GOVERNMENT OF THE REPUBLIC OF SLOVENIA

ECONOMIC PARTNERSHIP PROGRAMME

OCTOBER 2013

INTRODUCTION

Economic and fiscal policy guidelines of the Republic of Slovenia for the 2013–2016 period are laid down in the National Reform Programme and the Stability Programme, both adopted in May 2013. The European Commission has examined the two documents and the EU Council has adopted the *Council Recommendation on Slovenia's 2013 National Reform Programme and delivering a Council Opinion on Slovenia's Stability Programme for 2012–2016.*[1]

The EU Council established in July 2013 that Slovenia was still running an excessive government deficit. Slovenia is therefore, in compliance with Regulation *(EU) no. 473/2013 of the European Parliament and of the Council on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of Member States in the euro area,* required to present an Economic Partnership Programme with a consolidation strategy.

The purpose of the document is to provide information concerning the implementation of the recommendations of the European Council and present the priority measures and policies to ensure an effective and lasting correction of the excessive deficit.

MACROECONOMIC FRAMEWORK

In view of the measures for fiscal stability and restructuring of the financial system, the Slovenian economic sector is stabilising gradually. The recovery has been hindered mostly because of the decline in private and investment consumption, which is itself also due to the measures for stabilisation of public finances, since, with a view to achieving fiscal targets, the Government of the Republic of Slovenia, among other things, has reduced the wages of public employees and investment expenditure. The credit crunch, which is a key obstacle to growth, still inhibits corporate financing. The current account surplus in the balance of payments, which guarantees liquidity to the economy, increased to nearly EUR 1.2 million in mid-2013.

A gradual improvement is expected in 2014, when the economic contraction is projected to be slightly lower than in the last two years, i.e. by 0.8 per cent. Exports have already started to strengthen this year and will have a positive effect on economic activity in 2014. However, this effect will be limited, given that the elimination of the credit crunch and the restructuring of the banking system, which are prerequisites for boosting the economy, have been delayed by two quarters because of the requirements of the European Commission to conduct a system-wide bank asset quality review and stress tests. The intensive bank recovery and further consolidation of public finances will also have an impact on the household and general government consumption. The consistency between economic policies, i.e. fiscal and monetary, has decreased, and this does not stimulate growth in the private sector, as the financing conditions have not improved and fiscal policy provides an additional burden.

The situation in the labour market will stabilise in the next two years. The number of registered unemployed persons will hover around the 120,000 mark. This year the employment rate will fall owing to low economic activity and high inactivity rates recorded at the beginning of the year (related to the pension reform) and because of fiscal constraints imposed on the general government sector for the first time. This made the results of fiscal consolidation measures visible. There is still no employment absorption in the private sector, due to the delay in addressing the credit crunch affecting the corporate financing. The number of registered unemployed is thus expected to average at 120,600 in 2013, with ILO

[1] http://ec.europa.eu/economy_finance/economic_governance/macroeconomic_imbalance_procedure/index_en.htm

unemployment rate at 10.7%. The average gross wage this year will decrease in nominal terms, due to the reduction of wages in the public sector, while next year it may slightly increase on account of a strengthened private sector.

Inflation remains steady and this year, despite the rise in VAT in July, is lower than in the same period last year, which points to the limited effect of the increased VAT on final prices. The average inflation rate is estimated at 2.3% for 2013; taking into account the measures adopted in the field of taxation and the absence of price shocks from the international environment, inflation is expected to be lower (1.4%) next year.

The international situation may again stimulate economic activity in Slovenia more than currently expected. Hence the risks of decreased economic activity mainly arise from the domestic environment. The restructuring of the banking system constitutes the main risk. In the event of further delay, lending activity next year may be further decreased, whereas any increase in the scope of funds, needed for the restructuring, would hinder fiscal consolidation.

PRIORITY ECONOMIC POLICIES AND MEASURES TO ENSURE THE CORRECTION OF EXCESSIVE DEFICIT

1. Reinforcement of the budgetary strategy and correction of the excessive deficit

Recommendation no. 1:
For 2013 and beyond, implement and reinforce the budgetary strategy, supported by sufficiently specified structural measures, to ensure the correction of the excessive deficit by 2015 in a sustainable manner and the improvement of the structural balance specified in the Council recommendation under the EDP. After the correction of the excessive deficit, pursue a structural adjustment effort that will enable Slovenia to reach the MTO, which should be set in line with the Stability and Growth Pact by 2017. Durable correction of the fiscal imbalances requires the implementation of ambitious structural reforms which would increase the adjustment capacity of the economy and boost the potential for growth and employment. Safeguard growth-friendly spending, adopt measures to improve tax compliance and implement measures on the expenditure side underpinned by systematic reviews of public expenditure at all government levels. To improve the credibility of consolidation, complete the adoption of a general government budget balance/surplus rule in structural terms, make the medium-term budgetary framework binding, encompassing and transparent, and strengthen the role of independent bodies monitoring fiscal policy by the end of 2013. Take measures to gradually reduce the contingent liabilities of the state.

1.1 Fiscal Policy Objectives

The Government of the Republic of Slovenia has pursued the achievement of two **key fiscal objectives:**

- structural balance by 2017 and
- the elimination of the excessive deficit of the general government sector by 2015.

To this end, Slovenia has this year adopted an amendment to its Constitution introducing a fiscal rule in the highest legal act and imposing an obligation to plan the annual budget in a manner enabling the attainment of the target.

The correction of the excessive general government deficit below 3% of GDP by 2015 will be attained primarily through further implementation of measures to reduce general government expenditure and measures to increase revenues. The Government has ensured the achievement of objectives through the revised 2013 budget and the amended 2014 budget and, according to the principle of biennial budget planning, has also adopted the 2015 budget. The measures on the revenue and expenditure side ensure a gradual consolidation of public finances in a sustainable manner.

The revision of the 2013 budget was adopted in July. The revised budget takes into account the adjustments due to the deterioration of the macroeconomic situation and introduces new measures. To underpin the dedication to the objective pursued, the Government has decided to restrict the assumption of new budget commitments at national and local levels by the end of the year, as provided for in the Public Finance Act. **The budget for 2014 and 2015**, which was adopted by the Government and sent to National assembly in September, is a continuation of the restrictive expenditure policy and introduces additional revenue-increasing measures to enable the achievement of target deficit values.

Table 1: Public finance trends*

	2013 Estimate	*2014 Budgeted*	*2015 Budgeted*
National budget, cash flow:			
Revenues in EUR million	**7,876.2**	**8,619.3**	**8,638.7**
Expenditure in EUR million	**9,353.6**	**9,641.1**	**9,497.9**
Deficit in EUR million	**1,477.4**	**1,021.8**	**859.2**
Deficit in % of GDP	**4.2%**	**2.9%**	**2.4%**
Government sector, ESA 95			
Deficit in % of GDP	**4.0%**	**3.2%**	**2.5%**

*without bank recapitalisation;.

Measures to strengthen the fiscal framework are based on the amended Constitution of the Republic of Slovenia, with which Slovenia has fulfilled its commitment to include the fiscal rule in the Slovenian legal system and improve institutional regulation in relation to enhanced economic management at the EU level. The stated commitment will be implemented through the following:

- The Fiscal Rule Act (tabled for consideration by Parliament and submitted for comments to the European Commission) will lay down the manner and time-frame for the implementation of the medium-term balance between the revenues and expenditures of state budgets and define the medium-term fiscal target, the fiscal rule itself and the competences of the fiscal council.
- The Public Finance Act, by transposing the implementing provisions into the preparation, implementation and monitoring of the budget of all general government institutional units (besides the national budget, also pension and health insurance funds, municipal budgets and other institutional units which are included in sector S.13 under the Decree on the standard classification of institutional sectors). Strengthened in this manner, supervisory mechanisms for managing fiscal imbalances ensure a medium-term balance.
- The expansion of a single treasury system, which is intended for the streamlining of public finance flows and fund management, for all indirect budget users. The system is to be set up at the state and municipal levels, which includes public finance budgets and budget spending units.
- Constitutional amendment to referendum legislation, which limits the contents on which a referendum can be called to those having no impact on public finances; a referendum can presently be exclusively called by voters (and no longer by deputies or the National Council of the Republic of Slovenia). This has limited the possibilities of slowing down or halting measures and reforms having an impact on public finances.

Measures on the expenditure side comprise:

- wage reduction in the public sector;
- no pension indexation;
- no indexation and reduction of social transfers;
- rational use of current expenditure.

The contribution of the revenue side to fiscal consolidation covers:

- increasing VAT rates;
- introducing the real property tax;
- tax on lottery tickets
- halting the reduction in the corporate income tax rate;
- limiting the indexation of tax reliefs and personal income tax bases;
- measures to improve the effectiveness of tax collection and fight the shadow economy;
- changes to other taxes and allowances.

1.2 Overview of measures – expenditure

Public sector wages. The Government, in dialogue with trade unions, has continued to pursue the policy directed to the reduction of expenditure on labour costs with effects also expected in 2014 and 2015. In July 2013, basic wages in the public sector were again reduced by 0.5 to 5 per cent on 2012 levels, depending on the amount of the wage. In parallel, some allowances and supplements were also reduced (period of employment, specialisation, supplementary pension insurance and sick leave) and payment of "overdue" promotions for employees in the public sector was postponed. The pay for annual leave for 2013 and 2014 was reduced by an average of 50 per cent. A freeze on promotions and the proportion of salary paid to public employees as performance-related bonus was introduced. The Government continues to pursue a restrictive employment policy in the public sector, which is reducing the number of employees by one per cent per year. Hence the agreed measures will decrease total labour costs by an estimated 7% in 2013 and a further 1.5% in 2014 relative to 2012 figures. In the 2015 budget, the Government is providing for a further reduction of labour costs. Since some measures aimed at reducing labour costs are not of a permanent nature, the Government will again enter into negotiations with the public sector trade unions to reach an agreement for 2015. The negotiations should result in an agreement on permanent measures concerning the level of employees' rights and a further reduction in the number of public employees.

In 2014 and 2015, **pensions** will not be subject to indexation and the recreation allowance will be reduced. Savings due to non-indexation of pensions for 2014 are estimated at EUR 46.1 million.

Among **transfers**, the amount of maternity benefit has been limited since mid- 2013,[2] following the limitations for parental benefits and other social benefits and scholarships already introduced in 2012.

[2] With the Emergency Measures in the Field of the Labour Market and Parental Care Act, temporary measures were adopted that relate to the payment of maternity benefit in accordance with the Stability Programme (applicable as of 1 August 2013 until and including the year following that in which economic growth exceeds 2.5% of GDP). The maximum amount of maternity benefit is limited to twice the average monthly wage in the Republic of Slovenia, as provided for by the law regulating the adjustment of transfers to individuals and households, which currently amounts to EUR 2,863 gross per month. This is the same

Restrictions of other expenditure encompass:

- expenditure on goods and services:
    - Proposed amendments to 2014 comprises EUR 138 million less than the revised 2013 budget and almost 172 million less than the realization of 2012
    - Proposal for 2015 provides 102.5 million less available resources according to the revised 2013
- restructuring of subsidies:
    - Subsidies to public enterprises for 2014 have been decreased by EUR 18.8 million according to the 2013 revision, in addition to achieved decrease in the 2013 in comparison to outturn 2012;
    - Subsidies in agriculture are decreased (compared to the expected dynamics in the years 2012 and 2013);
    - In 2014, there are additional EUR 11 million envisaged (according to the revised 2013) to increase job creation through grants to companies and sole traders;
- investment project funds (more for investments in railway infrastructure with a simultaneous reduction of state budget transfers for investments);
    - Restricting capital transfers, which are decreased by EUR 35.5 million for 2014 according to the revised 2013 and 38.4 million in relation to the realization of 2012.
- optimisation of the operations of budget users within the restricted framework of current expenses;
- restriction of the carry-over amount of earmarked budget funds for the purpose of selective planning of and time schedule for implementation of projects;
    - The proposal of the budget execution law for the years 2014 and 2015, provides that in the year 2014 and 2015 2/12 accrued but unused revenue in the previous year can be transferred. This encourages better coordination and timing of investments in the field of environment and transport infrastructure, and limits pressure on the deficit in the coming years as a transferred asset balances for the year charged to expenses in the future (eg in the field of transport infrastructure is a transfer from 2012 to 2013 means approx. EUR 20 million);
- public procurement (joint contracts at the state level, joining organisation of work and computerisation of procurement or contracts related to the healthcare budget and local government).

1.3 Overview of measures – revenues

In July 2013, **value added tax** was increased by two percentage points (from 20% to 22%) at the general rate and by one percentage point (from 8.5% to 9.5%) at the reduced rate. In terms of financial effect, this measure will increase revenue by EUR 100 million in 2013 and by an additional EUR 150 million in 2014.

The reduction in the **corporate income tax rate** will come to a halt at 17% (i.e. from 2014). The measure is estimated to increase general government revenues by EUR 22 million in 2014 and by an additional EUR 25 million in 2015.[3]

type of measure as that applicable to child-care benefit, based on the Parental Protection and Family Benefit Act and the Fiscal Balance Act.

[3] The Act Amending the Corporate Income Tax Act, adopted on 24 September 2013, provides for the adaption of tax provisions to other applicable laws. In terms of the protection of the tax base and administrative simplification, the draft act envisages a measure of thin capitalisation. Two measures have been prepared with a view to adapting tax legislation to other applicable legislation (tax treatment of income or losses arising from debt cancellation in composition proceedings – which is harmonised with the applicable Financial Operations, Insolvency Proceedings and Compulsory Dissolution Act (the ZFPPIPP) – and tax relief for voluntary supplementary pension insurance); these have no impact on public finance revenues.

In the field of **personal income tax**, the Government envisages abolishing automatic harmonisation of tax reliefs and net annual tax bases with the growth in consumer prices. This will increase revenues by approximately EUR 30 million.[4] The measures envisaged by the Government also include the abolition of income tax relief for those older than 65 years, which is expected to increase revenues from personal income tax by EUR 17 million.

A **tax on lottery tickets** has been introduced with an annual effect of EUR 17 million.

The Government has also increased court fees and annual road-user charges.

The revenue-increasing measures that were adopted in 2012 have shown positive effects on public finance in 2013, which is due to the introduction of **carbon tax** on motor fuels (gasoline, diesel fuel). A further raising of the environmental levy by 15% in 2013 is estimated to bring in an additional EUR 50 million of revenues.

The effect of the new **tax on financial services** and of the amended **tax on total assets of banks** is estimated at a total of EUR 51.1 million in 2013.

The introduction of **real property taxation**. Tax on immovable property now accounts for 0.6% of Slovenia's GDP, while it has been shown that it least restricts economic growth. The Government expects that the first financial effects of the stated tax will be achieved in 2014 and are estimated at EUR 205 million.

With a view to improving the **fulfilment of tax liability**, the Government has adopted a comprehensive range of measures to curb the shadow economy and increase the efficiency of tax collection and enforcement. Key areas of action are as follows:

- <u>Supervision of cash operations</u>. July 2013 saw the adoption of stricter provisions relating to the use of computer programs for recording transactions replacing certified cash registers.
- <u>Limitations on cash operations</u>. Tighter restrictions on cash operations are being prepared.
- <u>Prevention of illegal work and employment</u>. The new law, which is to be adopted by the end of 2013, has been presented to the Economic and Social Council through public debate. The law lays down types of work and illegal employment and clearly delineates and expands the competences of supervisory authorities and sanctions.
- <u>Strengthened and better connected inspection services</u>. Enhancing the competences of inspection bodies and their strengthening, including through qualification of customs officers to work as inspectors (upon Croatia's accession to the EU). Strengthened mobile units will increase the presence of inspection bodies in the field. The efficiency will be increased as the result of the planned merger of the Customs and Tax Administrations into a single Financial Administration.
- <u>Construction system and prevention of illegal construction</u>. Keeping appropriate records and addressing the overall scope of illegal constructions, determining conditions and procedures under which certain constructions may be legalised. The Legalisation Act is envisaged for adoption in March 2014 – the law will eliminate the reasons for the occurrence of illegal construction and provide mechanisms for rapid detection of illegal construction and actions to be taken.

[4] Other envisaged changes relate to the harmonisation of the already adopted measures in new sector-specific laws, namely the Pension and Disability Insurance Act and the Employment Relationships Act (changes relating to the assessment of the tax base for income from another contractual relationship, tax treatment of occupational pensions is equal to the tax treatment of compulsory insurance pensions, and the possibility to claim tax relief for voluntary supplementary pension insurance for natural persons engaged in work activity). The proposal envisages the abolition of the special personal relief for cross-border migrant workers as a measure to eliminate the established unconstitutionality of the applicable Personal Income Tax Act.

- <u>Sector-based measures</u> for better regulation and improved records in the field of labour and operations in healthcare, forestry, wine production, bakeries, tourism, transport services, mining, aviation, trade in works of art and music activities.
- <u>Promoting a sense of liability</u>. Improving the tax culture and encouraging the voluntary payment of tax liabilities with an overall communication strategy, while promoting the awareness of citizens of the significance of the shadow economy and its consequences.

2. Long-term sustainability of the pension system and containing aging costs

Recommendation no. 2: *Strengthen the long-term sustainability of the pension system beyond 2020 by further adjusting all relevant parameters, including through linking the statutory retirement age to gains in life expectancy, while preserving the adequacy of pensions. Contain age-related expenditure on long-term care and improve access to services by refocusing care provision from institutional to home care, sharpening targeting and means-testing of benefits, and reinforcing prevention to reduce disability/dependency.*

Slovenia implemented the **pension reform** in 2013 and consequently limited the pressure of age-related expenditure on public finance. A model calculation[5] shows that pension expenditure will remain stable until 2020. Considering the estimated demographic and public finance trends, a more rapid decrease in age-related expenditure is expected after 2020. The effects of the adopted reform and the actual trends in aggregates compared to those anticipated at the time the reform was designed are being analysed in 2013. On this basis, the Government will formulate proposals for any amendments to legislation in the area of pension and disability insurance.[6]

With a view to improving the employability of older persons, **levies on temporary and occasional work of pensioners** were reduced from 25% to 3%.[7] The amendment introduced tax burden relief for these forms of work and made them attractive to both employers and retired people.

With a view to comprehensively addressing population-ageing issues, the Government identified the starting points for drafting an act to regulate **long-term care,** personal assistance and long-term care insurance. The objectives of this new act are to introduce special public insurance for long-term care and to link providers and services into an integrated system ensuring that people dependent on long-term assistance get access to quality services, primarily in their home environment and in community. No increase in social security contributions is envisaged: necessary funds are to be transferred from the existing health insurance and pension and disability insurance funds. In addition, it is proposed to introduce new compulsory supplementary insurance. The adoption of the act is expected in the first half of 2014.

3. Labour market and wages

Recommendation no. 3: *Ensure that wage developments, including the minimum wage, support competitiveness and job creation. Monitor closely the effects of the recent labour market reform and if necessary identify the areas where further action is needed to foster job creation and tackle segmentation, including through*

[5] Confirmed by the Economic Policy Committee (EPC), 2 July 2013.
[6] The Government of the Republic of Slovenia set up a working group to monitor the effects of changes in the regulation of pension and disability insurance in 2013. Its basic task will be to monitor the implementation of the adopted measures and their effect on further development of the pension system (demographic changes, the financial sustainability of the system and amounts of benefits) and to prepare an analysis.
[7] The Act Amending the Labour Market Regulation Act.

the regulation of student work. Take further measures to increase employment of young tertiary graduates, older persons and the low-skilled by focusing resources on tailor-made active labour market policy measures while improving their effectiveness. Address the skills mismatch by improving the attractiveness of the relevant vocational education and training programmes and by further developing cooperation with the relevant stakeholders in assessing labour market needs.

Labour market reform has been introduced this year. Currently, the Government is monitoring the actual effects of the reform with a view to identifying the areas where further action is needed to foster job creation and reduce labour market segmentation.[8]

Amendments to the **Minimum Wage** Act are expected; these aim to contribute to a more equitable system and greater competitiveness.

In the area of **student work**, negotiations are being held with student representatives. The Government is of the view that the tax burden on student work must be increased with a view to making this form of work comparable to employment relationships and holds that the form currently applicable is a labour market anomaly. A new act is envisaged for adoption by the end of March 2014.

With a view to improving employment opportunities for **young people** in Slovenia, employment incentives for employers were introduced. An employer who, during the period of validity of the Act, permanently employs an unemployed person under the age of 30 who has been registered as unemployed for at least one month is fully exempt from paying the employer's contributions (pension and disability insurance contributions, health insurance contributions, parental protection insurance, and unemployment insurance) for the initial two years of the employment. We estimate that the aforementioned incentive will enable 25,000 new employments per year – of which 7,000 will be permanent employments –, compared to 20,000 new jobs provided for young people in 2012 (of which almost 90% were fixed-term employment contracts).

Within the **active labour market policy** measures are focused on vulnerable groups of unemployed (young and older people). The Youth Guarantee Scheme includes measures adjusted to the level of education, while measures targeted at the older generation combine training and employment incentives (the 50+ Programme). A mentoring programme for young and older people was designed with a view to stimulating employers to employ first-time job seekers under 30 years of age and assign them experienced mentors. The programme provides for job sharing between a young first-time job seeker and an older worker who meets the partial retirement conditions.

The Resolution on the National **Youth Programme** 2013–2022 identifies areas, objectives and priorities in education, employment and entrepreneurship, living conditions, health and well-being, and the young and society and recognises the importance of the youth sector and culture, creativity, heritage and the media. It also establishes key orientations and sets the method of monitoring.

[8] **A working group to monitor the effects of changes in the regulation of the labour market in 2013** has been set up. Its tasks are:

- – to identify required amendments to the Employment Relationships Act and the Act Amending the Labour Market Regulation Act important in terms of the objectives and the impact on the labour market (reduced segmentation, increased labour market flexibility, enhanced efficiency of labour law protection);
- – to prepare a list of indicators to monitor and evaluate the effects of changes in the regulation of the labour market;
- – to prepare an analysis of the effects of changes to the labour market in terms of the objectives and other effects on the labour market;
- – to propose potential amendments to legislation and further changes in labour market regulation;
- – to prepare a report on the effects of changes in labour market regulation, the objectives attained and proposals for further changes.

The Employment Service of Slovenia is carrying out a pilot project to assess future **labour market needs**. The life-long career orientation projects are envisaged to encourage these processes within companies, improve the forecasting of future labour market needs and provide the basis for a more accurate forecast of jobs in demand. These forecasts will be used as the basis for designing the scholarship policy and other measures and for better linking the labour market with the education system.

The introduction of new **optional subjects** focused on developing particular interests and abilities among primary school pupils aim to improve their ability to adapt to labour market demands. The amendments to the Primary School Act provide for the opportunity to learn a second foreign language and ensure higher quality of knowledge.

Employers are stimulated to engage in practical training at technical and vocational schools through ESF financial incentives that are expected to expand and also include apprenticeships. The cohesion funds support the operations of regionally organised Business-to-Business Education Centres, which link the economy and education system. Changes in higher vocational education are aimed at better integrating the economy and education and primarily relate to requirements for junior experts teaching at those institutions; these changes are expected to enable graduates to directly engage in the work process.

With a view to **reducing structural unemployment**, the Act Amending the Labour Market Regulation Act limits a target group of unemployed persons for inclusion in public works to long-term unemployed persons (i.e. persons continuously registered as unemployed for more than one year), with a view to ensuring their social and labour market inclusion.[9]

4. Banks and the banking system

Recommendation no. 4
Take the necessary steps, with input from European partners, to contract an independent external adviser by June 2013 to conduct a system-wide bank asset quality review. Complete this exercise in 2013, with faster progress in the cases of the two banks already subject to the state aid procedure in order to accelerate their balance sheet repair. Stand ready to provide additional capital should the asset transfer or asset quality review reveal additional shortfalls. All measures, including objective assessments of capital needs, transfer of assets to the Bank Asset Management Company, the asset protection scheme and operational implementation of the restructuring measures, should be implemented in full compliance with state aid rules where state aid is involved. In parallel, develop by March 2014 and implement a comprehensive sector strategy to ensure arm's-length management of reformed banks and to substantially improve governance, risk management and profitability in the sector, including through consolidation where appropriate. Swiftly proceed with preparations for the announced privatisation of NKBM and establish, by September 2013, an ambitious timetable for the divestment of direct and indirect state shareholdings of banks.

In line with the EU Council recommendations, an independent external adviser has been contracted by the Bank of Slovenia and the Government of the Republic of Slovenia to conduct a system-wide bank **asset quality review** (AQR) and bottom-up stress tests. As recommended by the Council, in addition to the three systemically important banks (NLB, NKMB and Abanka Vipa), Banka Celje, Gorenjska banka, Unicredit banka Slovenije, Hypo Alpe Adria Bank and Raiffeisen banka have also been included in the review under the established criteria. Factor banka and Probanka were also under review until the two became subject to the orderly winding down. The Bank of Slovenia (BS) engaged the Oliver

[9] A long-term unemployed person will receive a wage instead of unemployment benefit (i.e. payment for work in a percentage of the minimum wage as set in Article 52 of the Act plus the reimbursement of the costs of meals during work and travel to and from work covered by the Employment Service of Slovenia), while the entitlement to unemployment benefit will no longer be suspended during the relevant period.

Wyman company to carry out the stress tests and the Deloitte and Ernst & Young companies to conduct the banks' asset quality review. For the purposes of the two reviews, the real estate appraisals will be prepared by several independent real estate appraisers.

The **quality review** includes a verification of the completeness and integrity of data, a review of individual credit operations, classification of clients and transactions with regard to credit rating, and detailed loan security valuations. On this basis and in accordance with international financial reporting standards, the engaged experts are expected to assess the appropriate level of credit impairment for each credit operation in the sample in order to provide an estimate of any potential further impairments. The asset quality review draws on the average historical loss values and the assessed ability to liquidate securities. In addition to an assessment of potential further impairments, a final report must also include a description of the banks' internal control functioning and any inadequate practices concerning security valuations.

The **stress tests** are carried out with a view to assessing potential **need for capital** in the basic scenario context and in the case of increased macroeconomic imbalances in the 2013–2015 period. To this end, the Oliver Wyman Company will use the data obtained by the asset quality review to design a specific model for the Slovenian banking sector, which will ensure an assessment of potential bank losses considering the macroeconomic environment and the ability of the banks to absorb these losses. The model will be used as a basis to assess the impact on the banks, which must ensure at least 9% core Tier 1 capital under the basic scenario and at least 6% under the stress scenario. The time limit for the preparation of the final report for the whole banking system is 29 November 2013. The stress test results will be transparent and clear. The Government plans to transfer a part of non-performing assets from the three biggest banks to the Bank Asset Management Company in accordance with the EU rules on state aid. At the same time, the banks' capital adequacy will be ensured.

On 6 September 2013, the Bank of Slovenia appointed the compulsory administration at two smaller banks to carry out an orderly winding down. For this purpose, the Bank of Slovenia ensures liquidity support to the two banks on the basis of collateral (in part bank assets and in part state guarantees). In accordance with the Measures to Strengthen the Stability of Banks Act and upon receiving a positive opinion from the European Commission, the state issued a EUR 1,030 million guarantee; the final wind-down programme will be prepared by the beginning of November 2013.

5. Regulatory framework for banks and supervisory capacities

Recommendation no. 5:
Review the bank regulatory framework by the end of 2013 and, based on this review, strengthen supervisory capacity, transparency and statistical disclosure.

Slovenia has reviewed the bank regulatory framework and, in order to strengthen it, adopted several amendments to the Banking Act and the Financial Conglomerates Act and also adopted the Act Regulating Measures to Strengthen the Stability of Banks. The amended Banking Act (ZBan-1J) has taken into account all major findings and recommendations provided by the International Monetary Fund in its preliminary assessment, the Financial Sector Assessment Program (FSAP).

Slovenia has **strengthened the powers of the Bank of Slovenia** and introduced additional measures to increase the share capital of banks.[10] This arrangement and pertaining additional measures relating to risk management enable the Bank of Slovenia, as a

[10] The Bank of Slovenia imposes measures by an order if a bank fails or is likely to fail to attain, within a reasonable period of time, an appropriate level of capital consistent with the assessment of the Bank of Slovenia.

supervisor, to eliminate negative effects and potential breaches in any bank in a timely manner by introducing preventive measures taken on the basis of trends identified in a bank or the banking system. The Bank of Slovenia may impose specific supervisory measures if breaches of capital adequacy requirements or inappropriate liquidity positions are likely to give rise to a withdrawal of authorisation to perform banking services. The legal framework has also been put in place to allow the Bank of Slovenia to take additional measures to manage crisis situations in banks. A clear legal basis allowing the Bank of Slovenia to provide liquidity assistance to banks (the ELA) has been given in Measures of the Republic of Slovenia to Strengthen Bank Stability Act.

The issuing of authorisations for qualifying holdings of banks in financial sector entities established in the EU or in third countries has also been regulated by law. Within the additional measures aimed at increasing the share capital of a bank, the Bank of Slovenia may instruct a bank's management board to convene a general meeting within a set period of time and propose the adoption of a decision to increase the share capital of the bank. Moreover, the Bank of Slovenia may issue a decision disqualifying a member of a bank's supervisory board from performing the functions of a supervisory board member if violation of his or her duties has been found, if there is an obstacle to the appointment, or if the conditions for the appointment are not fulfilled.

The arrangements concerning the funding of bank rescue have been provided by the Measures of the Republic of Slovenia to Strengthen Bank Stability Act; these provide for liquidity loans in emergency cases and regulate the measures of recapitalisation. The Act Amending the Banking Act (ZBan-1J) and the Measures of the Republic of Slovenia to Strengthen Bank Stability Act were adopted with a view to providing the Bank of Slovenia a more comprehensive set of measures and powers to rescue and rehabilitate banks; in addition, we are preparing to set up a mechanism to raise bank share capital from private funds, i.e. banks' shareholders and certain categories of bank creditors, so as to reduce the need to utilise public funds.

In the preparation of the aforementioned Acts, the directives on capital requirements and supervision of conglomerates were taken into account, so they also refer to the areas of capital requirements and securitisation and expanded supervision measures, conglomerate supervision, etc. The amendments give the Bank of Slovenia substantially increased powers to impose measures; this partly follows the draft bank recovery and resolution directive.

On 19 September 2013, the Government adopted a proposal for the Macro-Prudential Supervision in the Financial System Act; its aim is to establish a legal framework to determine **the macro-prudential mandate of national authorities** and to assign the Bank of Slovenia the leading role in identifying and assessing systemic risks.

According to the Measures of the Republic of Slovenia to Strengthen Bank Stability Act, the institutional platform for carrying out the relevant measures is the Bank Assets Management Company (BAMC); its aim is to implement the measures to enhance bank stability in a way ensuring efficient use of public funds and repayment of budget funds, to expand loan portfolios to the non-financial sector, to ensure conditions for disposing of the state assets in banks, and to establish responsibility for the debt and investments that are considered impairments on balance sheets of banks to which the measures apply. Currently, the BAMC is setting up its organisational structure.

6. Reform of regulated services

Recommendation no. 6: *Accelerate the reform of regulated services, including a significant reduction of entry barriers. Improve the business environment, including through ensuring the independence of and providing sufficient and autonomous financing to the Competition Protection Agency.*

Currently, Slovenia is making strong efforts to **reform the regulation of professions and activities**. *The efforts are aimed at cutting the number of regulated professions and activities to bring it into line with the EU Member State average and at reducing administrative and other regulatory burdens. Particular attention is paid to easing the requirements and/or conditions for performing activities.* In 2010, when the reform started, there were 323 regulated professions in Slovenia; currently there are 287. In addition to reducing the number of regulated professions and activities (deregulation), the procedure to obtain permits was significantly simplified.

This year, the Craft Act was amended and a new decree establishing entry requirements for a list of small business activities was adopted. The number of entry regulations decreased from 64 to 25**.** In several segments, a significant reduction in formal requirements (education level) has been achieved. Now the opportunity to enter the market on the basis of acquired knowledge and experience under the national vocational qualifications programme is available for half of regulated small business activities.

New entry requirements for the tourism sector are currently undergoing government procedures. In addition to reduced requirements for tourist agencies, simplifications in relation to tourist guiding are also envisaged. Likewise, deregulation of formal entry requirements for sellers and shop managers has been submitted to government procedures. New regulation in the area of civil engineering is being prepared.

The independence of the **Competition Protection Agency** has been enhanced by its legal restructuring as a classic public agency and staff reinforcement. The Agency is no longer affiliated to the Ministry but continues to be funded from the budget as conventional indirect budget user.

7. **Reduction of the length of judicial proceedings**

Recommendation no. 7: *Build on previous efforts to further reduce the length of judicial proceedings at first instance in litigious civil and commercial cases and the number of pending cases, in particular enforcement cases.*

In order to enhance efficiency of the courts, **including shortening of judicial proceedings**, a relevant commitment has been signed for the purposes of improving the situation in the judiciary. In 2012, proceedings before a particular court took 13 to 20 months on average; the objective to be attained by June 2014 is aimed at resolving cases before courts in less than a year's time on average, and in some cases before particular courts in only three months. The objectives regarding acceleration of judicial proceedings have been set for each type of court and case specifically, and are objectively measurable. Based on the data for the first half of 2013, the majority of first-instance courts regarding all types of cases have already started reducing the time from receiving a case to fixing the first hearing; the average time has been reduced for most types of cases awaiting resolution.

In the first half of 2013, the Slovenian courts achieved the objective of **reducing the number of pending cases** by 6.7%,[11] and for matters of major importance by as much as 10.9%. The judicial statistics also show an encouraging trend with respect to the length of proceedings in litigious civil and commercial cases, including enforcement and infringement proceedings. The courts are being successful in managing the new caseload, since they are resolving more cases than they actually receive: they have resolved 5% more cases with respect to all cases before courts and 16% more cases of major importance with respect to the new caseload. The average expected time for case resolution concerning all judicial case types has reduced to 4 months,[12] while for the cases of major importance this was initially shortened by a month to reach 6.7 months in mid 2013.

An expeditious and more efficient judiciary will be ensured through relevant amendments to the judicial legislation adopted in July 2013 and aimed at enhancing the courts' efficiency and shortening the duration of cases. To this end, the Supreme Court of the Republic of Slovenia has envisaged adoption of criteria for quality work of courts, which are to include the processes of resolution of cases[13] and relevant instructions for an efficient implementation of judicial administration, and set the expected time of conduct of typical procedural acts and of resolving cases in specific types of courts and instances. The supervision of meeting the criteria for quality work of courts in their implementing matters of judicial administration will be carried out by the Unit for the Supervision of the Organisation and Operation of Courts. Presidents of courts have been given more responsibility and can be discharged in the event of failure to conduct matters of judicial administration in compliance with the rules and/or criteria relating to quality work of courts or in the event of their implementation but not in due time.

Changes in the regulation of the judicial service introduce the possibility of organising work in a manner which is not based on the classical processing of cases and which defines the possibility of different assessment of judges with respect to their working capacity.[14] By December, changes have been planned with respect to eventual modification of the existing court network, establishment of the district as a basic management unit, rationalisation regarding the organisation of courts, and reform of courses for judges and of the exam for judges.

With a view to increasing the courts' efficiency, several amendments are in the process of preparation in the area of **enforcement**. Key objectives include efforts aimed at increasing the efficiency of enforcement in commercial proceedings and changes in the scope of action of enforcement agents intended for speeding up relevant judicial proceedings.

In order to ensure more appropriate relationships between the complexity and volume of work, the conduct of particular proceedings, and the amount of the corresponding court fees, **court fees** rose in July 2013 or were redefined. In our estimation, general government revenue from court fees is expected to grow by approximately EUR 8 million annually, constituting an increase of 20%.

[11] The NRP 2013 target value forecast, with regard to the situation of the pending cases considered under the condition of currently equal new caseload, foresees a reduction by 3% in 2013 and further reduction by 3% in 2014.
[12] This includes matters which are expeditiously resolved due to their nature – for example land register proceedings and e-enforcement (approval phase; so-called proceedings at the level of the Central Department for Authentic Document (COVL)).
[13] For example the "Triage" project, which has shown good results in the commercial law departments of district courts.
[14] Consideration will be made of the ratio between the accomplished and the expected volume of work as a criterion for the assessment of the judge's working performance relating to fulfilling objectives of the expected volume of work either at the court level or at the organisational unit of the court level, as defined by the president of the court.

8. Management of state-owned companies and privatisation

Recommendation no. 8: *As part of the planned strategy of the Government to be completed by September 2013, classify core and non-core state assets according to economic criteria, with a view to divesting of non-core assets. Make the Slovenia Sovereign Holding (SSH) fully operational in a timely manner, and transfer both ownership and management of all stakes to the SSH, potentially excluding those that are on the list for immediate full privatisation. Ensure professional management of the SSH from the outset, potentially including international expertise, and a clearly defined arm's-length relationship with the companies involved. For core stakes, develop sector-specific strategies to improve profitability and corporate governance. Introduce an obligatory and publicly available register of management and supervisory board appointments in state-owned enterprises with requirements for disclosure of interests. Ensure that the regulatory framework facilitates divestment of non-core state assets and that administrative hurdles are minimised.*

The Government of the Republic of Slovenia has submitted for public debate a new proposal for the **Slovenian Sovereign Holding Act** (ZSDH-1). The proposal was also sent for opinion to the OECD and the European Commission. The Slovenian Sovereign Holding (SSH), which is to be created from the present Slovenian Compensation Company (SOD), will manage and conduct the process of privatisation. The main objective is aimed at establishing centralised management of all state-owned assets with a view to providing for more stable and transparent management and clear competencies and responsibilities of management and supervisory boards in companies where the Republic of Slovenia or SSH have a share, including reduction of corruption risks and conflicts of interest. The purpose of the Act is to ensure the independence of the SSH supervisory board members, including the independence of the management and supervisory board members of companies directly or indirectly owned by the state. The mentioned change also concerns the appointment of SSH supervisors. The supervisory board will be composed of five members to be appointed by the Government in the capacity of the SSH assembly pursuant to clearly defined criteria (individual and collective). Under the new proposed Act, assets owned by the Pension Fund Management (KAD), Management and Consultancy Company (DSU) and Special Company for Corporate Advisory, Inc. (PDP) will be transferred to the SSH by way of a merger procedure.

A more detailed management of companies and of particular groups of assets will be defined in the **Assets Management Strategy**. The proposed Act envisages the classification of assets into three categories, i.e. strategic, important, and portfolio; these are included in the Assets Management Strategy Framework, where the management of companies and particular groups of assets will be defined in more detail. The Strategy is to be adopted by the National Assembly of the Republic of Slovenia, whereby the SSH's establishment will no longer be dependent on the strategy's adoption, but instituted directly through the entry into force of the relevant Act.

Privatisation has been started gradually. The first package of companies intended for privatisation has been identified.[15] Sales of state-owned assets will be carried out in a transparent manner and respecting equal treatment for all tenderers. Operational privatisation procedures on behalf of the Republic of Slovenia are implemented by the Slovenian Restitution Fund (SOD). Preparations are underway for the majority of relevant procedures (for example selection of financial advisers and preparation of sales activities), and realisation of one part of the sales has been foreseen already this year.

[15] In June 2013, the National Assembly gave its consent to the Slovenian Restitution Fund (SOD), Pension Fund Management (KAD), Modra zavarovalnica, Management and Consultancy Company (DSU) and Special Company for Corporate Advisory, Inc. (PDP) for the disposal of shares in 15 companies: Adria Airways, Aero, Elan, Fotona, Helios, Aerodrom, Adria Airways Tehnika, NKBM, Telekom, Cinkarna Celje, Gospodarsko razstavišče, Paloma, Terme Olimia Bazeni, Unior and Žito.

9. Restructuring of companies and improving the business environment

Recommendation no. 9:

Identify and start to work on removing all existing legal and administrative impediments to sustainable restructuring of over-indebted/undercapitalised but viable companies through market-based solutions. In this context, take measures to ensure sufficient private burden sharing, to increase private investment, including foreign direct investment, and to achieve efficiency gains in troubled companies as part of the restructuring process. Adopt the necessary legal framework for out-of-court restructuring by September 2013, ensuring that it is coherent with the existing provisions on insolvency and provides incentives for both creditors and shareholders to reach out-of-court restructuring agreements. Improve the enforcement of corporate insolvency procedures and in-court settlements, including swiftly resolving pending court cases related to bankruptcy procedures, in order to maximise recovery value and to facilitate the timely and efficient resolution of non-performing loans.

In order to ensure restructuring of over-indebted companies, two effective fundamentals are required which will reinforce the role of creditors in the process of restructuring of companies:

- improvement of insolvency proceedings and
- introduction of out-of-court settlement.

In May 2013, in order to ensure more effective opportunities for **financial restructuring of over-indebted companies**, the Act Amending the Financial Operations, Insolvency Proceedings and Compulsory Dissolution Act was adopted; this introduced a simplified compulsory settlement proceedings. The first such proceedings were initiated in the beginning of September.

The Systemic Deleveraging Act and a new amendment to the Act Amending the Financial Operations, Insolvency Proceedings and Compulsory Dissolution Act are in the process of coordination with the interested public and have been sent for opinion and supplementing to the IMF and EBRD.

Systemic deleveraging of over-indebted companies and preserving their healthy parts will be facilitated via accelerated out-of-court conclusion of agreements on financial restructuring. The system is to provide for a change in the ownership structure of over-indebted companies, which is expected to create the conditions for their organisational and business restructuring. This is aimed at preventing the reoccurrence of illiquidity and/or insolvency. Deleveraging the Slovenian economy is essential for ensuring effective and real restructuring of insolvent companies and for preserving the healthy part of the economic sector and jobs.

The comprehensive system has two central goals:

- ensuring conditions for an effective financial restructuring of systemically important companies and
- rationalisation of the operation of the courts in the conduct of insolvency proceedings.

Rules regulating the newly introduced simplified compulsory settlement proceedings are to be simplified further by extending the use of this institution to debtors meeting the criteria of a small business. As regards debtors which meet the criteria of large or medium-sized companies of systemic importance, a proposal has been made for setting out simplified rules on judicial proceedings to facilitate faster and more efficient restructuring in view of financial and insurance-related obligations, since in practice the creditors are generally well-informed subjects (banks, savings banks, financial companies, etc.).

ENCLOSURES:
– Description of measures and their impact in terms of quality
– Assessment of the quantitative impact of key measures