EUROPEAN CENTRAL BANK

EUROSYSTEM

OPINION OF THE EUROPEAN CENTRAL BANK

of 12 November 2010

on the Banco de Portugal's staff remuneration and the budget

(CON/2010/80)

Introduction and legal basis

On 25 October 2010, the European Central Bank (ECB) received a request from the President of the Portuguese Parliament for an opinion on several provisions of the draft law containing the annual State budget proposed by the Government for 2011 (hereinafter the '2011 draft budget law'). Once approved, such provisions will apply to the whole public sector, including the Banco de Portugal (BdP)[1].

The ECB's competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union and on the third indent of Article 2(1) of Council Decision 98/415/EC of 29 June 1998 on the consultation of the European Central Bank by national authorities regarding draft legislative provisions[2], as the 2011 draft budget law relates to the BdP. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. Purpose of the 2011 draft budget law

1.1 The 2011 draft budget law contains exceptional austerity measures, mostly focusing on tax increases and public spending cuts. The Portuguese Government deems these measures necessary for the progressive stabilisation of public finances, which it proposes to achieve through the reduction of the budgetary deficit to 4.6 % of GDP in 2011.

1.2 The planned measures are not only aimed at restoring the budgetary balance but also Portugal's reputation in the international community, thereby ensuring the regular financing of the economy and the sustainability of social policies. The measures will apply without exceptions and supersede all currently applicable *lex specialis* regimes, collective bargaining agreements and individual employment contracts.

1.3 The draft provisions on which the ECB is consulted will directly affect the BdP from 1 January 2011 in the following ways:

1 Pursuant to Article 2(1) of Law No 3/2004 of 15 January on public institutes, the BdP is part of the indirect administration of the State. See also paragraph 3.1 of this Opinion.

2 OJ L 189, 3.7.1998, p. 42.

(a) Article 17 introduces a progressive reduction rate up to 10 % on the excess amount of gross total monthly remunerations above EUR 1 500 earned by staff and members of decision-making bodies;

(b) Article 20 introduces the same reduction rate to the amount paid to any person under a service provision contract. The conclusion or renewal of such contracts requires the prior authorisation of the Ministry of Finance. Failure to obtain authorisation could mean that such contracts are declared void;

(c) Article 22 prohibits the BdP from awarding its staff or managers any salary increases, performance-related bonuses or cash payments of a similar nature. In addition, the BdP is prohibited from: (i) opening procedures for promotion to specific positions and it must suspend any such ongoing procedures, (ii) granting any seniority-based automatic career progression, and (iii) undertaking career restructuring or reclassifications, until 31 December 2011 at the earliest. Acts carried out in breach of the above will be void and will result in the persons responsible for such acts incurring civil, financial and disciplinary liability;

(d) Article 25 prohibits the BdP from hiring or recruiting any new staff, regardless of the type and duration of the employment relationship, unless exceptionally justified by a significant public interest. In such case, the BdP is to provide information on recruitment on a quarterly basis to the Minister for Finance.

1.4 In addition, the 2011 draft budget law caps the amount of the meal allowance, prohibits the award of variable performance-related pay to managers and officers and imposes a tax surcharge of 10 % on any pension payments by the BdP exceeding EUR 5 000 per month.

2. General observations

2.1 The ECB understands and very much welcomes that the 2011 draft budget law is intended to serve the purpose of reducing public expenditure.

2.2 The President of the Parliament has requested the ECB to deliver an opinion by 12 November 2010. The ECB notes that, in cases of particular urgency which do not allow for the normal consultation period, the consulting authority may indicate such urgency in its consultation request and ask for a shorter deadline for the adoption of the ECB's opinion. However, even though the ECB welcomes this consultation request and understands the need for an accelerated legislative procedure, it would have appreciated being consulted by the authority preparing the draft legislation at an earlier stage.

2.3 Article 4 of Decision 98/415/EC requires Member States to ensure that the ECB is consulted at an appropriate point in time to allow the consulting authority to take its opinion into consideration before deciding on the substance of the draft legislative provisions. The ECB therefore expects that the consulting authority will take any additional measures necessary to reflect the ECB's opinion to the extent appropriate. It also encourages further consultation on any new amendments to the adopted law or any related implementing measures which fall within its field of competence, provided that such measures do not merely constitute the implementation of the ECB's recommendations. More generally, internal administrative procedures should be in place to ensure that timely consultation of the ECB is taken into account whenever such consultation is mandatory.

3. Specific observations

3.1 *Scope of the draft legal provisions*

3.1.1 In the absence of an express exemption, the provisions apply to the BdP and to its Pension Fund[3], even though they are not specifically mentioned. Since the BdP is statutorily classified as a public institution governed by a *lex specialis*[4], it simultaneously falls within the corresponding category of addressees foreseen in Article 17(9)(q) and (s) of the 2011 draft budget law.

3.1.2 For this reason, the spending cuts and additional fiscal surcharges on salaries and pensions provided in the 2011 draft budget law will directly affect the members of the BdP's decision-making bodies and its staff.

3.2 *Central bank independence*

The 2011 draft budget law has implications for central bank independence, in particular financial and institutional independence, as well as the personal independence of the members of the BdP's decision-making bodies.

Financial independence

3.2.1 The concept of financial independence is assessed from the perspective of whether any third party is able to exercise either direct or indirect influence, not only on the performance of a national central bank's (NCB) tasks, but also on its ability, both operational in terms of manpower and financial in terms of appropriate financial resources, to fulfil its mandate[5]. As stated in the ECB's convergence reports[6] and several ECB opinions[7] on issues concerning autonomy in staff matters, as provided for under Article 130 of the Treaty, a Member State may not impair the ability of its central bank to employ and retain the qualified staff necessary to perform independently the tasks conferred on it by the Treaty, the Statute of the European System of Central Banks and of the European Central Bank (hereinafter the 'Statute of the ESCB') and national legislation. In addition, a Member State may not put its NCB in a position where it has limited or no control over its staff, or where the government of that Member State can influence its policy on staff matters. Autonomy in staff matters extends to issues relating to staff pensions.

3.2.2 In order to protect the BdP's autonomy in staff matters, the Portuguese authorities are under an obligation to ensure that the specific set of draft provisions on which the ECB was consulted, and

3 See Article 48(1)(e) of Law No 3/2004.

4 According to Article 48(2) of Law No 3/2004.

5 See, for example, the ECB's Convergence Report 2007, p. 20.

6 See, for example, the ECB's Convergence Report 2010, p. 23.

7 See Opinions CON/2008/9, CON/2008/10, CON/2009/15, CON/2009/45, CON/2009/47, CON/2010/42, CON/2010/51, CON/2010/56, CON/2010/58, CON/2010/59 and CON/2010/69. All ECB opinions are published on the ECB's website at www.ecb.europa.eu.

which are set out in paragraph 1.3, are decided on by the competent Portuguese authorities in close cooperation with the BdP[8]. Such cooperation must ensure the ongoing ability of the BdP to perform independently the tasks conferred on it by the Treaty, the Statute of the ESCB and national legislation. To this end, the BdP should be involved in drawing up the relevant parts of the draft legislative provisions in an effective manner so as to safeguard central bank independence. Taking this into account, effective cooperation with the BdP would require:

(a) that the competent Portuguese authorities invite the BdP in a timely and transparent manner to consider whether the overall objectives of the 2011 draft budget law can be achieved without affecting the BdP's ability to carry out its tasks and, if so, to present the measures the BdP intends to autonomously implement in the area of staff matters, and in particular staff remuneration, for the purposes of achieving the overall objectives of the 2011 draft budget law; and

(b) that the BdP's position is properly considered and reflected in the 2011 draft budget law prior to its final adoption with a specific focus on ensuring the BdP's ongoing ability to carry out its tasks.

Opinion CON/2010/58 provides a good example of effective cooperation between a government and an NCB. The Italian legislative provisions exempted the NCB from its scope, while at the same time inviting the NCB to consider, taking into account its own legal order, whether the underlying reasons for the legislative provisions can be achieved without prejudicing the performance of the NCB's tasks under the Treaty, the Statute of the ESCB and national legislation. The Portuguese authorities could follow the same or a similar approach in order to achieve effective cooperation and to safeguard central bank independence.

3.2.3 In the light of the BdP's expanded tasks, including in the fields of consumer protection and the increased prudential supervisory responsibilities, notably in the field of macroprudential supervision, the ECB is particularly concerned that qualified and sufficient human resources will be required, in addition to adequate financing. The ECB refers to Opinion CON/2007/29 which highlighted the importance of having appropriate and available resources to ensure BdP's performance of the new tasks[9].

3.2.4 The combination of salary reductions with the prohibition on both: (a) hiring or recruiting new staff, unless exceptionally justified by a significant public interest accompanied with the duty to provide information on recruitment on a quarterly basis to the Minister for Finance; and (b) undertaking career restructuring, promotions or reclassifications, directly impairs the ability of the BdP to employ and even possibly retain qualified staff and may amount *de jure* to depriving its decision-making bodies from their powers of internal organisation and control over staff, or at least to significantly limiting them.

8 See Opinions CON/2008/9, CON/2008/10, CON/2009/15, CON/2009/45, CON/2009/47, CON/2010/42, CON/2010/51, CON/2010/56, CON/2010/58, CON/2010/59 and CON/2010/69.

9 Opinion CON/2007/29, paragraph 2.5.

3.2.5 The ECB is not aware of any cooperation between the Portuguese authorities and the BdP in drawing up the 2011 draft budget law. The ECB understands that Parliament is currently debating the 2011 draft budget law, and therefore the BdP could still be given the opportunity to express its views to accommodate a specific legal solution subject to the general qualifications made in paragraph 3.2.2. In this regard, the ECB understands that the BdP's remuneration structure differs from that of the rest of the public sector, which is an additional reason that effective cooperation is necessary in order to take account of this difference, including any possible distortive effects. Absence of effective cooperation as set out in paragraph 3.2.2 would amount to a serious infringement of the principle of central bank independence.

Institutional independence

3.2.6 Article 130 of the Treaty prohibits third parties from giving instructions to NCBs and requires governments of the Member States to respect this prohibition. Under the current regime, the BdP enjoys statutory autonomy in determining its personnel policy[10] and the BdP's staff are subject to individual employment law and collective bargaining agreements entered into between the BdP and banking sector unions[11], which are complemented by internal rules.

3.2.7 The proposed changes to the 2011 draft budget law represent a departure from this current regime. In particular, the 2011 draft budget law indirectly requires the BdP to take specific personnel measures, i.e. not to hire or recruit new staff, unless exceptionally justified by a significant public interest accompanied with the duty to provide information on staff recruitments on a quarterly basis to the Ministry of Finance, and not to undertake career restructuring, promotions or reclassifications.

3.2.8 Taking into account that these measures go beyond what is considered necessary to give full effect to the objective of reducing public expenditure, it would be a breach of the BdP's institutional independence if such requirement would lead to an authorisation procedure whereby staff recruitment by the BdP could be rejected by the Ministry of Finance. The ECB considers that the exception from this requirement provided in the 2011 draft budget law based on a significant public interest reason does not offers sufficient safeguards for the protection of central bank independence and therefore recommends that it be amended.

Personal independence

3.2.9 The 2011 draft budget law not only affects the remuneration of the BdP's staff, but also that of the members of its decision-making bodies. Article 130 of the Treaty requires governments of the Member States to respect the principle of central bank independence and not to seek to influence the members of an NCB's decision-making bodies in the performance of their tasks. To comply with the Treaty requirements with regard to personal independence of members of decision-making bodies, any adjustments to the salaries of the Governor and other members of the BdP's decision-

10 Article 57 of the Organic Law of the BdP.

11 Article 56 of the Organic Law of the BdP.

making bodies who are involved in the performance of ESCB-related tasks should not affect the terms under which they have been appointed[12] and should only apply to future appointments.

3.2.10 The ECB understands that the proposed legislative changes apply not only to the BdP's decision-making bodies, but also more generally to the management of public institutions in Portugal and as such are not seeking directly or indirectly to influence the BdP's decision-making bodies in the performance of their tasks. However, the ECB considers that the 2011 draft budget law provisions may not be considered compatible with the principle of personal independence unless the qualifications made in respect of the principle of financial independence are taken into account.

3.3. *Prohibition of monetary financing* - *use of the funds resulting from the reduction in salaries*

3.3.1 The provisions on NCB salary reductions must also comply with the monetary financing prohibition laid down in Article 123 of the Treaty, as further clarified in Council Regulation (EC) No 3603/93 of 13 December 1993 specifying the definitions for the application of the prohibitions referred to in Articles 104 [now 123] and 104b(1) [now 125(1)] of the Treaty[13]. This provision prohibits overdraft facilities or any other type of credit facility with the ECB or NCBs in favour of Union institutions, bodies, offices or agencies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States, and the purchase directly from these public sector entities by the ECB or NCBs of debt instruments. With a view to preserving the integrity of the NCB's balance sheet, the monetary financing prohibition is of key importance in ensuring the primary monetary policy objective of price stability, which must not be impeded. Therefore, the prohibition must be interpreted extensively to ensure its strict application. Even if Article 123(1) of the Treaty refers literally to 'credit facilities', i.e. with an obligation to repay such credit, the prohibition also applies *a fortiori* to other forms of funding, i.e. without an obligation to repay, since it has the overall aim of public finance discipline and of prohibiting NCBs from financing the public sector. This implies that both the ultimate objective and the spirit of this provision must be taken into account in its interpretation[14].

3.3.2 From an accounting perspective, a reduction in staff salaries will reduce an NCB's operational costs, resulting in an increase in its financial results and leading to a potential increase in its financial resources. The principle of central bank financial independence guarantees that the BdP can independently use its financial resources as it sees fit to fulfil its mandate. The ECB notes that the BdP must be fully independent in deciding how to use the funds resulting from any reduction in salaries or pensions that it pays.

3.3.3 Under current Portuguese law, part of the NCB's profits for the fiscal year (80 %) must be transferred to the State as a dividend, or to other reserves proposed by the Board of Directors and approved by the Minister for Finance, as provided for in Article 53(2)(c) of the Organic Law of the BdP. In the absence of effective cooperation with the BdP as set out in paragraph 3.2.2, the 2011

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12 See, for example, Opinion CON/2010/56.

13 OJ L 332, 31.12.1993, p. 1.

14 See paragraph 9 of Opinion CON/2003/27.

draft budget law could be interpreted as restricting the BdP's freedom with respect to staff matters, for example, as regards the hiring of new staff or deciding on promotions of existing staff. Consequently, the BdP would not be seen as having full independence in deciding how to use the funds resulting from the reduction in salaries or pensions. If the BdP is not free to use the increased funds in accordance with the principle of financial independence, this could be considered as an increase in the funding of the Portuguese State at the BdP's expense.

3.3.4 The draft law does not contain any provisions changing the rules on the BdP's profit distribution. In particular, the BdP does not seem to be required to transfer to the State any net savings from the reduction in staff salaries and pensions during the fiscal year. As recently pointed out in Opinion CON/2010/69[15], if the main purpose of the salary reductions was to eventually increase the financial resources of the State through an interim distribution of increased profits from the NCB to the State, this would appear to be a circumvention of the objectives of the prohibition on monetary financing. In this respect, the ECB notes that any financial transfer of this nature from the BdP to the State budget, without the BdP having the opportunity to use the related resources independently for the fulfilment of its tasks, could be assimilated to monetary financing under Article 123 of the Treaty. By contrast, a decrease in the NCB's operational costs with a view to increasing its own financial resources to strengthen the performance of its mandate would be acceptable.

This opinion will be published on the ECB's website.

Done at Frankfurt am Main, 12 November 2010

[signature]

The President of the ECB

Jean-Claude TRICHET

15 See paragraph 3.5.