, binding to all members of management and auditing boards, employees, representatives, agents and other persons providing services to them on a temporary or permanent basis. Facts or data subject to professional secrecy may only be disclosed to the BoP, the Portuguese Securities Market Commission, the Deposit Guarantee Fund and to the Investor Compensation Scheme, within the scope of these institutions' powers; similar confidentiality duties are imposed on their officers and agents under the terms laid down in the criminal law and the law of penal procedure (being subject to imprisonment of up to one year), except when any other legal provision expressly limits the obligation of professional secrecy, or upon the client's authorisation transmitted by the institution.

b In respect of prudential supervision:
- the initial capital of banks set up originally or as a result of alterations to the purpose of a given company, or of a merger of two or more banks, or of a split, shall be no less than €17.5 million. Likewise, the own funds of banks is at all times required be less than the minimum capital;
- banks shall invest their available funds in such a way so as to ensure appropriate levels of liquidity and solvency at all times;
- own funds shall never be lower than minimum equity capital, and at least 10 per cent of net profits in each fiscal year must be allocated to the building up of legal reserves up to the amount of equity capital;
- no less than 10 per cent of the net profits of a bank for each fiscal year must be earmarked for the building up of a legal reserve, up to an amount equal to the capital stock or to the sum of its set up free reserves or the carried forward results, if higher; and
- banks shall also build up special reserves to strengthen their net worth or to cover losses that their profit and loss account cannot support.

In the case of non-compliance by banks with these rules, the BoP may rapidly adopt the measures or actions that are needed to remedy the situation, by issuing recommendations and specific determinations and when necessary, by imposing fines that can amount to

€2 million and related penalties (in case of breach of the professional duties including banking secrecy, banks may even be subject to heavier penalties).

Of importance with respect to the conduct of banking business in Portugal over the past few months is to note that the BoP has invested significantly in the 'behavioural supervision' aspect and insisted on undertaking a policy devoted to the protection of customers of banking and financial products.

Along these lines, the BoP has published semi-annual reports covering behavioural aspects of banking in Portugal and took a more active position as a mediator of conflicts between consumers and banks. With the implementation of the 'twin peaks' supervision model, this is a tendency that will certainly increase (particularly if the behavioural supervision is located within the scope of the new regulatory and supervisory authority, it is likely to devote more efforts and resources to these matters).

V FUNDING

The funding strategies of banks have changed substantially as a result of the financial market crisis. The economic environment prior to the crisis favoured funding structures that were highly dependent on ample liquidity. When that liquidity ceased to be available, banks that relied heavily on market funding were forced to make significant adjustments, not only to their funding strategies, but also in some cases even to their business models. This was necessarily the case with Portuguese banks that had been adapting their funding structures to cushion the impact of this turbulence on their activity, profitability and solvency.

The groundwork for this adjustment has been the expansion of customer funds, deposits as a source of funding playing an important part in the improvement concerning the structural liquidity situation of the Portuguese banking system. Risk aversion on the part of investors became the watchword and substantial withdrawals from unit investment funds became the norm. Portuguese banks have also used their avenues of recourse to central banks, in line with what happened with other European banks, even though they have also managed to maintain some access to wholesale debt markets.

Over and above this, during the financial crisis, the Portuguese banks managed to continue to issuing debt in the markets in spite of the hurdles that had to be overcome to accessing financing in the markets for securitised debt, especially for maturities in the medium to long term. Maturities became shorter, and the funding costs were higher (spreads wider and fees or commissions payable to arrangers, dealers and brokers also increased). There was consequently a big fall in the net flow of liabilities represented by securities in this period. In spite of this, Portuguese banks succeeded in issuing a substantial volume of debt over the year 2008, there being, however, a big fall in the overall net issuance of bonds, which were the main source of financing through securitised debt, with a considerable part seeming to be earmarked for refinancing debt that was contracted in previous years.

Portuguese issuers also completed several Euro medium-term note-type (mostly using programmes established for such purpose, but sometimes simply on standalone basis) or similar issues, which have been placed in both European and US markets.

In what may be seen as another interesting development in Portuguese debt capital markets, the use of foreign-based vehicles (for instance, the Dutch BV legal vehicle) became increasingly less popular, as issuers turned themselves to Interbolsa notes, cleared and settled through a Portuguese-based system directly connected to international clearing systems and benefiting from a withholding tax exemption on interest payments made to investors located in white-listed jurisdictions.

There are still persistent difficulties hindering access to this type of finance, however, the guarantees provided by the Portuguese government to the issue of debt securities by the banks (to be analysed in more detail on the last chapter and important not only for the amounts issued thereunder but for the mere availability thereof as a last recourse in favour of Portuguese banks) were also important, easing the refinancing of liabilities in the markets during the most critical times.

VI CONTROL OF BANKS AND TRANSFERS OF BANKING BUSINESS

i *Control regime*

The National Council of Portuguese Financial Supervisors ('NCFS'), comprising the BoP, the CMVM and the ISP, has been focused on better regulation measures aimed at improving transparency and control over qualifying holdings within the Portuguese financial sector.

In this context, the NCFS published a preliminary draft proposal for the implementation into Portugal of European Directive 2007/44 of 5 September 2007, referring to the procedural rules and evaluation criteria for the prudential assessment of acquisitions and of the increase of holdings in the financial sector ('the Directive'). The envisaged implementation directly targets banks, insurance companies and investment companies and, therefore, will trigger amendments to the respective existing legal frameworks.

In strict compliance with the Directive, the proposal deals with the prudential assessment by supervisory authorities of acquisitions and increase of qualifying holdings. For such purpose, the proposal establishes disclosure obligations for the proposed acquirer whenever, by virtue of an intended acquisition or increase in qualifying holdings in a financial institution, the proportion of the voting rights or of the capital held reaches or exceeds 10 per cent, 20 per cent, one-third or 50 per cent, or whenever the relevant financial institution becomes its subsidiary. Naturally, these thresholds relate solely to banking of financial supervision requirements and we would note additionally that these matters need also to be seen in light of the disclosure requirements applicable to banks and financial entities that also qualify as listed or 'open' entities, as precisely happens in the case of the major Portuguese banks.

While assessing qualifying holdings, supervisory authorities shall, in order to ensure the sound and prudent management of the relevant financial institution – and having regard to the likely influence of the proposed acquirer on such financial institution – appraise the suitability of the proposed acquirer and the financial soundness of the proposed acquisition.

In this regard the following criteria should be taken into account: (1) reputation of the proposed acquirer; (2) reputation and experience of any person(s) that will direct the business or participate in the management and supervision as a result of the proposed acquisition; (3) the financial soundness of the proposed acquirer; and (4) whether there are reasonable grounds to suspect that, in connection with the proposed acquisition, money laundering or terrorist financing is being or has been committed or attempted, or that the proposed acquisition could increase the risk thereof.

Additionally, and in what concerns the likely influence of the proposed acquirer, Portuguese supervisors are expected to provide general guidance on when a holding in the equity of a bank or financial entity would be deemed to result in significant influence.

In order to determine whether the criteria for a qualifying holding are met, the voting rights as well as the conditions regarding aggregation thereof that are already laid down in Articles 20, 20A and 21 of the Portuguese Securities Code will now be imported into the legal frameworks of all financial undertakings, thus allowing an essential harmonisation of criteria, not only among financial sector players, but also among the issuers of shares admitted to trading on regulated market. In essence, this will mean that the criteria for imputing rights will be enlarged to cover all cases of indirect control or ability to influence the exercise of voting entitlements.

ii Transfers of banking business

The more relevant transactions regarding the transfer of banking business in the Portuguese legal framework are the transfer of commercial undertakings integrated within the activities of banks and, in respect of corporate reorganisations, mergers and demergers.

Transfer is a type of an asset deal, which has as direct object the commercial undertaking of the bank itself or of a part of its business relationship within a certain clientele. This transaction usually aims at ensuring the transfer of each and every element of the relevant business undertaking as an ongoing concern and has been construed as a business that must necessarily be announced to third parties (including the concerned employees) in writing, under penalty of nullity. However, the absence of a specific legal regime governing transactions of this nature leads to the necessity of complying with different legal rules foreseen in respect of each class of elements of the transferred company, such as:

a in respect of real property, transfer implies the need of a formal legal act and the update of the applicable and registration extraits;

b in respect of moveable property also enjoying some sort of registration, the need for such registration to be updated; or

c in respect of credits or debits, the possible need for consent of the relevant third party(ies) and/or their notification, depending on their position being either active or passive.

The transfer of a business concern is, therefore, a process of business transmission governed by both principles of unity of legal title (which is reflected in the transfer agreement in itself) and of diversity of modes of circulation of the various assets contained therein, as set out in specific transmission laws.

The uniqueness of this process (making it often particularly complex and time-consuming) forces necessarily a case-by-case analysis, in order to determine what procedures and steps need to be accomplished to ensure that the right result is provided for and to avoid the transfer affecting in a negative way the maintenance of the business and the relationships with clients and third parties in general.

Since the universal and automatic transmission of contracts, credits and debits is not as such provided for in the Portuguese legal framework applicable to transactions of this type, it needs to be governed by general civil rules, therefore forcing creditors' consent to be obtained for the transfer to take place and imposing the requirement that debtors be notified thereof.

Exception should be made in respect of transfers of credits, when an express or tacit agreement to this effect is obtained upfront between the transferor and the relevant parties. This usually requires a case-specific analysis to be conducted in order to ensure that the transfer becomes enforceable against each consumer (as debtor) only upon notification or acceptance by the latter (no express consent being then required).

Please note that the aforementioned elements (contracts, credits and debits) may also be transferred in part or individually on an asset-by-asset basis. Should this be the case, the consent notification rules stated in the paragraphs above should be complied with in respect of any transferred asset, but naturally this will also have to be seen in light of the contracts governing the relevant situations.

In respect of corporate reorganisations, in particular, mergers and demergers, a specific legal regime is applicable much in line with the other EU legislation. Thus, mergers and demergers are complex legal transactions, the validity and effectiveness of which is subject to a wide range of legal steps and procedures, in particular, merger proposal, internal and external audit, approval by board members, register and publication requirements, etc.

The effects of such transactions are characterised by a unitary legal regime resulting in the transmission of the entirety of the absolved, merged or demerged entity without the need for any individual compliance requirement with transmission laws in respect to the various components forming part of the relevant transaction, under a principle of universal transfer (such as real estate, contracts, credits, debits etc.).

However, it must be borne in mind that, under the contractual freedom principle established on the Portuguese legal framework, this set of rules may not be applicable whenever this is otherwise agreed between the parties, as provided for in the working of any relevant agreement entered into in respect of the analysed transactions.

VII THE YEAR IN REVIEW

In the context of the international financial crisis, and the consequent breach of investors' confidence and the increase of the difficulties in liquidity raising, the Portuguese state provided, until December 2009, an optional guarantee scheme for debt issues to be made by banks through Law No. 60-A/2008 of 20 October, approved by the European Commission as a valid state aid measure aimed at assisting the financial sector in the handling of the liquidity crisis, making available a total of €20 billion for guaranteeing debt issuances of up to three years (or five years, in exceptional cases).

In total, no less than seven Portuguese banks entered into these state-guaranteed deals, for a total issued amount of almost €5 billion, a number that falls much short of the original expectations, evidencing therefore the agility banks have shown in accessing other sources of liquidity and in extracting an advantage from using the covered bond route that had been opened only in 2006.

Notwithstanding the above guarantee scheme and the relevance thereof it is worth mentioning that several senior (non-guaranteed) bonds were also issued in 2009, something that certainly represents a positive sign as to the stability of the financial system in Portugal.

Understanding the mortgage credits market as the main cause of the credit crunch associated with sub-prime housing financing, the Portuguese legislator gave heed to an asset of main importance: housing. In such context, three Decree-Laws were enacted in the past year with a view to granting more flexible conditions to have access to mortgage loans, precisely recognising the importance of this sector for the economy of a small and peripheral jurisdiction having, however, many pros for the housing market, such as a vivid second housing market benefiting from tourism and many Portuguese immigrant communities spread throughout the world.

In this respect, new information duties on promotion of financial products and services which the client is invited to contract in order to obtain reduction of spread and the reduction of other mortgage loan connected expenses were implemented, trying to keep the momentum for the housing market.

New rules concerning consumer loans were also implemented through the transposition of Directive No. 2008/48 setting new pre-contractual duties to be performed by banks, in particular:

- the obligation to assess the solvency of the borrower, through the confirmation of the information rendered by the latter and consultation of the BoP's Central Credit Register; and
- additional data to be made available to the consumer and the manner of their rendering has been harmonised, so that the delivery of a normalised information chart has also become mandatory.

Several regulations were also issued by the BoP on bank deposits, imposing information duties to be rendered to the public on the taking of simple bank deposits (in particular, the duty to deliver a normalised information sheet and the definition of the minimum elements to be reflected in the bank extracts) and to the BoP on the distribution of indexed deposits and dual deposits.

VIII OUTLOOK AND CONCLUSIONS

Pursuant to the international financial crisis, the banking activity in Portugal has been adapting itself to a new reality as well as trying to respond and react to the difficulties that have emerged since 2008: the implementation of a new and more demanding kind of supervision model, a different remuneration policy in respect of payments to management and employees of banking groups, as well as a substantial change of the funding strategy due to the absence of liquidity on funding structures that were highly dependent on it, are examples of an ongoing effort that was made in this direction.

All the aforementioned measures prove that the effort made by the banks as well as by their regulator(s) reflects that the Portuguese financial system has endured the crisis reasonably well, overcoming market hurdles and presenting a robust legal background.

However, recently, Fitch ratings downgraded the state of Portugal from AA to AA– due to significant budgetary underperformance in 2009, by virtue of a general government deficit that greatly increased during 2009, reaching a mark corresponding to 9.3 per cent of gross domestic product, which was much higher than the 6.5 per cent forecast on September 2009. This downgrading has already had direct consequences in the banking system since, on 25 March 2010, the same rating agency downgraded the public sector-covered bonds of the Portuguese bank Caixa Geral de Depósitos from AAA to AA+.

The question now becomes how Portugal will react to recent developments, particularly if the banking system will endure its capacity to remain afloat during this long and endless crisis.

On the political front, the parliament has given a positive sign in late March 2010 when it approved a stability pact covering a three-year period and attempting at cost to keep public budgetary deficits under control.

The financial front also seems to be coping but we will certainly have to wait and see how the Portuguese cope against greater adversity. A push from the south Atlantic and namely from countries with long and well-established ties with Portugal such as Brazil and Angola will certainly prove helpful and we are already feeling such positive influences in the market.

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