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ENHANCING JUDICIAL EFFICIENCY TO FOSTER ECONOMIC ACTIVITY IN PORTUGAL

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ABSTRACT/RÉSUMÉ

Enhancing judicial efficiency to foster economic activity in Portugal

A well-functioning justice system is indispensable to business activity and to a society as a whole. Judicial efficiency measured by trial length, one of the essential factors in the effectiveness of the justice system, ensures contract enforcement, which is the basis of market transactions. Judicial efficiency is closely associated with accessibility to judicial services and the certainty of judicial decisions, raising people's confidence. Portugal has undertaken numerous judicial reforms in the past, to the extent that it is difficult to disentangle and evaluate fully the effects of each reform. Overall, judicial efficiency remains weak, as reflected in the average trial length and bottlenecks in a number of courts. The data collection system, significantly developed as part of the reforms, can be more fully utilised for allocating court resources. The autonomy of the judicial council and court presidents can also be strengthened so that they can effectively manage resources. Individual judges can be better incentivised through performance-oriented evaluation. Competition in the legal profession sector can be enhanced while increasing the transparency of legal services. Also, alternative dispute resolution mechanisms can be developed further, meeting different needs for judicial services, in particular those on insolvency, while alleviating court congestion. Finally, building on past and ongoing reform efforts, the judicial system should continue to improve the capacity to undertake forensic investigations of economic and financial crimes.

This Working Paper relates to the *2018 OECD Economic Survey of Portugal*
(http://www.oecd.org/economy/portugal-economic-snapshot/)
JEL classification: D02, K23, K40, K42
Keywords: Judicial efficiency, trial length, allocation of court resources, governance in the court system, workload assessment, regulation in the legal service sector, alternative dispute resolution mechanisms

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Améliorer l'efficience du système judiciaire pour stimuler l'activité économique au Portugal

Le bon fonctionnement du système judiciaire est indispensable à l'activité des entreprises et à la société dans son ensemble. Mesurée par la durée des procès, qui constitue un des déterminants essentiels de l'efficacité de la justice, l'efficience du système judiciaire garantit l'exécution des contrats, qui est le fondement des transactions marchandes. L'efficience du système judiciaire est étroitement liée à l'accessibilité des services judiciaires et à la sécurité juridique des décisions de justice, qui renforcent la confiance des individus. Le Portugal a engagé de nombreuses réformes judiciaires par le passé, au point qu'il est difficile de distinguer et d'évaluer véritablement les effets de chaque réforme. Globalement, l'efficience du système judiciaire demeure faible, ainsi que l'illustrent la durée moyenne des procès et l'engorgement d'un certain nombre de tribunaux. Le système de collecte de données, qui a été sensiblement étoffé dans le cadre des réformes, peut être davantage exploité pour répartir les ressources au sein du système judiciaire. Il est par ailleurs possible de renforcer l'autonomie du Conseil supérieur de la magistrature et des présidents de tribunaux, de manière à leur permettre de gérer efficacement leurs ressources. On peut améliorer les mécanismes d'incitation individuelle auxquels sont soumis les juges en veillant à ce qu'ils fassent l'objet d'une évaluation axée sur leurs résultats. Les autorités peuvent par ailleurs renforcer la concurrence dans le secteur des professions juridiques tout en améliorant la transparence des services juridiques. En outre, il est possible d'étoffer encore les modes alternatifs de règlement des différends, de manière à satisfaire les différents besoins de services juridiques, notamment en matière d'insolvabilité, tout en atténuant l'engorgement des tribunaux. Enfin, en s'appuyant sur les réformes antérieures et actuelles, le système judiciaire devrait continuer d'améliorer sa capacité de réaliser des enquêtes techniques sur les infractions économiques et financières.

Ce document de travail est lié à l'*Étude économique de l'OCDE* de 2018 consacrée au Portugal
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Classification JEL : D02, K23, K40, K42
Mots-clés : efficience du système judiciaire, longueur des procès, répartition des ressources au sein du système judiciaire, gouvernance du système judiciaire, évaluation de la charge de travail, réglementation du secteur des services juridiques, modes alternatifs de règlement des différends

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Enhancing judicial efficiency to foster economic activity

By Yosuke Jin and Sofia Amaral-Garcia[1]

Economic development in the long run is shaped by institutions and the associated regulatory framework. Favourable regulatory settings are only effective if they are complemented by legal institutions that ensure their implementation. Portugal has made significant progress in regulatory reforms over the past decade. The beneficial effects of these reforms can be boosted further by addressing efficiency in the judicial system. A more efficient judiciary ensures contracts are enforced effectively and in a timely manner, thereby improving business dynamics and productivity and boosting investment.

The judicial system is very complex and its effectiveness comprises many facets, including efficiency, fairness, and the quality of decisions. Judicial efficiency is a key factor to ensure the proper functioning of markets. Trial length is the indicator of judicial efficiency that tends to be most closely related to economic activity (Palumbo et al., 2013). From the perspective of businesses, the certainty of judicial decisions and the accessibility of judicial services are also essential. Trial length is closely associated with these other two aspects of the judiciary, because lengthy trials constrain access to judicial services (due to the capacity constraints of the courts) and compromise the certainty of judicial decisions (as in the legal maxim: "justice delayed is justice denied"). Furthermore, judicial efficiency is positively related to individuals' confidence in the justice system (Palumbo et al., 2013).

The average time to resolve a case in courts is long in Portugal (Figure 1), indicating inefficiency in the court system. Trial length is affected by factors within the court settings such as resources and governance in courts (Figure 2), which are essential factors explaining the performance of most efficient court systems across OECD countries (Palumbo et al., 2013). Improving these aspects can reduce trial length without reducing the quality of judicial decisions. Trial length is also explained by the behaviour and incentives of different actors in a broader legal system (Figure 2). While ensuring fair access to the judiciary for all, ill-founded litigation that unnecessarily boosts court congestion needs to be reduced.

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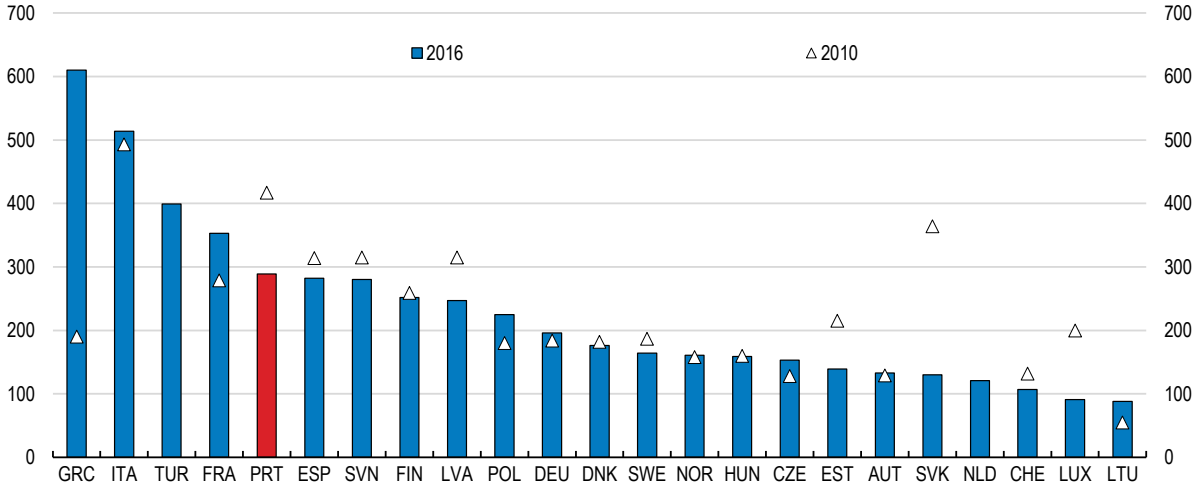
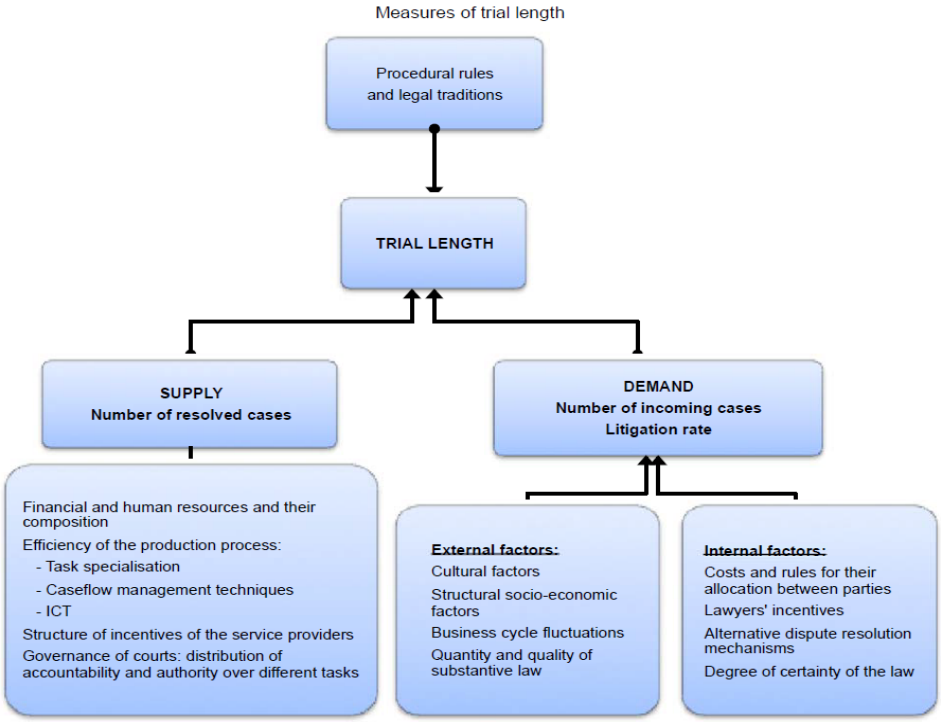
Figure 1. Court proceedings are shorter than before, but still long

Average time needed to resolve civil and commercial cases, first instance courts, in days



Source: European Commission for the Efficiency of Justice (CEPEJ).

Figure 2. Judicial efficiency as measured by trial length



Source: Palumbo et al. (2013), "The Economics of Civil Justice: New Cross-country Data and Empirics", OECD Economics Department Working Papers, No. 1060.

The main findings of this paper are:

- Judicial efficiency needs to be improved, which is indicated by the average trial length and significant bottlenecks in some courts, in order to ensure timely contract enforcement for businesses, facilitating firm expansion as well as insolvency proceedings;
- Significant reforms have been undertaken over the past years, which substantially reformed the framework of the judicial system (Box 1). Nonetheless, operational problems remain. Judicial resources, such as judges and budgets, can be better allocated across court districts through developing workload assessment and strengthening the governance structure;
- Court congestion remains significant, due mainly to debt enforcement proceedings, which can be alleviated by developing further alternative dispute resolution mechanisms, in particular those aiming at debt enforcement; and
- The Public Prosecution Office and the Criminal Investigation Police should be endowed with adequate resources and continue to provide specialised training for public prosecutors on economic and financial crime, including corruption.

Box 1. Recent reforms in the Portuguese court system

In recent decades, several reforms were implemented in the Portuguese judicial system. More recently, the Memorandum of Understanding on Financial Assistance signed in May 2011 with the IMF and the European Union demanded the implementation of judicial reforms, setting as priority the efficiency of the judicial process. A series of reforms followed:

The Backlog Reduction Program

A special task force from the judiciary and the executive reviewed all pending enforcement cases. Then, a Decree Law was enabled to close more than 500 000 enforcement cases in 2013 (45% of all pending enforcement cases as of May 2011), which had been inactive for long periods.

The new Code of Civil Procedure

The new Code of Civil Procedure (Law 41/2013, June 26) aimed to simplify some excessive procedural rules in court proceedings.

- The new Code of Civil Procedure allows judges to set time frames for their decisions and gives them the right to dismiss parties' submissions aiming solely at delaying the court process.
- It increased certainty in court proceedings by, for example, limiting enforceable titles (e.g. private documents such as promissory note are no longer enforceable).
- It reduced administrative burdens, as no separate enforcement action is necessary to enforce an enforceable court decision.
- It allows an enforcement proceeding to terminate after three months, if no assets are found in the procedure.

The Law for the Judicial System Organisation

The Law for the Judicial System Organisation (Law 62/2013, August 26) reorganised the courts in Portugal and reformed the management model in the court system.

- The reorganisation of courts resulted in a reduction in the number of courts to 23 district/comarca courts, from 323 first instance courts in total (142 specialised or specific competence/jurisdiction and 181 generic competence).
- The management responsibility of the High Council for the Judiciary at the central level was strengthened. The High Council for the Judiciary sets overall strategic objectives every three years, including performance targets, which are translated into annual performance targets.
- The reform introduced a new management structure in each of the new 23 district/comarca courts and these courts acquired autonomy in the management of their own courts, developing the annual work plans, the attendant budgets, and personnel requirements.
- The reform introduced performance targets for each court, set by each district/comarca court and the High Council for the Judiciary, with quarterly assessments on performance.

Other reforms to speed up enforcement proceedings

- In 2012 the Special Proceeding for Revitalisation (PER) was introduced and reformed in 2017. The Out-of-court regime for firm restructuring (RERE) was also introduced in 2018, as well as the Company Recovery Mediator.
- "PEPEX" which is an expedited procedure allowing creditors to verify whether debtors have assets and to decide whether or not to pursue enforcement came into effects in 2015, applying to small value claim cases (up to EUR 10 000);
- "Automated" procedures for seizing amounts in bank accounts, in which the enforcement agent has access to a database in Banco de Portugal;
- Electronic platforms for auctioning of seized assets were also introduced.

Judicial efficiency is crucial for business activity

Judicial efficiency is a critical framework condition for doing business and attracting FDI (Box 2). As discussed further below, the Portuguese judicial system is inefficient, with firms reporting perceived inefficiency in the judicial system as one of the most severe constraints to their operations (INE, 2018).

Box 2. Impact of judicial efficiency on economic performance

The legal environment affecting financing and firm growth:

Secure property rights are associated with better financial and economic outcomes, such as a greater use of external finance (La Porta et al., 1997). The reliability of the legal system for dispute resolution is found to increase firms' use of external financing to fund growth, using firm-level data from 30 countries (Demirgüç-Kunt and Maksimovic, 2002). The trust in judicial efficiency is found to be particularly important to finance investment in intangible assets, which in turn increases the size of firms investing in these assets, using firm-level data from 15 European countries (Kumar, Rajan and Zingales, 1999).

Creditor rights affecting bank lending:

Creditor rights are found to affect the terms of bank loans, such as bank lending spreads (Laeven and Majnoni, 2005; Qjan and Strahan, 2007) as well as loan maturities (Qjan and Strahan, 2007), using an extensive firm-level dataset. Besides the legislation on creditor rights, the enforceability of contracts on the ground also matters. The enforceability of contracts is found to increase the amount of bank lending and loan maturities and to reduce bank lending spreads, using a larger sample of loans than the above mentioned studies (Bae and Goyal, 2009).

Insolvency regime and bank lending:

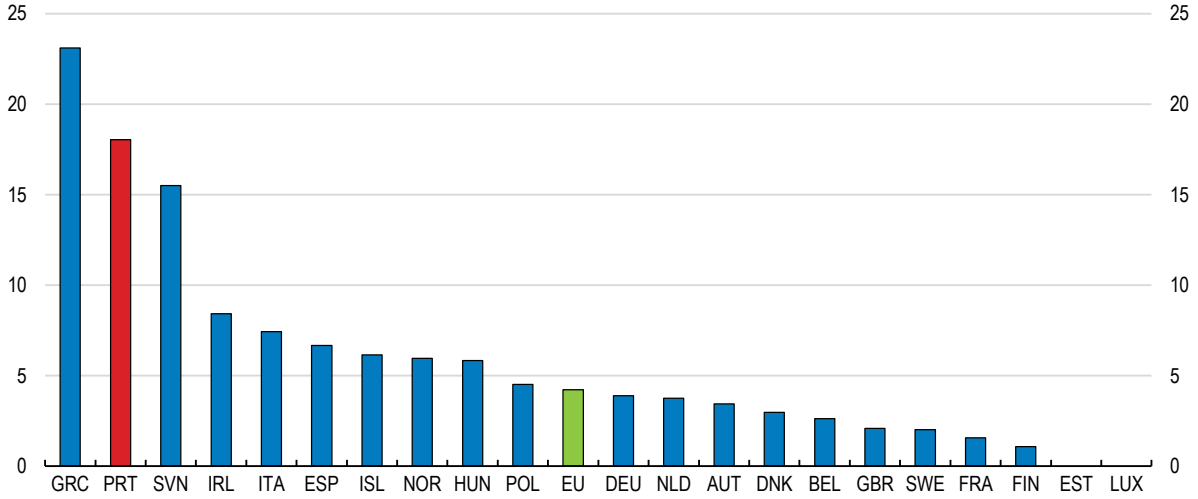
The insolvency regime affects bank lending and its conditions. The effectiveness of insolvency regimes, facilitating debt resolution, is found to be positively related to the size of debt markets (the credit-to-GDP ratio), using data from 88 countries and the World Bank Doing Business indicator on insolvency (Djankov et al., 2008). The inefficiency in debt resolution impedes the reallocation of resources from unproductive to productive firms. Such delays in debt resolution, associated with difficulties in recovering collateral quickly, are found to negatively affect bank lending, based on an analysis of SME loans in European countries (Bergthaler et al. 2015; Aiyar et al. 2015).

Judicial efficiency ensures contract enforcement

Judicial efficiency facilitates financial transactions by ensuring creditors' rights, promoting investments and innovation. In the case of default, the enforcement of collateral would limit subsequent losses. Collateral enforcement most often requires court proceedings, which are quite long, complex and surrounded by uncertainty in Portugal. The collateral value can decline markedly during the proceedings. This is reflected in a very low recovery rate; just 12% on average (Ministry of Justice, 2018). Thus instead of pursuing court proceedings, forbearance has been granted in some instances (Figure 3), which has the potential to crowd-out new lending to healthier firms (Anderson, Riley and Young, 2017).

Figure 3. Forbearance loans are frequently extended in Portugal

The forbearance loans ratio as a percentage of total outstanding loans in the corporate sector, Q2 2018



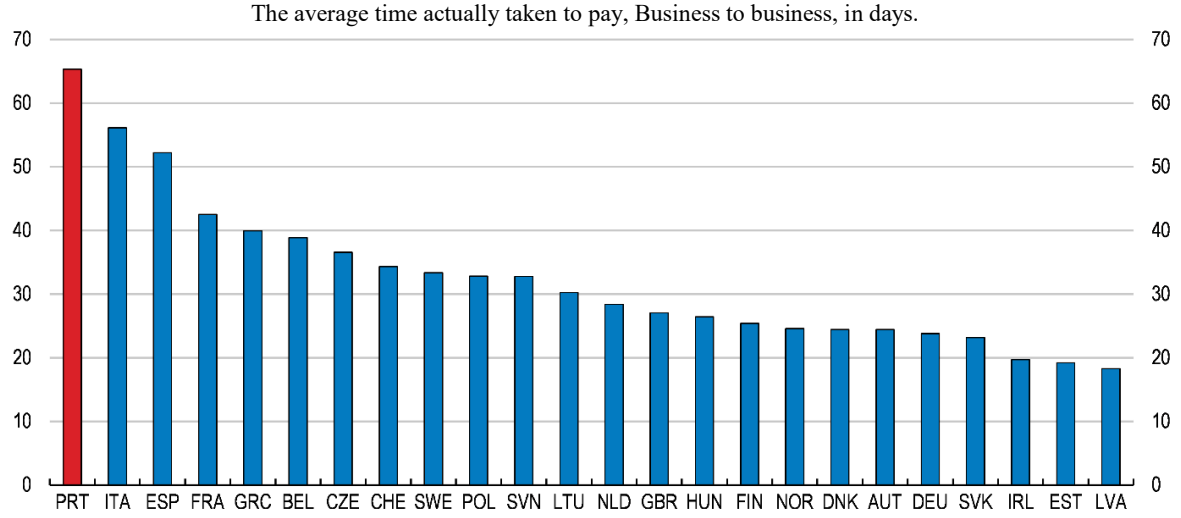
Source: EBA, "Risk Assessment Report", December 2018.

Judicial efficiency facilitates market transactions by ensuring timely contract enforcement, thus promoting competition in the business sector. Payment risk in Portugal is high, as late payments are very frequent (Figure 4), affecting Portuguese firms most often through liquidity constraints. These problems are also perceived to be hampering firm expansion and even to be a threat for firm survival in some cases (Intrum, 2018). Breaches of contract can be remedied by court order, but court proceedings can be long and complex in Portugal, encouraging negligent behaviour of some debtors.

Apart from economic and geographic conditions, institutional factors affect the inflow of FDI. Among different institutions, the judicial system is found to be significantly important for FDI inflows (Bénassy-Quéré, Coupet and Mayer, 2007; Júlio, Pinheiro-Alves and Tavares, 2013), with contract enforcement among these factors (Júlio, Pinheiro-Alves and Tavares, 2013). The quality of FDI inflows can also be affected by these factors. Despite Portugal's economic openness, the stock of FDI remains below that of other comparable small European economies (Westmore and Adamczyk, 2019).

Figure 4. The average time to pay is long in Portugal

The average time actually taken to pay, Business to business, in days.



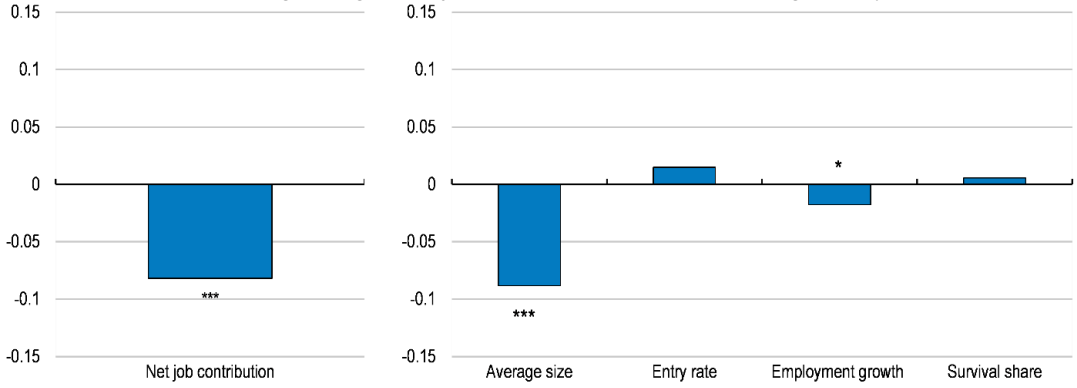
Source: Intrum (2018), "European Payment Reports 2018".

Judicial efficiency affects business dynamics

Judicial inefficiency, measured by trial length, is negatively associated with firm expansion, in particular, for start-ups. For instance, Calvino, Criscuolo and Menon (2016) show that a trial length that is 100 days longer than the average reduces net job creation by 8% (Figure 5). The size of firm at entry is negatively affected by judicial inefficiency because potential costs in the case of dispute rise with firm size. Furthermore, post-entry growth in employment is negatively affected by judicial inefficiency which impedes the reallocation of resources to highly-productive firms. Portuguese start-ups tend to remain small in size in both the manufacturing and services sectors, compared with other OECD countries (Criscuolo, Gal and Menon, 2014), due to problems in the reallocation of resources.

Figure 5. Net job creation of start-ups is reduced by judicial inefficiency

Percentage change in net job creation associated with trial length in days



Note: The DynEmp project aims at creating a harmonised cross-country micro-aggregated database on employment dynamics from confidential micro-data, where the primary sources of firm and establishment-level data are national business registers.

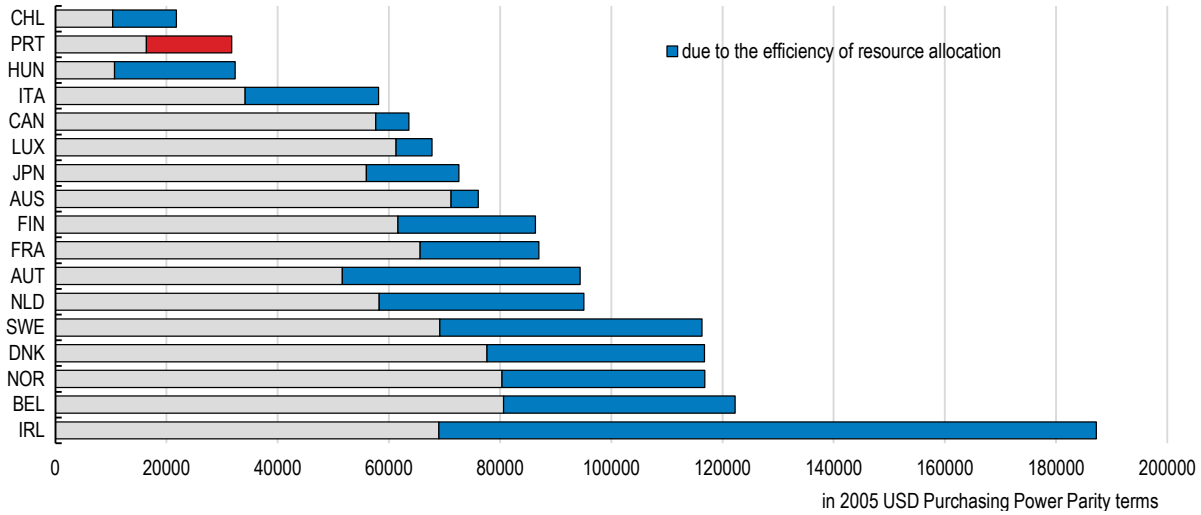
***, **, *: the results are statistically significant at the 1%, 5% and 10% level, respectively.

Source: Calvino et al. (2016), "No Country for Young Firms?" OECD Science, Technology and Industry Policy Papers No.29.

Judicial inefficiency can weaken market selection mechanisms. It is reflected in the limited expansion of highly-productive firms. The prevalence of non-viable firms, potentially associated with judicial inefficiency, weakens the efficiency of resource allocation, as they trap resources and stifle the ability of highly-productive businesses to expand (Figure 6). Such non-viable firms have reduced the investment and employment growth of healthy firms in many OECD countries over the past decade (Adalet McGowan, Andrews and Millot, 2017), and in Portugal (Gouveia and Osterhold, 2018).

Figure 6. The allocation of resources is inefficient in Portugal

Labour productivity of firms in the manufacturing sector



How to read this chart: aggregate productivity is decomposed into the contribution of two terms, an unweighted productivity term representing average firm level productivity, and a covariance term that links productivity to firm size. The latter term is a measure of allocative efficiency, since it increases if more productive firms capture a larger share of resources in the sector, the contribution of which to aggregate productivity is shown as "due to the efficiency of resource allocation" in the chart.
Note: The MultiProd project in the OECD uses existing official firm-level data (official surveys and administrative sources) in a harmonised framework to provide micro-aggregated statistics and analysis that are comparable across countries (see Berlingieri et al., 2017 for more details).
Source: Berlingieri, G. et al. (2017), "The MultiProd Project: a Comprehensive Overview", OECD Science, Technology and Industry Working Papers 2017/04.

Court settings are key for judicial efficiency

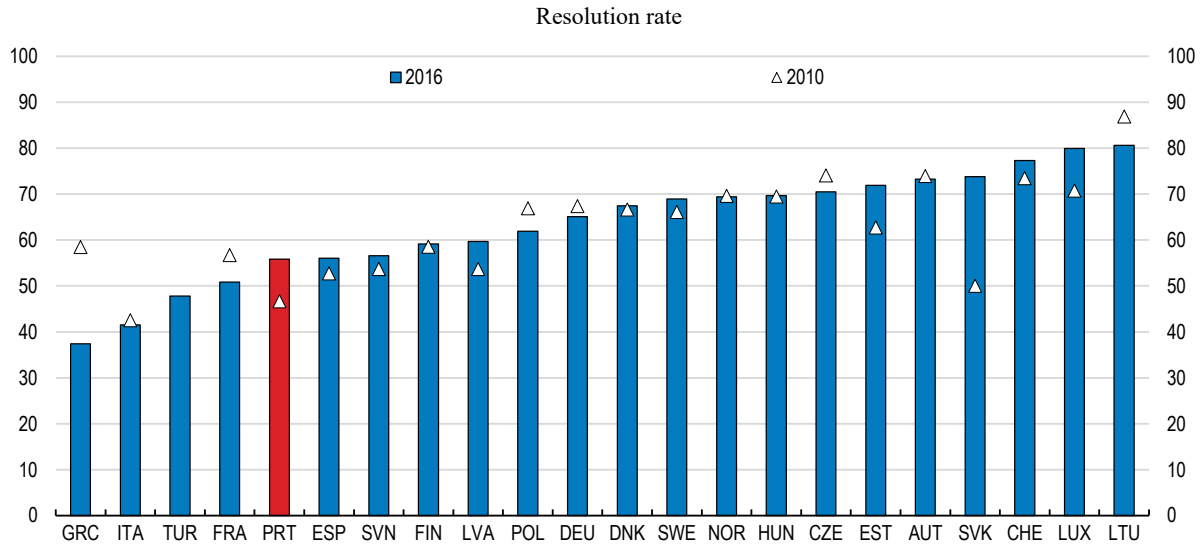
Courts play a crucial role in proceedings and adjudicating cases, which operate within particular institutional settings (Box 3). The efficiency of Portuguese courts is weak, with lengthy court proceedings (Figure 1), associated with slow case resolution (Figure 7). The most common possible explanations for slow case resolution are the structure of trial procedures and procedural formalism (e.g., Djankov et al., 2003), inefficiency in the allocation of court resources (e.g. Palumbo et al., 2013), and weak incentives for judges (e.g., Miceli and Coşgel, 1994).

Box 3. The Portuguese court system

Portugal is a civil law tradition country, in common with two-thirds of the legal systems worldwide. The Portuguese court system is mainly divided into two jurisdictions, as established in the Constitution of the Portuguese Republic: administrative and civil. This separation of jurisdictions is a typical feature of this legal tradition (Merryman and Perez-Perdomo, 2007), where a strong distinction between private law and public law is made.

- Judicial courts with civil and criminal jurisdiction are organised in three levels: first instance courts (*tribunais de comarca* / district courts), courts of appeal (*tribunais da relação*) and the Supreme Court. There are currently 23 district courts and specialised courts such as the commercial courts, enforcement (execution) courts or family and minors courts. There are also enlarged jurisdiction courts (with national jurisdiction) such as the Maritime Court; Intellectual Property Court; Competition, Regulation and Supervision Court; Criminal Prosecution Central Court.
- Tax and administrative courts are also organised in three levels: first instance administrative and tax courts (*tribunais administrativos de circulo e tribunais tributários* / circuit administrative courts and the tax courts), central administrative courts (*tribunais centrais administrativos*) and the Administrative Supreme Court.

Figure 7. Resolution in courts is slow in Portugal



Note: "Resolution rate" is defined as the number of resolved cases divided by the cases in stock (the latter is defined by the sum of the number of pending cases at the end of the previous year and the number of incoming cases).
Source: European Commission for the Efficiency of Justice (CEPEJ).

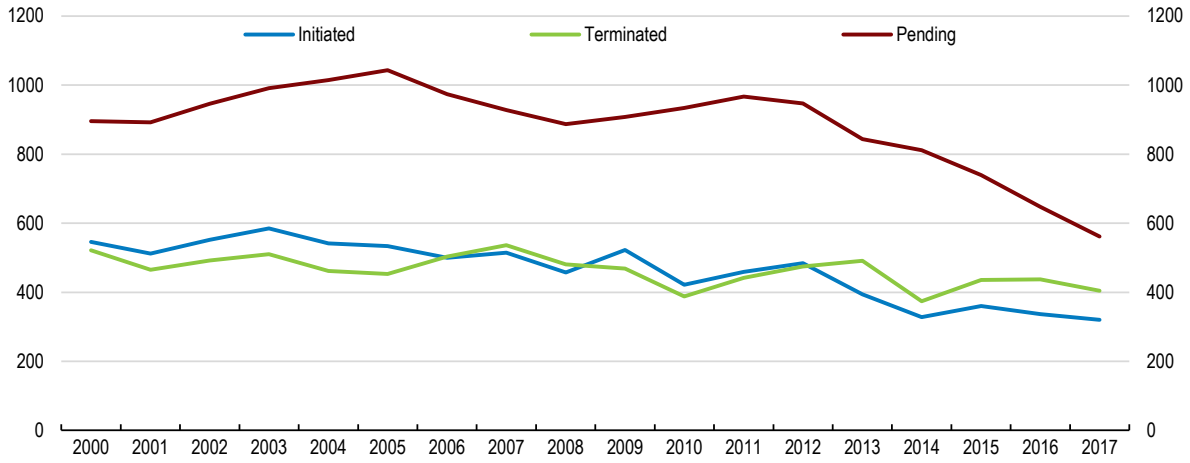
Trial length remains long with significant disparities

Court congestion has significantly declined over the past decade, but the number of pending cases remain high (Figure 8). The backlog in the civil justice system has declined by 45% since 2007, likely reflecting a series of reforms undertaken over the past years. The number

of terminated proceedings has consistently surpassed that of initiated proceedings over the past five years, eroding the backlog of pending cases in the system (Figure 8). It is difficult to fully assess recent reforms due to the lack of additional data. For instance, it is not possible to control for case complexity completely, while more complex cases can take longer to be decided. There is no information regarding the quality of judicial decisions, although decisions with higher quality might require more time (Bielen et al., 2018).

Figure 8. Court congestion has been alleviated, but remains significant

Number of initiated, terminated and pending proceedings per judge

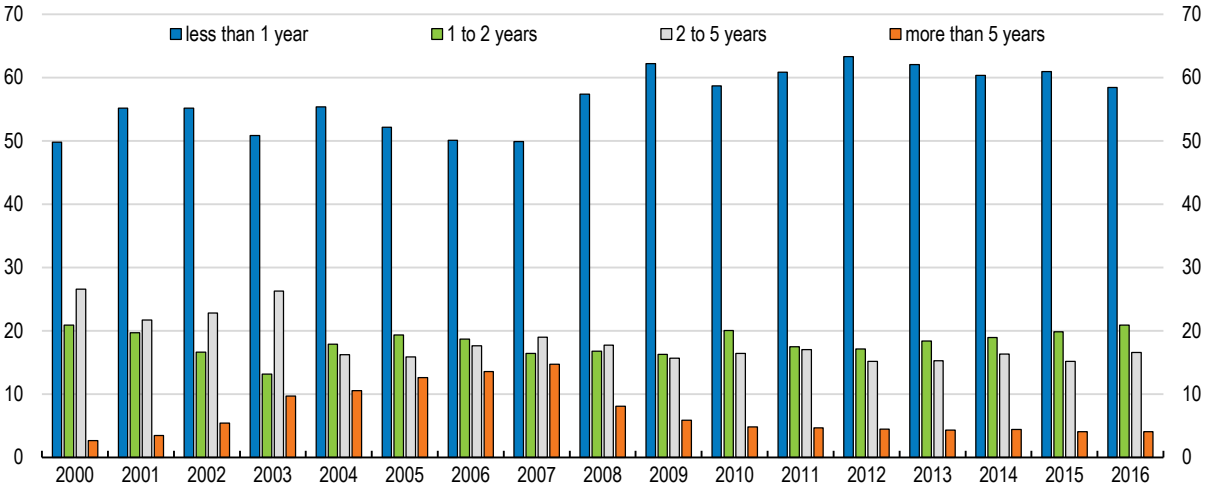


Source: Pordata.

Overall, the incidence of very long proceedings has declined over time, but some cases still require a significant amount of time (Figure 9). At least half of cases have always been disposed in less than 1 year. The proportion of disposed cases that take more than 5 years has also decreased. Nonetheless, the proportion of cases taking more than 1 year remains high, accounting for more than 35% of all cases.

Figure 9. Some cases still require a significant amount of time

Share of resolved cases according to duration, civil cases, first instance courts



Source: Pordata.

In what follows, the focus will be on civil cases, since they are essential for businesses, including contract enforcement and insolvency proceedings. It is also in this type of cases that delays are the most significant: in 2016, the average duration in first instance courts was 33 months for civil cases, 8 for criminal cases and 11 for labour cases. In 2017, civil cases accounted for 64% of initiated proceedings and 69% of terminated proceedings. These are also congested cases, as 89% of pending proceedings correspond to civil cases. If we consider the type of civil cases, those related to commercial and civil debts account for 60% of initiated proceedings and 86% of pending proceedings.

Indeed, long delays in enforcement are one of the characteristics in Portugal. The post-court enforcement process in Portugal often requires the intervention of the court even after a court decision is made, which is not common across other EU countries. Such requirements add further delays in the whole process to resolve a case. Although the series of recent reforms likely increased the chance of resolving a debt enforcement case in the early months, debt enforcement typically takes a long time despite a reduction from around 60 months in 2010 to 30 months in 2015 for the median case (Pereira and Wemans, 2018).

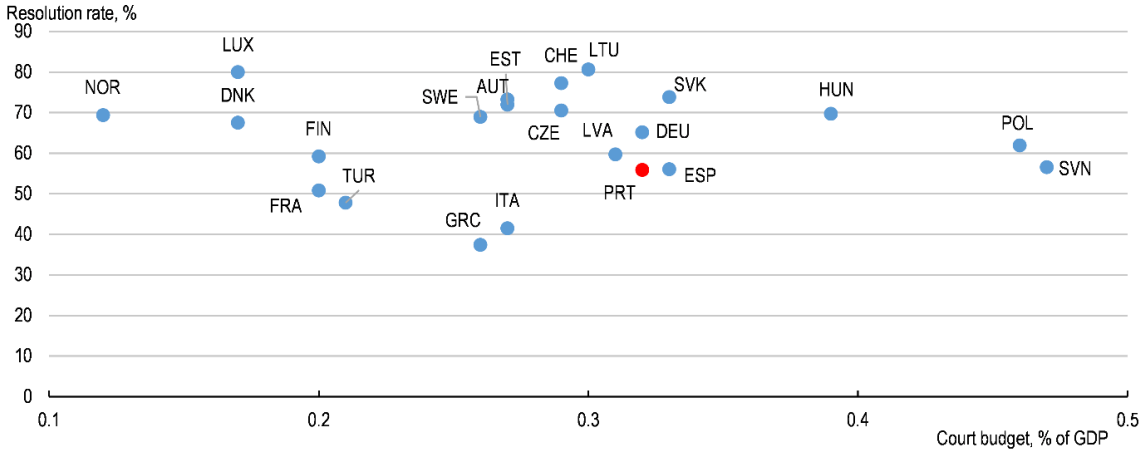
Judicial resources are not allocated efficiently

Judicial resources and allocation

Overall court performance can be affected by the total amount of resources, but the efficient allocation of judicial resources is even more important (Palumbo et al., 2013). In fact, countries with similar budget allocated to courts as a percentage of GDP have very different average trial lengths (Figure 10). Previous studies do not support a statistically significant relationship between the budget allocated to courts and court performance (e.g. Cross and Donelson, 2010; Voigt and El-Bialy, 2016).

Figure 10. Total court budget does not explain court performance

Budget allocated to courts as a percentage of GDP and the resolution rate, 2016



Note: GBR includes England and Wales only.
Source: European Commission for the Efficiency of Justice (CEPEJ).

The composition of spending items can affect court performance. The budget allocated to the judiciary is divided into different items such as salaries, ICT, training for judges and real estate. All other things being equal, countries devoting a larger share of the budget to ICT have shorter trial length (Palumbo et al., 2013). In Portugal, the share of salaries was

the largest across OECD countries for which data were available in the early 2010s. Since then, Portugal has increased the budget for digitalisation, while consolidating, strengthening and expanding computer applications, notably, the information system on court proceedings (as part of the *Justiça Mais Próxima* reforms). Portugal is now among the top countries in Europe in terms of digitalisation and ICT in the justice sector (CEPEJ, 2016).

An increase in the number of judges is unlikely to improve overall court performance in itself. The total number of judges per inhabitant in all courts has increased by 13.5% between 2004 and 2017 (Table 1). Several studies investigated the relationship between the total number of judges and court performance, but overall, court performance does not statistically significantly depend on the number of judges, in particular, when the causal relationship is properly controlled (e.g. Dimitrova-Grajzl et al., 2012).

Table 1. The number of judges has increased strongly

	Total Judges per 100,000 inhabitants and type of court:			
Year	All Courts	First Instance Courts	Tribunais da Relacao	Supreme Court
2004	16.8	11.4	2.9	0.6
2005	17.2	11.7	3.1	0.6
2006	17.5	11.9	3.2	0.6
2007	17.6	12.0	3.4	0.6
2008	18.2	12.1	3.6	0.6
2009	18.6	12.4	3.8	0.6
2010	18.6	12.6	3.7	0.5
2011	18.4	12.5	3.6	0.6
2012	19.3	12.7	3.9	0.6
2013	19.5	13.1	3.8	0.6
2014	19.3	12.9	3.7	0.6
2015	19.4	13.1	3.6	0.6
2016	19.4	12.8	3.7	0.6
2017	19.6	12.7	3.9	0.6

Note: "All courts" includes judges from judicial courts, from administrative and tax courts, and the Constitutional Court.
Source: Ministry of Justice.

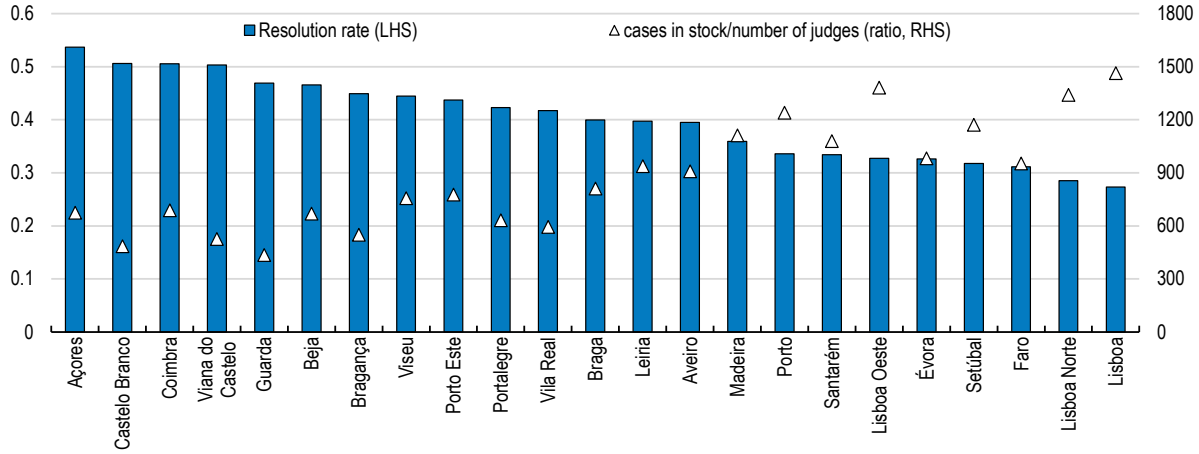
The allocation of judges across courts is a key factor to explain court performance (Palumbo et al., 2013). There remain significant bottlenecks in some first instance courts, in spite of the increase in the total number of judges, and these bottlenecks are clearly associated with a low resolution rate (Figure 11). The reallocation of judges from relatively vacant courts to congested courts would be beneficial to resolve such bottlenecks. Using district court level data in Portugal, it was found that the workload was very different across court districts and cases are resolved progressively slowly as the number of incoming cases grows, all else equal (Pereira and Wemans, 2017), supporting such a reallocation of judges. The inability to do such reallocation can result from problems in workload assessment and a lack of effective management of resources.

Currently, it is difficult to fully assess the effectiveness of the court system, including the effects of recent reforms. There is a discontinuity in data at court district level due to the introduction of a new judiciary matrix (*mapa judiciário*), which modified the boundary of court districts (Box 1). In general, data on some key aspects are not sufficient to evaluate the court system, such as information on quality, complexity of cases, and costs of litigation. Such disaggregated data would enable researchers to assess properly the

efficiency of judges and courts (as measured by trial length), the effects of the past reforms, as well as the characteristics of complex cases associated with longer case duration. Overall, the recent reforms have improved the effectiveness of the court system (further detailed in OECD, 2019a), but significant bottlenecks in some court districts imply scope for further improvements (Figure 11).

Figure 11. Significant bottlenecks remain in some court districts

Civil cases, 2017



Source: Ministry of Justice and High Council for the Judiciary.

Courts' infrastructure for workload assessment

Case-flow management indicates the set of actions that a court can take to monitor the progress of cases and to make sure that they are managed efficiently, ensuring a smoother functioning of courts and improving the performance of courts. Among the different case-flow management techniques evaluated by Palumbo et al. (2013), the early identification of long or otherwise potentially problematic cases appears to be associated with shorter trial length.

An information system, CITIUS, was introduced in 2007 in the civil justice system. CITIUS aimed at treating electronically all information belonging to a proceeding, giving judges the possibility of making sentences, court orders and other judicial decisions in the application; signing sentences and court orders; receiving and sending proceedings electronically to the registry; and identifying which procedures were assigned to judges and corresponding stages (Contini and Lanzara, 2013). The use of CITIUS became mandatory in judicial courts and intensive training was provided to judges. The system brought significant changes, not only positive but also negative ones. There are non-negligible technical aspects that make it challenging to use, such as the need for a server and capacity to store millions of documents.

The CITIUS system was not necessarily well adapted to meet judges' needs, at least partly because judges were not involved in the process of designing the system. In 2009, a survey on the functioning of the CITIUS system was completed by 13.3% of judges using it (Associacao Sindical dos Juízes Portugueses, 2009). 79% of respondents noted that CITIUS brought an increase in time spent with daily tasks (of up to 114%), mostly due to an inadequate word processor, difficulties in accessing and consulting the proceedings and problems connecting to the system. A significant proportion of judges reported issues

related to trust in the system and other problems including: inadequate information equipment; the inability to consult the proceedings during trial; the inability to access away from the office, an increase in the number of steps to perform a given act; and the lack of immediate technical assistance, and the inability to fulfil some mandatory procedural norms. Several problems reported in 2009 have been addressed since then and there are on-going efforts to address other limitations of the CITIUS system as part of the *Justiça Mais Próxima* reforms, which should be extended.

When functioning properly, an information system can be a powerful tool in assessing judges' caseloads. A significant challenge for judges is to identify which cases should be prioritised, and a well-designed IT tool could aid them in undertaking such prioritisation. Even though CITIUS was meant to produce such a tool, it was unable to identify blockages in the court system (Contini and Lanzara, 2013). In the early years of its implementation, the system had no early warning devices for, for example, the detection of cases that had been in the system for several years (CEPEJ, 2016). Since then, the system has evolved and now includes such features, which should be fully utilised by the courts to identify problematic cases and those that should be prioritised. The system can be improved further for this purpose, if necessary. This should allow necessary measures to be taken to avoid an additional increase in congestion, such as replacement and reallocation of judges.

The distribution of cases among judges has been a concern in the Portuguese judicial system, and several studies have tried to assess bottlenecks and ways to improve the system so that delays can be reduced (Hay Group, 2002; Observatório Permanente da Justica Portuguesa, 2005). The High Council for the Judiciary, in its functions as the managing body of judicial courts, is in charge of distributing cases among judges. The question is how cases should be distributed considering that they might entail different levels of complexity. The allocation of cases depends little on the complexity of judges' existing caseload. There are lists of criteria proposed by judges and approved by the High Council for the Judiciary that set a separate allocation for complex cases, although it is not clear what these criteria are and how they effectively translate into the distribution of caseloads.

Management of courts remains weak

Governance structure

The governance structure is a critical element for court performance, making decisions for a better functioning of the judicial system. Under many jurisdictions, judicial councils serve for the administration of courts and the entire judicial system. Such autonomy from the executive (the Ministry of Justice) can affect judicial efficiency. Allowing judges to administer at least a part of their own affairs can improve judicial efficiency taking advantage of their own knowledge in management, but judges are not necessarily experts in administrative affairs (Voigt and El-Bialy, 2016). According to Palumbo et al. (2013), rather than the presence of judicial councils, governance models within judicial councils matter to explain court performance.

In Portugal there is no single body in charge of strategic governance (CEPEJ, 2016). Different roles are assigned to the executive (the Ministry of Justice) and the judiciary (the High Council for the Judiciary at the central level). The Ministry of Justice retains the vast majority of power, but some shift of power to the judiciary took place recently. Namely, the High Council for the Judiciary is now in charge of paying wages to first instance court judges. This change in financial and administrative autonomy from the Ministry of Justice took a long time: it had been established by law in 2007 (Articles 1 and 3 of Law 36/2007

of 14 August), but it was not implemented until 2016. Importantly, judges' wages are regulated, and the High Council for the Judiciary does not have any power to change this.

Within the judiciary, the High Council for the Judiciary sets mandatory goals. These goals include a reduction in the number of pending cases, a maximum delay for scheduling of hearings (3 to 4 months) and the prioritisation of older pending cases. The High Council for the Judiciary monitors courts and judges. At the judge level, it identifies the total proportion of proceedings terminated and initiated, delays and scheduling of hearings according to the length of delays/scheduling. This information is sent every 4 months by each individual court.

A new management structure in individual courts was implemented by a recent reform (Box 1). The reform established a tripartite management structure in each court composed of the Court President (with functions of representation, direction, procedural, administrative and functional management), the Magistrate of the Public Ministry Coordinator (who directs and coordinates the activity of the District Attorney's Office) and the Administrator of the Court (with management functions, appointed by the Court President among candidates that are selected by the Ministry of Justice). Each court district (*comarca*) has one Court President, who assumes broader management responsibilities than those assumed by the Chief Judge before the reform, corresponding to the structure of best-practice (Palumbo et al., 2013). The Court President is appointed for three years by the High Council for the Judiciary and is accountable to it.

In spite of increased management responsibilities, the Court President has not gained sufficient autonomy in practice. The Court President manages the court, monitors the objectives set for the court's judicial services, and monitors the court's case-flow, among other functions. In terms of case-flow monitoring and management, the Court President can report to the High Council for the Judiciary the cases that have an excessive delay, suggest a reallocation of judges, and prepare reports on the current state of the court being managed. Nonetheless, the scope of such a reallocation of judges may be limited by the total number of judges in the system and by the fact that the number of judges in each court district is determined by law (which can hamper for instance the reallocation of judges from court districts with relatively few cases since the minimum number of judges should be met in these areas), although allowing flexibility.

In this context, the courts should be given increased operational autonomy in order to achieve the objectives for which they are responsible. Reports from first instance courts mention several bottlenecks at the budget management level, with some proposing greater financial autonomy. For instance, the courts' budget is typically used for buildings, materials, utilities, and so on, and it is managed by the Administrator of the Court on the behalf of the Ministry of Justice. The Court Presidents can have a relevant role in the governance of the judicial system, but there were no significant reforms at this level.

Performance evaluation

The capacity and behaviour of judges themselves are a crucial factor for an efficient judicial system. Judges' behaviour is determined by their incentives such as career prospects, salary and the entire organisational structure of the judiciary, among others factors (Voigt, 2016).

There is scope to strengthen the performance evaluation of judges. Judges are evaluated by the High Council for the Judiciary. There is a first evaluation one year after starting their judicial career, and then judges are evaluated every 4 years. The criteria for evaluation are given by Article 34 of Law 21/85 and by Article 12 of Judicial Inspections Regulation

approved in 2016, but the reference to quantitative criteria is limited and they are not fully defined. While performance evaluation is also taken into account, seniority is very important in judges' career progression. There is also the potential to enhance the objectivity in the evaluation of judges. The evaluation of judges is made by inspector judges, who are judges themselves. Having experience as a judge may be helpful in properly evaluating some tasks that are specific to the profession, but it may lead to a lack of objectivity in the evaluation of peer judges. If evaluations consider judgments' length, judges end up writing long opinions which is more time consuming and increases delays. Indeed, inspections tend to consider written judgments to a large extent. Compared with other countries, judges in Portugal tend to write complex and long decisions (Pompe and Bergthaler, 2015).

The authorities could consider reviewing the overall system of performance evaluation with a view to ensuring its full objectivity. As an example, the Netherlands implemented the *RechtspraaQ* system that measures judicial quality, and it was developed by the judicial council in consultation with courts. *RechtspraaQ* focuses on quality regulations and performance measures, with a strong focus at the court level (Contini, 2017). Additionally, it also included instruments such as peer review visits, audits, staff satisfaction surveys, customer satisfaction surveys. There is no obvious or straightforward way of designing incentives for judges, but a more balanced combination of qualitative and quantitative elements could lead to better outcomes in Portugal.

Apart from the evaluation of judges for their career, salaries can also directly affect judges' incentives. In Portugal, salaries are regulated, therefore there are no rewards for performing well and penalties for underperformance. The introduction of an effective incentive salary scheme can be a possibility but it presents several challenges and requires caution. If incentives are set so that judges resolve more cases, judges can simply solve easier cases and avoid more complex ones. In Spain, there was a strong focus on quantitative elements which seems to have resulted in changing judges' behaviour so that they "cherry picked" cases that would allow a higher reward (Doménech Pascual, 2008). On balance, linking salaries directly to performance may be difficult, at least for the moment, when performance measures are not well developed.

Other factors also affect judges' performance. For example, judges' educational background and experience, along with their experience of the specific court (institutional experience) can affect the length of procedures (Ramseyer, 2012 and references therein).

Specialisation of courts and judges

Task specialisation is often advocated as a major performance-enhancing factor. Specialisation can enhance court efficiency by allowing judges to acquire detailed knowledge of a given area of law and of the issues. It can also aid a more efficient organisation of the work, by preventing judges from being assigned to widely different categories of disputes, and is likely to guarantee a higher consistency and accuracy of decisions. The negative side of specialisation is the inability for judges to benefit from knowledge spillovers. These effects consider the specialisation of individual judges, not that of courts, and the empirical evidence on the effects of specialisation is mitigated (e.g. (Voigt and El-Bialy, 2016).

The current judicial organisation implemented by the 2014 reform also aimed to enhance specialisation. The reform mentions a reinforcement of specialisation brought by an increase in family and juvenile courts, criminal instruction courts, enforcement courts and commercial courts. However, as judges may rotate between geographic locations, they

might be working mostly on one type of cases in one year and on a completely different case the year after, especially in the first years of judges' career. If the authorities aim at further specialisation in the court system, they should consider introducing greater specialisation of individual judges, including appropriate training as specialised judges.

A different kind of specialisation is the presence of non-judge staff providing legal assistance to judges. Legal assistance may enhance performance by freeing judges from auxiliary tasks (legal research, drafting of memoranda, case preparation and management), enabling them to concentrate only on adjudication. Judges could speed up case resolution by up to 30% if they were supported by assistant clerks in Portugal (Hay Group, 2002). Borowczyk-Martins (2010) also finds a positive effect of clerks on the resolution rate in Portuguese civil courts.

It could be a good option to strengthen legal assistance to judges by other professionals. In respect of Law 62/2013, it should be ensured that the organisation of clerks' work should be made more flexible in responding to arising needs. Greater specialisation of clerks would also be advisable in order to promote efficiency in the assistance they provide to judges. Finally, it could also be a good option to increase other professionals, such as assistant clerks, or assistant judges, which are currently available only at the Supreme Court.

Better meeting the demand for judicial services

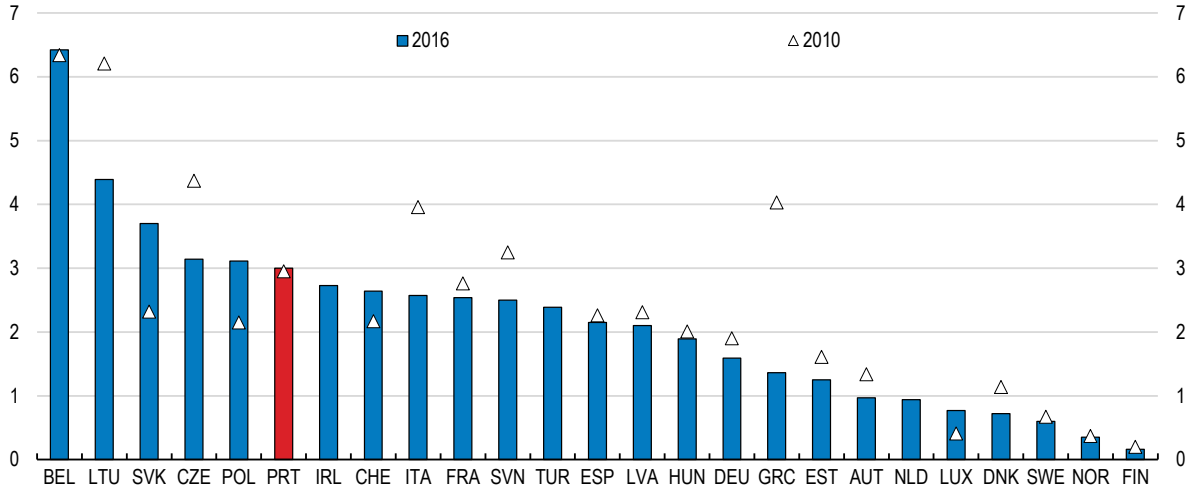
A high demand for judicial services induces court congestion, extending the average trial length in courts. Litigation is frequent in Portugal compared with other European countries for which comparable data are available (Figure 12). The majority of cases brought to judicial courts are civil cases (accounting for 64% of cases, followed by criminal, labour and other types of cases).

A relevant policy question is how to better meet different kinds of demand for judicial services. The high number of litigation cases could be for good reasons. Therefore, it is important to identify properly where so many litigation cases come from. As illustrated below, a number of cases are considered to be ill-founded, which weaken court case resolution and crowd out legitimate demand for judicial services from other people. It is also important to consider if some disputes can be better solved outside the court system.

The number of cases brought to courts depends on the frequency of disputes in society. This is influenced by the business cycle, structural socio-economic factors and the volume and complexity of economic transactions, among others (Palumbo et al., 2013). Over the past decades, the number of litigation cases has been on a rising trend, reflecting the structural change in the economy, such as the rise in the share of the services sector. In this context, so-called "mass-litigation" has developed significantly. This is about a small number of bulk litigants, typically large companies such as cable television operators, mobile phone companies, insurance companies, banks and consumer credit companies, claiming for a small amount of debt, in many cases less than EUR 1 000 (Gomes, 2011).

Figure 12. Litigation is comparatively frequent in Portugal

Number of incoming cases per 100 inhabitants



Source: European Commission for the Efficiency of Justice (CEPEJ).

There is one particular type of demand for judicial services, which is apparently abused. In the Portuguese debt enforcement system, debtors can contest a court decision on debt payment. The problem is that they often contest the court decision with the sole objective to block enforcement procedures and thus to delay payment (Pompe and Bergthaler, 2015). Such spurious litigation was encouraged since trial costs and penalties to lose a case are low (Pompe and Bergthaler, 2015). It has increased bottlenecks in courts, preventing many citizens and companies from using the judicial system for more substantive matters. Such spurious litigation should be reduced, while their debt resolution problem should be settled through different pathways (see below).

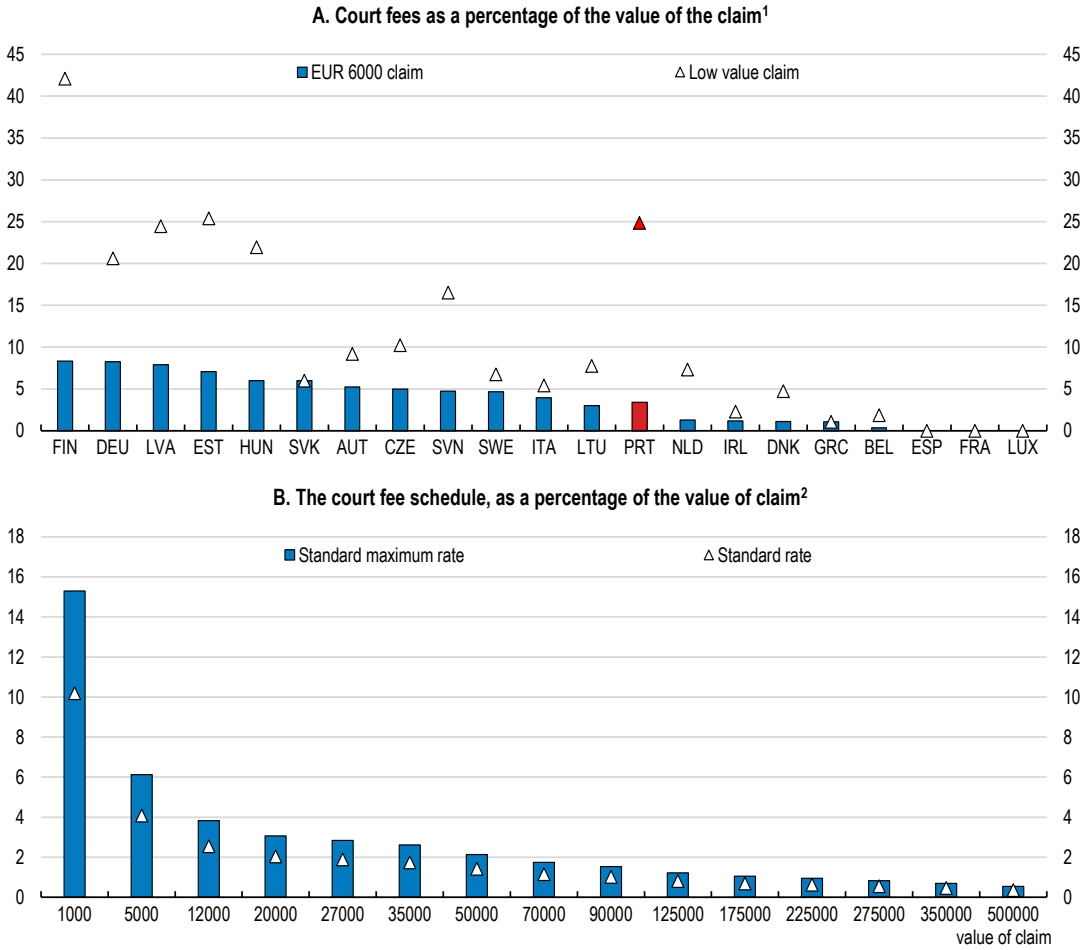
Trial costs shape the demand for judicial services

Costs of trial

The private costs of trial affect the decision to file a case to court. Overall, according to the current system, basic court fees remain very low, except for very low value cases (Figure 13, Panel A). This is particularly so, when the value of claims is high (Figure 13, Panel B). In Portugal, these costs consist of:

- Court fees;
- Charges (actual expenses such as transcriptions, court solicited documents, transport expenses, etc.); and
- Party costs paid by the losing party (cost-shifting rules).

Figure 13. Court fees for a high value claim are low in Portugal



Note: In Panel A, "low value claim' means a claim which corresponds to the poverty threshold for a single person in each Member State in terms of monthly income. In Panel B, the value of claims is the median value across different bands of the value of claim (for e.g. the first band ranges between EUR 0 to 2000; and the bar shows that for a case with the value of claim of EUR 1000, the parties have to pay around 10% of the value or around 15.5% of the value if the standard maximum rate is applied).
Source: EU Justice Scoreboard 2017 and Council of Bars and Law Societies of Europe (CCBE); Procedural Costs Regulation, Portugal.

Court fees are paid for the services of the judiciary and its staff. They are increasing with the value of claims which are specified in the Procedural Costs Regulation. The judge can apply the standard maximum rate (higher by 50%) at their discretion, depending on the complexity of cases within the limits specified in the regulation. When the procedure is particularly complex, such as those requiring preliminary injunctions, execution or reclamation of credits, and opposition to execution or embargos by third parties, the judge can apply even higher court fees, calibrated by legal criteria, specified by the regulation.

The Procedural Costs Regulation has been reformed successively over the past decade. One of the major changes was an increase in court fees for corporates that often litigate (specifically those that litigated 200 times or more in the previous year), so that they face the standard maximum rates (Figure 13, Panel B). This selective increase of court fees specifically targeted so-called bulk litigants (see above) who made the most use of the system and who are able to bear the costs. However, given the overall low costs, in

particular, when the value of claims is high, such effects are likely to be limited. Going forward, court fees can be significantly increased for the above-mentioned "spurious litigation" (debtor contesting a court decision for the purpose of delaying debt enforcement), thus making litigation a conscious choice for these litigants.

The rules determining the allocation of trial costs between the litigants (cost-shifting rules) also affect decisions on litigation. Cost-shifting rules are claimed to induce better litigation decisions by filtering out unmeritorious cases (Palumbo et al., 2013). In Portugal, the losing party is ordered to pay to the winning party the amounts specified by the regulation (so-called "party costs"). Specifically, they pay the court fees and charges paid by the winning party as well as related costs, notably lawyer fees, which are considered to be equivalent to 50% of the court fees paid by both parties, which are low compared to average lawyer fees. Strengthening cost-shifting rules may reduce the frequency of litigation, since it makes litigation a conscious choice, but the effects of such a policy change are not found to be unambiguous. If anything, such a policy change can be introduced in a targeted way, for instance, to debtors litigating for the sole purpose of delaying enforcement processes.

Legal services profession

Lawyers have a central role in determining the pattern of demand for judicial services. Lawyers often decide whether to file a case in court or resolve the issue in alternative ways on behalf of their client. Behind such decisions lie their incentives, which are in turn shaped by regulations and the market structure.

The Bar Association both represents its members and regulates the exercise of the profession. Regulations in the legal services sector are justified to a certain degree, due to the specificities of this sector characterised by the risk of market failures. Among others, problems arising from the fact that consumers cannot judge the quality of judicial services and often rely only on prices ("the asymmetry of information" between lawyers and consumers) are important (Darby and Karni, 1973; OECD, 2007). Therefore, low-quality providers charging low prices can drive out high-quality providers charging high prices, leading to overall quality deterioration in the market ("adverse selection"). On the contrary, the asymmetry of information can incentivise lawyers to supply unnecessarily higher quality services or a larger quantity of services than consumers would require ("moral hazard"). These problems limit the extent to which free markets in legal services produce efficient outcomes (e.g. Ehlermann and Atanasiu, 2006). However, self-regulation tends to identify with the interests of the regulated profession, rather than the public interest (Canton, Ciriaci and Solera, 2014).

In certain circumstances, lawyers can be incentivised to generate more litigation than is necessary. Given the asymmetry of information, lawyers may persuade their clients to file a case to court even when it is not in the best interests of their clients, because the case deals with the claim of a low value or because the case has a low probability of winning (OECD, 2007; Carmignani and Giacomelli, 2010). The behaviour of lawyers to seek excess benefits over production costs lies behind this mechanism (Palumbo et al., 2013). Such behaviour is encouraged when competition in the market is limited, while in a competitive market lawyers are less likely to bring such cases to court.

Previous studies found that the number of lawyers is positively related to the frequency of litigation (e.g. Carmignani and Giacomelli,2010 for Italy; Mora-Sanguinetti and Garoupa, 2015 for Spain). Pereira and Wemans (2015), investigating causes for litigation in Portugal, first find the court district specific effects and related them to the number of lawyers per inhabitant, and conclude that some inducement effects by lawyers exist. These studies

found this causal relationship, controlling for the possibility of the reverse causality (lawyers might increase the frequency of litigation while an increased number of litigation cases might attract more lawyers).

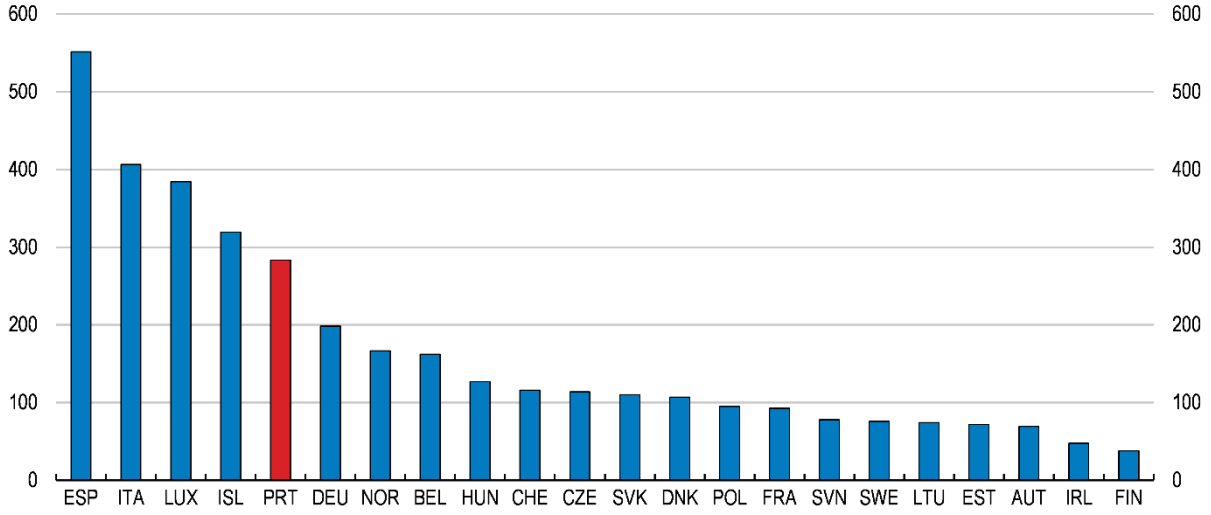
There is an excess supply in the Portuguese legal services sector. The number of lawyers per inhabitant is larger than in many other European countries (Figure 14) and the number of law firms per inhabitant is also large (Paterson, Fink and Ogus, 2007), in spite of very strict entry regulation in the sector. Productivity is low compared with other European countries (Paterson, Fink and Ogus, 2007; Figure 15), implying lawyers are more frequently involved with low productivity cases. Within the context of very strict conduct regulation (Figure 16), which normally is associated with rents, it is likely that excess profits are shared among a large number of lawyers, which generate more litigation than needed by their clients (OECD, 2018a).

From the policy point of view, it is necessary to increase the transparency of legal contracts for clients to better understand the services provided by lawyers (Carmignani and Giacomelli, 2010) and more generally to increase competition in the legal profession sector.

Many provisions foreseen in the recent reform have not been implemented effectively. Framework Law 2/2013, establishing the legal regime for the creation, functioning and organisation of professional associations, intended to remove unjustified restrictions. Along with this framework law, a new bylaw (legislation put forward by the professional associations and adopted by Parliament) was adopted for the legal services profession sector. This bylaw (Law 145/2015) receded from Framework Law 2/2013 in many fronts, notably, the removal of restrictions on the access to regulated professions and the recognition of professional qualifications (OECD, 2018a).

Figure 14. Number of lawyers per inhabitant is high in Portugal

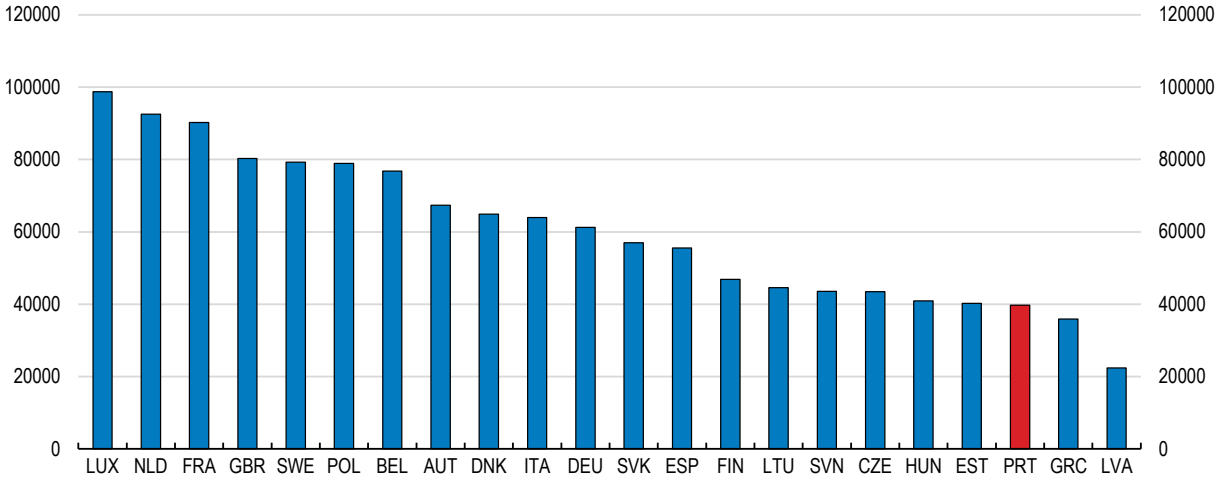
Number of lawyers per 100 000 inhabitants, 2016



Note: 2015 for Belgium, Czech Republic, Estonia, Hungary, Iceland, Italy and Slovenia.
Source: Council of Bars and Law Societies of Europe (CCBE) and OECD.

Figure 15. The productivity in the legal services sector is low in Portugal

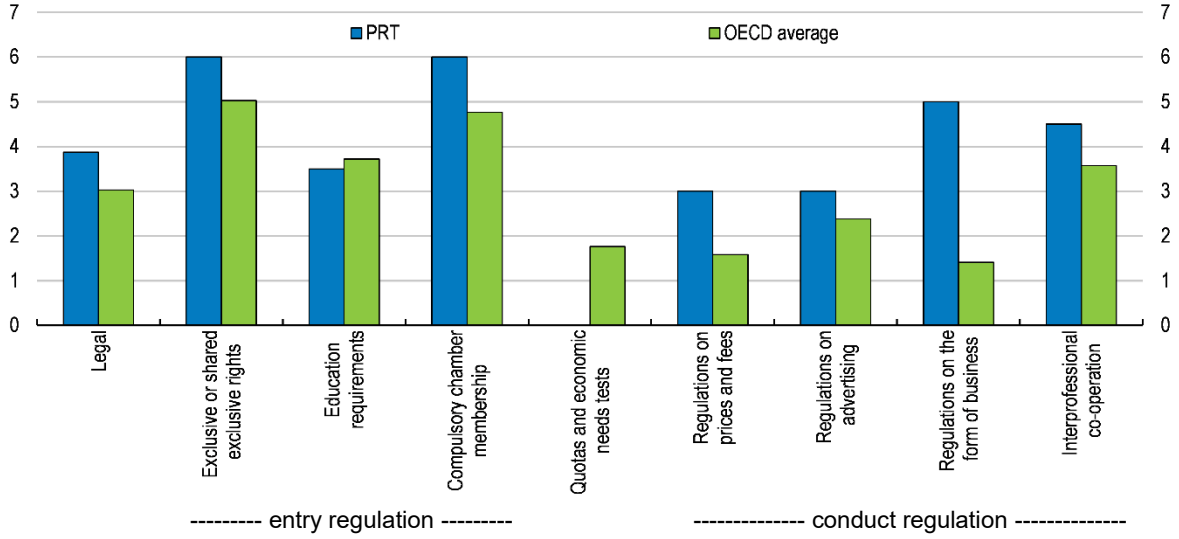
Gross Value-Added per person in employment, USD PPP, in 2015



Note: The chart refers to Gross Value-Added (GVA) and the number of employment in the industry "V69_70: Legal, accounting, head offices, management consultancy activities". 2014 for Lithuania and Sweden. 2011 for Spain. GVA in the industry at 2005 constant prices are measured in terms of USD PPP using the industry level price index provided by the Groningen Growth and Productivity Centre following the methodology in Robert Inklaar and Marcel P. Timmer (2014), "The Relative Price of Services" Review of Income and Wealth 60(4): 727–746.
Source: OECD National Accounts Statistics (database) and the Groningen Growth and Productivity Centre.

Figure 16. Regulation in the legal professions sector is generally strict

OECD Indicators of regulation in the legal services sector



Note: The OECD Indicators of Product Market Regulation are a comprehensive and internationally comparable set of indicators that measure the degree to which policies promote or inhibit competition. The indicator ranges from zero (least stringent) to six (most stringent).
Source: OECD Product Market Regulations Statistics (database).

Restrictions on fees

Fee regulations exist in order to ensure the quality of services offered and to protect consumers from excessive charges. Fee restrictions can take several forms, such as mandatory fixed fees, minimum fees or maximum fees, and recommended fees. When fees are negotiated, recommended fees can also inform consumers of the average fees to be paid for certain services, which reduces transaction costs. However, these restrictions on prices prevent competition among service providers. This is clear for mandatory fixed fees and minimum fees. Maximum fees can lead to a levelling of prices towards the maximum threshold. Recommended fees have similar effects and they can facilitate coordination among service providers at the expense of consumers.

In Portugal, fees are freely negotiated between the relevant parties. The Bar Association, the self-regulatory body, does not set fees for services provided by its members. However, the law specifies the criteria on which the fee structure should be based, including the number of hours worked, the value of claims, the lawyer's qualifications, and the complexity of cases. The criteria in the fee structure also include the outcome of cases ('success fees'), although contingency fees, which tie the lawyers' remuneration entirely to the outcome of cases, are forbidden. As a matter of fact, the criteria are very detailed and exhaustive, which can be useful when the fees charged need to be arbitrated, but are not easily understood by clients, which hampers competition in the legal services market (OECD, 2018a). The complexities in the criteria in the fee structure likely solidify the bargaining power of lawyers, in particular, those in large firms, in negotiating fees with consumers.

The existing regulatory functions of professional associations can be shared with an independent body, which would take on a supervisory role vis-à-vis the Bar Association. The competence to deal with disputes over the legal contract against lawyers, which currently lies with the Bar Association, can be assumed by the independent supervisory body. The latter can ensure an independent and impartial judgment, as it is free from protecting the members which the Bar Association represents. Thus, the independent supervisory body could provide the impartial assessment of legal costs and make them more transparent, seeking to achieve a balance between the costs involved and the services rendered by lawyers.

Reserved activities for lawyers

Excessive regulation of the professions is anti-competitive. Other anti-competitive regulations in the legal services sector include reserved activities for lawyers that cannot be exercised by other professions. The rights to exercise reserved activities exist in order to guarantee the quality of legal services against the risk of market failures (adverse selection). Nevertheless, they can also contribute to excessive market power and inflated prices for regulated services at the expense of consumers. In Portugal, the following activities are reserved for lawyers:

- Exercise of the judicial mandate (representing clients in courts);
- Provision of legal advice and consultation;
- Drafting of contracts and the practice of preparatory acts related to the constitution, alteration or extinction of legal transactions;
- Negotiation aimed at collecting credits; and

- Exercise of the judicial mandate for the challenge of administrative or taxation acts.

The scope of reserved activities by lawyers in Portugal is wide, which may unduly restrict competition from other providers (OECD, 2018a). The rationale for some reserved activities is clear, such as the exercise of the judicial mandate. However, it is not necessarily so for other activities. For instance, it is not obvious why negotiations on credit collection should be reserved for lawyers. Moreover, the mandatory involvement of lawyers on such negotiations is likely to prolong debt enforcement proceedings (see above). This provision could be relaxed so that negotiations on credit collection activities can be exercised also by other professionals, possibly in the form of extended partnership between lawyers and other professionals (see below).

Restrictions on ownership and management

Law firms are subject to regulatory rules governing the form of business, which generally restrict competition. Such restrictions exclude non-regulated legal professionals from running, owning or being shareholders in law firms. Non-lawyers are not members of the Bar Association, thus they would not be bound by the same professional obligations as those for lawyers. The legal profession defends such restrictions on the grounds that they prevent the independence of lawyers being threatened by non-lawyers, undermining the lawyer-client privilege, and giving rise to conflicts of interest (Aulakh and Kirkpatrick, 2016).

In Portugal, law firms are exclusively owned by lawyers ("professional partnership" model), which is disproportionately restrictive. Only lawyers or other law firms can be partners or associates in a law firm, which must be registered with the Bar Association, thereby excluding co-ownership or co-partnership with other professionals which are not lawyers. Also, the Bar Association's self-regulation requires all members of management to be lawyers, although Law 2/2013 requires that only one of the managers or administrators of a professional firm be a member of the professional association. According to the OECD PMR indicator, the restrictions on ownership and management is where Portugal lags the furthest behind other OECD countries, with other European countries including Italy and Spain having removed barriers to the ownership by non-lawyers, albeit modestly. The UK 2007 Legal Services Act reformed ownership and partnership rules, allowing for the creation of Alternative Business Structures (ABS), where non-lawyers may own or partner with lawyers in a legal firm.

Removing barriers to the ownership and management of law firms would rationalise their activities and raise their productivity. Opening ownership to external investors could allow law firms to expand by utilising more sources of capital and to achieve further economies of scale, and to become more competitive in the market, while improving risk management (OECD, 2018a). Alleviating the restriction on management would enhance the ability of professionals to optimise the structure of their firms or groupings. Broadening the sources of funding for the profession can also promote game changing innovations that are better able to respond to the legal needs of a wider range of clients (Hadfield, 2017). Such changes would also open the way to diversifying their businesses. Moreover, evidence from the United Kingdom after the liberalisation of ownership rules, points to ABS being more innovative and having faster take-up of new technology (OECD, 2018a).

Restrictions on inter-professional cooperation

Law firms are also subject to regulatory rules on multi-disciplinary practices between lawyers and other professionals, which also hamper competition and innovation. Multi-

disciplinary practices can threaten the lawyer-client privilege, since non-lawyers are not bound by the same professional obligations as those for lawyers. The legal profession defends the restrictions on multi-disciplinary practices in order to guard professional secrecy and to prevent conflicts of interest (OECD, 2007), as multi-disciplinary practices can be pressured into acting in the commercial interests of the owners, not in the best interests of the clients.

In Portugal, the Bar Association's self-regulation exclude multi-disciplinary practices in law firms. According to its self-regulation, law firms should pursue a single and exclusive objective which is the exercise of legal advocacy. In the mid-2010s, there were some proposals by the Bar Association which examined the possibility of introducing multi-disciplinary practices with other professionals or non-professionals, but none of them was adopted in the end. The *Conselho Superior do Ministerio Publico* (Public Prosecution Judicial Council) also questioned the prohibition on multi-disciplinary practices and found it disproportional to its objective. Indeed, such a prohibition is questionable since currently law firms from other EU Member States can provide multi-disciplinary services in Portugal, which are prohibited to Portuguese law firms.

The removal of the prohibition on multi-disciplinary practices would help better meet clients' demand and raise productivity among law firms. Multi-disciplinary practices can generate further economies of scale and offer 'full service' by bringing together the know-how of members of different professions within the same firm (OECD, 2018a). Such practices would spread diverse risks faced by different professionals within the same firm, thus reducing the overall internal risks (Stephen and Love, 2000). Finally, such practices can also promote innovation, as for instance the experience of Alternative Business Structures for law firms in England and Wales shown in UK Competition and Markets Authority (2016). In Portugal, such cooperation can be beneficial for the development of out-of-court mechanisms for insolvency where the accountant has an increasing role (see below). The risk related to professional secrecy could be countered by imposing similar obligations on all professionals within the same firm (Deards, 2002). The UK 2007 Legal Services Act prescribed that the regulatory safeguards are put in place to overcome this particular problem.

Alternative dispute resolution mechanisms can be developed further

There exist alternative dispute resolution (ADR) mechanisms other than the formal court proceedings. Some of them are literally out-of-court proceedings while others include the intervention of courts. The availability of such alternative dispute resolution mechanisms, also affect the demand for judicial services. Indeed, disputes can be effectively and efficiently resolved through various alternative dispute resolution mechanisms, such as online dispute resolution, mediation, and arbitration. The challenge for lawmakers is to design a justice system that supports parties in bringing their disputes to the right forum, depending on its nature and severity (OECD, 2018b).

Mediation

Mediation is underdeveloped in Portugal. Mediation is one of the alternative dispute resolution mechanisms where the parties try to reach an agreement as regards their dispute, guided by the mediator, an impartial third party. The parties are responsible for the decision they make. Countries offer different types of mediation services under different frameworks (e.g. service providers can be courts or private). In Portugal, mediation is an out-of-court process intervened by a mediator certified by the Ministry of Justice. In 2017,

only 487 cases were resolved through mediation, while the narrowly defined system of mediation is limited only to the three domains – family, labour and criminal. Mediation can be extended to deal with commercial cases, if there are such needs. It can also be strengthened by the intervention of courts, which however comes at the cost of increasing the workload of the courts which is already significantly heavy, in particular, in some court districts.

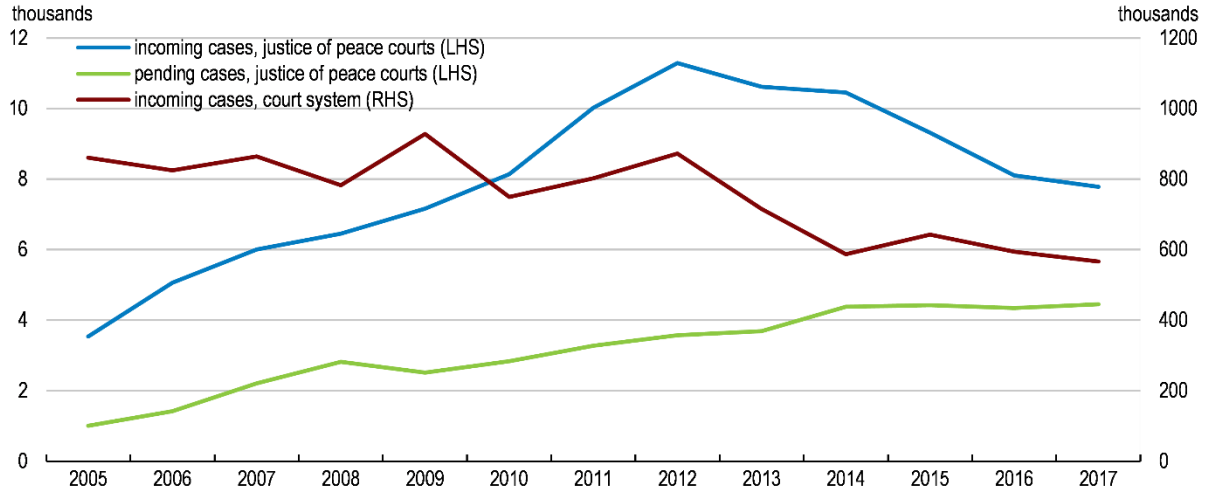
Arbitration

Arbitration is frequently used in some limited cases in Portugal. In contrast with mediation, the arbitrator makes a judgment through arbitration. There are so-called "Arbitration centres" authorised by the Ministry of Justice, which promotes voluntary arbitration. They provide information to the citizens and mediation or arbitration in the form of "Arbitration Court". There are 11 Arbitration centres which are concentrated on certain segments of the economy (such as those in the automobile sector, and the one specialised in taxation matters). Arbitration can be further developed, by establishing more Arbitration Centres. Such needs for arbitration exist, as for example, foreign-owned companies located in Portugal often resort to the Tax Arbitration Centre in order to avoid long proceedings in the tax and administrative court.

The Justice of Peace Courts

The Justice of Peace Courts ("Julgados de Paz") are the unique form of alternative dispute resolution mechanisms in Portugal. It has a particular structure and procedures, which, in practice, make them perceived as a mix of judicial courts and out-of-court proceedings. In the Justice of Peace Courts, disputes can be solved through mediation, conciliation or, if an agreement is not reached, through a court hearing. The latter has simplified proceedings and is presided by the Judge of Peace who delivers a judgment. The Justice of Peace Courts are competent to hear and decide on a number of civil actions, as long as the value of the claim does not exceed EUR 15 000 (with some exceptions, notably, those related to so-called "Contract of Adhesion", which are typically those related to consumption). There are 25 Justice of Peace Courts across 69 municipalities, based on public and/or private financing. The use of the Justice of Peace Courts remains limited and lags far behind the formal court system (Figure 17). In recent years, the number of pending cases has continued to increase in spite of the reduction in the number of incoming cases (Figure 17), suggesting inefficiency in their operation. The Justice of Peace Courts have a scope to be developed further, while strengthening their operation reducing pending cases. They can deal with relatively straightforward disputes over small value claims, the demand for which is apparently very high.

Figure 17. Alternative dispute resolution mechanisms falls far behind the court system



Source: INE.

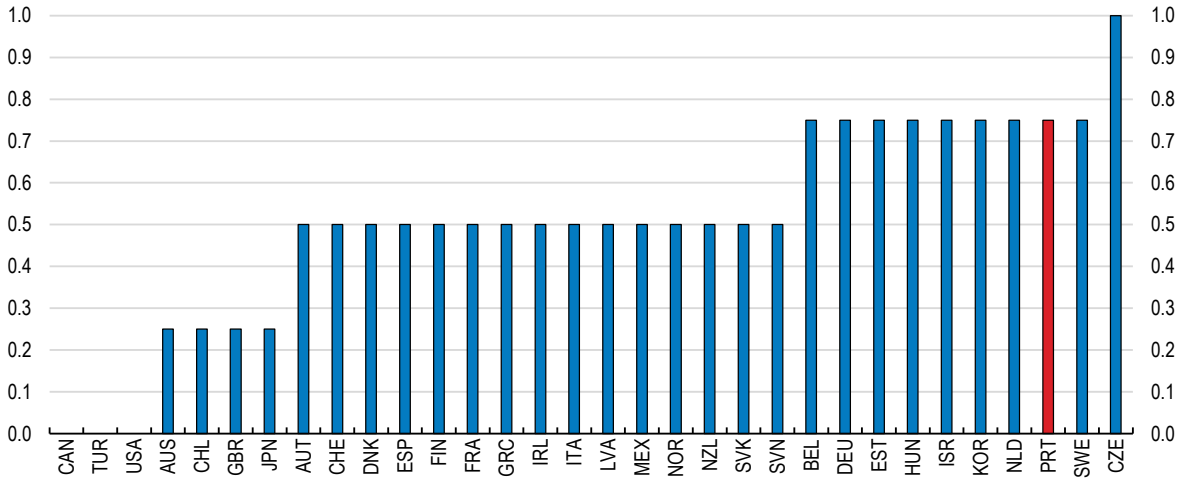
Alternative dispute resolution mechanisms for debt enforcement

As described earlier, enforcement proceedings typically take around 30 months, with some cases taking excessively long time. Over time, the nature of cases has also evolved, and complex cases with a high value claim requires a quite long time. These complex cases include the category "embargo", where the debtor contest the court order on the debt payment obligation, which is quite often spurious (debtors contest only for the purpose of delaying debt payments as mentioned earlier). Among other cases, the category "creditors' claims" (the procedure allowing other creditors with secured claims over the seized assets to intervene in the case, even if their debt is not overdue or they do not yet have an enforcement title), also takes a long time (Pereira and Wemans, 2018). The latter problem illustrates the difficulties of coordination among different creditors.

The chance for a case to end with the fulfilment of the debt payment obligation is low (only 36% out of total enforcement cases). Around 29% of cases were closed due to a lack of assets. This phenomenon can be explained by the provision that enforcement proceedings are terminated if the debtor's assets are insufficient. This provision, however, would not solve the debt payment obligation altogether. There should be other ways to relieve heavily indebted persons from the debt payment obligation. These include making the bankruptcy regime more effective by reducing its stringency (Figure 18; OECD, 2019b) and developing financially attractive alternative dispute resolution schemes for firm liquidation (see below).

Figure 18. Personal bankruptcy law is stringent in Portugal

OECD insolvency indicator: Treatment of failed entrepreneurs, 2016



Note: The indicator is constructed based on the OECD questionnaire on insolvency regimes. It ranges from zero (least stringent) to one (most stringent). "Treatment of failed entrepreneurs" takes into the following aspects: time to discharge; and bankruptcy exemptions.
Source: Adapted from Adalet McGowan et al. (2017).

Special Proceedings for Revitalisation (PER)

Some specific alternative dispute resolution mechanisms to tackle corporate insolvency have been developed in recent years, among others, the *Processo Especial de Revitalizacao* (PER). The PER comprises two alternative proceedings. One is the "pre-pack" PER, which is applicable when the debtor and its creditors agree in advance the terms of a restructuring plan and file the PER in the court to obtain the judge's confirmation of the plan and to make it binding on all creditors including those who did not take part in the negotiations. The other one is the "negotiated-through-court" PER, where the negotiations to reach a restructuring agreement are conducted after the filing of the proceeding and are supervised by the Judicial Administrator, without any interference by the judge.

The PER has improved Portugal's firm restructuring regime, which is reflected in the World Bank's Doing Business indicators, as well as the OECD's Insolvency Indicators (Adalet McGowan, Andrews and Millot, 2017). It has contributed to around 3 000 firm restructuring cases over the past three years. In 2018, in the context of *Programa Capitalizar,* the government reformed the PER to limit its access only to viable firms, in order to maximise the probability of successful restructuring. To start a PER proceeding, the debtor must present to the court an accountant's statement certifying that it is not insolvent and a proposal of the recovery plan. The commencement of a PER proceeding is now also subject to the approval of at least 10% of its creditors.

Out-of-court regime for firm restructuring (RERE)

In parallel, a new out-of-court regime for corporate recovery (*Regime Extrajudicial de Recuperacao de Empresas*, RERE) was introduced in early 2018. In this out-of-court regime a debtor company in financial distress negotiates with all or some of its creditors, to be selected by the debtor, to reach an agreement on a restructuring plan without the intervention of courts. The agreement is binding only on the participant creditors while it is confidential to others. Both the debtor and creditors can benefit from the same tax

treatment that would apply should they have reached the same agreement through a PER or through insolvency proceedings.

Also in the context of *Programa Capitalizar*, the Company Recovery Mediator was created, the statute of which came into force in 2018. The Corporate Recovery Mediator is responsible for assisting a debtor company in financial distress in negotiations with its creditors. Where appropriate, the Mediator may even assist the debtor in a PER or a RERE proceeding.

An alternative dispute resolution mechanism for firm liquidation

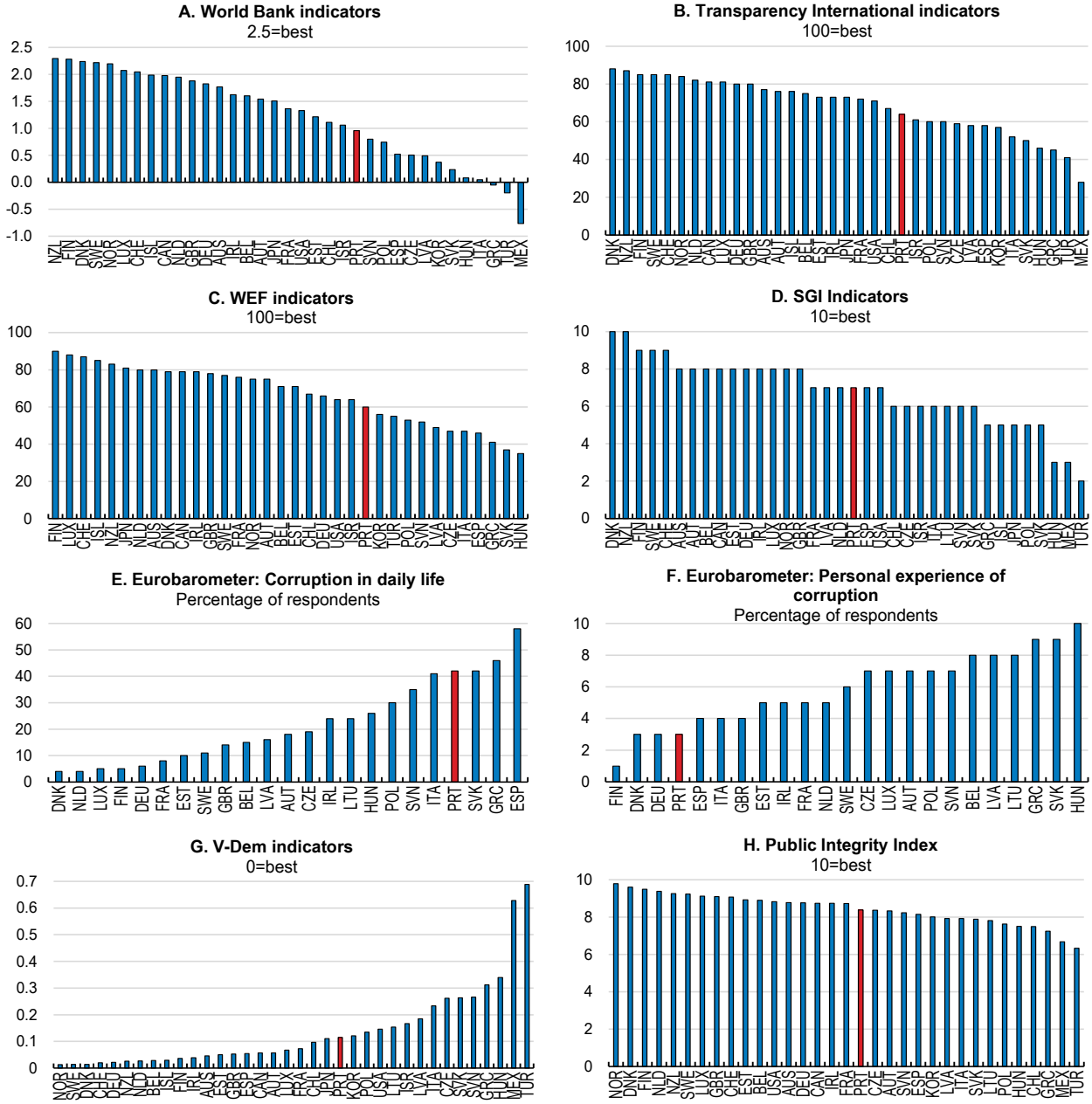
These are positive developments, but it is worth considering the introduction of an alternative dispute resolution regime for firm liquidation. There exists an out-of-court mechanism for defaulting firms, the so-called "Martian pact", through which the creditor appropriates the pleaded assets of the debtor. This is a voluntary mechanism and facilitates the appropriation of the debtor's assets without recourse to the courts. However, the scope of this regime is limited precisely to those assets pledged in the prior agreement between parties. Going further, an out-of-court regime which would primarily facilitate the liquidation of non-viable firms would help, in order to ensure their smooth exit from the market and thereby reduce the costs related to business failure.

Such an out-of-court regime should facilitate coordination among creditors and enhance cooperation among the parties concerned. In this respect, a recent example in Japan (the Guideline for Personal Guarantee Provided by Business Owners) can be insightful. It aims at starting a proceeding on debt resolution at early stages, thus preventing the deterioration of the firms' financing status, which raises the amount of assets which can be collected by the creditor. It makes the financial state of the firm transparent, allowing for an accurate valuation of the firm, which also often leads to revealing hidden assets of the debtor. Finally, the debtor is allowed to keep more assets than if they declare personal bankruptcy (the legal protected assets), within the limit of the increment in the collectable assets (OECD, 2017). Such debt resolution can also be encouraged with financial incentives, namely, the deduction of losses incurred by creditors as a consequence of debt resolution from corporate taxes, as is the case in Japan.

Improving institutional quality and preventing corruption

While extending past and on-going reform efforts, the judicial system should improve institutional arrangements to ensure transparency and strengthen the prevention of corruption. The assessment of the level of corruption is difficult since existing indicators are mainly based on perceptions. Various measures point to different levels of perceived corruption (Figure 19). Corruption distorts economic activity, reducing efficiency and increasing inequality by favouring the well-positioned. As a result, the cost of doing business increases, public resources are wasted and the poor are pushed aside. Perceived corruption is also found to negatively affect FDI inflows (Júlio, Pinheiro-Alves and Tavares, 2013).

Figure 19. Indicators of corruption



Note: "World Bank indicators" refers to "Control of Corruption" in the Worldwide Governance Indicators by World Bank; "Transparency International indicators" refers to the "Corruption Perception Index"; "WEF indicators" refers to the World Economic Forum's Executive Opinion Survey; "SGI Indicators" refers to "Corruption Prevention" in the Sustainable Governance Indicators Score. "Eurobarometer: corruption in daily life" refers to the share of respondents who agreed with the statement "You are personally affected by corruption in your daily life"; "Eurobarometer: experience of corruption" refers to the share of respondents who answered positively to the question "In the last 12 months have you experienced or witnessed any case of corruption?"; "V-Dem indicators" measure six distinct types of corruption that cover both different areas and levels of the polity realm; and "Public Integrity Index" measures six policy areas that can contribute to effective control of corruption.

Source: World Bank, Transparency International, World Economic Forum; Bertelsmann Stiftung; Eurobarometer; Varieties of Democracy Institute, University of Gothenburg; and European Research Centre for Anti-Corruption and State-Building.

Establishing safeguards and integrity frameworks can help effective prevention. The government has pledged to create a public registry of interests for members of local governments, even though this has not yet been implemented (European Commission, 2018). Such a registry should be kept in electronic form, regularly updated and monitored.

Reliable judicial systems are crucial to make sure laws and regulations are actually enforced. In this respect, court judgement should be rapid and effective, including through allocating court resources more effectively. Also, specialised courts with national jurisdiction for corruption could be considered. Such courts currently operate in some other OECD countries, such as the Slovak Republic. The appeal procedures should be reviewed with a view to minimising abuse. Finally, it is important to continue using financial investigations to seize assets obtained through the commission of criminal offences. These measures would prevent the value of assets from declining and the ownership of assets being appropriated by criminals, thus making sure that crime does not pay.

A key factor to fight against crime is an effective mechanism of prosecution (Box 4). There is scope to continue strengthening the prosecution mechanism in Portugal. A package of 88 measures proposed by judges, prosecutors, lawyers and other legal professionals in January 2018 contained some measures on this front. The recommended measures include setting up a technical assistance office in all court districts (*comarcas*), creating multidisciplinary teams of experts, developing international judicial cooperation, and increasing transparency in enforcement proceedings by presenting proof of bank account ownership.

Box 4. Public Prosecution in Portugal

As defined by the Council of Europe (2000), "Public prosecutors" are public authorities who, on behalf of society and in the public interest, ensure the application of the law where the breach of the law carries a criminal sanction, taking into account both the rights of the individual and the necessary effectiveness of the criminal justice system. Public prosecutors have a crucial role in enforcing and effectively applying the law in any judicial system (Garoupa, 2012). They exercise a critical role in criminal cases, but also in other cases. Prosecutors, together with judges and the police, are central actors when it comes to the implementation of the rule of law. Still, little attention has been devoted to the study of public prosecutors, in comparison with judges or the police (Garoupa, 2012; Voigt and Wulf, 2019). In fact, little is known about the impact of the organisation of public prosecution (Gutmann and Voigt, 2017). The precise way in which public prosecution is organised varies across legal systems. Even though there are remarkable institutional differences among European countries, prosecutors tend to be part of the judicial branch.

In Portugal, the Public Prosecution Service represents the State, defends the interests prescribed by law, takes part in the enforcement of criminal policy, carries out the prosecution according to the principle of legality, and defends the democratic legality (Constitution of the Portuguese Republic and Statute of the Public Prosecution Service). Besides exercising tasks and powers in the criminal field, the Public Prosecution Service extends its functions to other relevant areas of the law, such as administrative, civil, constitutional, family and juvenile, taxes and labour. Similarly to judicial courts, the public prosecution service tends to have little control over the budget. The Prosecutor General's Office is the highest body of the Public Prosecution Service, and its president is the

Prosecutor General. The Prosecutor General is nominated by the political power for a six-year mandate.

Public prosecutors are trained in the same judicial school as judges (CEJ). They are subject to inspections made by the High Council of the Public Prosecution Service.

Considering the development of criminality, appropriate and additional training have been regarded as crucial to reach consistent and effective results (Council of Europe, 2000). Appropriate training should continue to be provided to public prosecutors before their appointment and on a permanent basis. Moreover, specialisation should be considered as a priority, along with the use of multi-disciplinary teams that can assist public prosecutors. In the past years, new forms of crime have emerged, namely with transnational organised criminal groups who seek to exploit legitimate activities for criminal purposes (United Nations Office on Drugs and Crime).

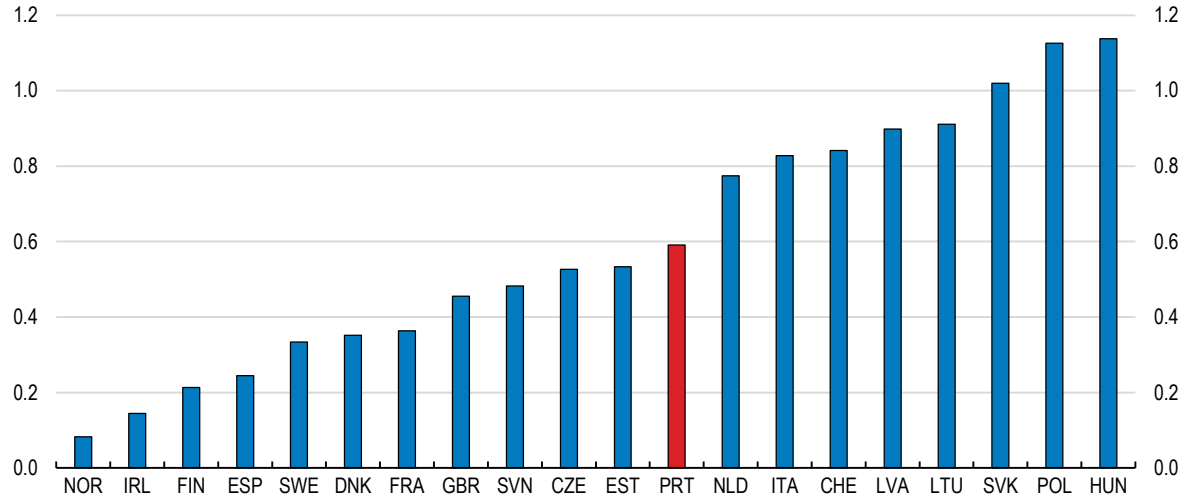
The Public Prosecution Office and Criminal Investigation Police should be endowed with adequate resources, which helps to investigate crimes but also to deter corruption from occurring in the first place. The Public Prosecution Office has strengthened the collection and analysis of evidence to improve the effectiveness of anti-corruption investigations and the cooperation with audit and control bodies to improve the detection of graft (European Commission, 2018). "Forensic-lab" is a new equipment processing a huge amount of information, recently purchased by the Central Department for Criminal Investigation and Prosecution. This lab is able to quickly locate specific information that must be reported during investigations, resulting in an improvement in terms of treatment of materials.

In tandem, specialised training for public prosecutors should be reinforced. Specialised training is important because it enables public prosecutors to be able to perform their professional activity, as complex cases such as those related to economic and financial crime often require specific knowledge and expertise. The "ETHOS project", which ended recently, provided internal specialised training to approximately 60 public prosecutors. One of the main focuses was to provide training regarding asset recovery and non-legal issues that are also relevant for corruption cases. It is important to make specialised training mandatory.

Forensic investigations of economic and financial crimes often entail long and complex judicial processes. It is important that the public prosecution services have adequate resources at their disposal to undertake such forensic investigations. The funding of the Public Prosecution Office in Portugal is comparable with most other European jurisdictions (Figure 20), although it is notably lower than in some countries such as Switzerland and the Netherlands in which the available indicators suggest perceived corruption is very low. It should be noted that such comparisons of budget allocation do not take into account cross-country differences in the remits of public prosecution offices. In the next few years, a significant proportion of the current stock of public prosecutors will be retiring, meaning that there needs to be a strong effort in recruitment and training.

Figure 20. Resources to public prosecution services differ notably across countries

Public budget allocated to public prosecution services per inhabitant as a ratio to GDP per capita, 2016



Note: The numbers are multiplied by 1000.
Source: European Commission for the Efficiency of Justice (CEPEJ).

Recommendations to enhance judicial efficiency

Institutional settings of the judicial courts

Key recommendations

- Increase the managerial autonomy of the courts so that they can effectively allocate resources such as judges, other judiciary staff and budgets.
- Fully analyse the data collected from the information system on court proceedings (CITIUS) so that it allows the courts to identify problematic cases and those that should be prioritised.

Other recommendations

- Improve the CITIUS information system by extending on-going efforts on digitalisation.
- Review the overall system of performance evaluation of judges with a view to ensuring its full objectivity.
- Provide access to detailed data on court decisions to allow the quality of court decisions, case complexity and related costs to be identified in order to assess court performance and the effects of past reforms.
- Strengthen legal assistance to judges by increasing the specialisation of clerks and ensuring the organisation of clerks is flexible.
- Consider introducing assistant judges in lower level courts.

Demand for judicial services

Key recommendations

- Introduce an out-of-court mechanism to facilitate the liquidation of non-viable firms.
- Set up an independent supervisory body to ensure that regulations in the legal profession are in the public interest.

Other recommendations

- Review the reserved activities for lawyers, which unduly restrict competition, such as those on negotiations on credit collection.
- Remove the restrictions on external professionals owning and managing law firms responding better to the needs of a wider range of clients.
- Remove the prohibition on working directly with other professionals in law firms to gain further economies of scale and offer a wider range of services.

Strengthening the prevention of corruption

Key recommendations

- Continue to enhance the capacity of the Public Prosecution Office to address economic and financial crime, including corruption. Public prosecutors should continue to undertake specialised training in this area.
- Establish an electronic registry of interests for all government members and senior civil servants that is regularly updated.

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