CORONAVIRUS: INTERNATIONAL REGULATORY UPDATE AUGUST 2020

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International

In view of continuing improvements in US dollar funding conditions and the low demand at recent 7-day maturity US dollar liquidity-providing operations, the Bank of England, the Bank of Japan, the European Central Bank and the Swiss National Bank, in consultation with the Federal Reserve, have jointly decided to further reduce the frequency of their 7-day operations from three times per week to once per week. This operational change is effective as of 1 September 2020. At the same time, these central banks will continue to hold weekly operations with an 84-day maturity.

European Union

The EU Commission has submitted to the Council proposals to grant financial support worth EUR 81.4 billion to Belgium, Bulgaria, Croatia, Czechia, Greece, Spain, Italy, Latvia, Lithuania, Malta, Poland, Romania, Slovakia, Slovenia and Spain, and an additional proposal to grant EUR 5.9 billion to Portugal, under the temporary support for the mitigation of the risks of unemployment in emergency situations (SURE) instrument, established by Council Regulation (EU) 2020/672 of 19 May 2020. If approved, the EU will be able to offer financial support to the Member States in the form of loans granted on favourable terms.

The European Securities and Markets Authority (ESMA) has published a final report on draft regulatory technical standards (RTS) postponing the entry into force of the CSDR settlement discipline regime until 1 February 2022. The final report follows Commission Delegated Regulation (EU) 2020/1212

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postponing the entry into force of the settlement discipline RTS from 13 September 2020 until 1 February 2021.

ESMA has also announced that the 2019 guidelines on stress test scenarios under the Money Market Funds Regulation (MMFR) will be updated to include revised risk parameters modified in light of the COVID-19 pandemic. Pending the 2020 update, which ESMA intends to publish in Q4 2020, the 2019 guidelines continue to apply, including the existing calibrated scenarios and the internal stress test exercise to be carried out by managers of MMFs. The calibration of the risk parameters will be carried out by ESMA in collaboration with the European Systemic Risk Board (ESRB) and the European Central Bank.

The European Banking Authority (EBA) has published its updated annual work programme for 2020 to reflect the changes to its activities as a result of the pandemic. The updated work programme is intended to alleviate the burden on banks and to limit interaction with the industry to a minimum. For this reason, the EBA has only launched new consultations which were considered critical, postponed the publication of final technical standards depending on their degree of finalisation and expected time of implementation, and put on hold data collections normally used for ad-hoc analyses.

The EBA has published the final reports on its:

- guidelines on supervisory reporting and disclosure requirements in compliance with the CRR 'quick fix' in response to the COVID-19 pandemic (EBA/GL/2020/11);
- guidelines amending the guidelines on uniform disclosures under Article 473a of the CRR on the transitional period for mitigating the impact of the introduction of IFRS9 on own funds to ensure compliance with the CRR 'quick fix' in response to the COVID-19 pandemic (EBA/GL/2020/12); and
- draft implementing technical standards on supervisory reporting by institutions under CRR, accommodating CRR2 and the CRR 'quick fix' in the light of COVID-19 (EBA/ITS/2020/07).

The EBA has also published a set of frequently asked questions related to the implementation of its Guidelines on reporting and disclosure of exposures subject to measures applied in response to the COVID-19 crisis. The technical clarifications provided by the EBA are intended to assist supervisors and credit institutions in the implementation of the guidelines. The implementation questions and technical clarifications have been included in a newly added section 4 to the EBA Report on the implementation of selected COVID-19 policies first published on 7 July 2020. As a significant number of issues have arisen and may continue to arise in the context of the EBA's monitoring of the implementation of COVID-19 policies, the EBA expects to update the report again at a later stage.

Luxembourg

The Luxembourg insurance sector supervisory authority, the Commissariat aux Assurances (CAA), has issued a new circular letter (20/15) with respect to the European Systemic Risk Board (ESRB) Recommendation of 27 May 2020 on restriction of distributions during the pandemic (ESRB/2020/7). The CAA recommends that Luxembourg (re)insurance companies refrain, for a period from 1 August 2020 and at least until 1 January 2021, from:

- making a payment of dividends or irrevocably undertaking to make a payment of dividends,
- repurchasing common shares, and/or
- creating an obligation to pay variable remuneration to a significant risks taker,

if such measures have the definite or probable effect of reducing the quantity or quality of own funds at the level of the EU group or, where applicable, at the individual level where the financial institution is not part of an EU group.

The CAA has also provided further recommendations applicable at the individual level and for companies which are not part of an EU group. Luxembourg (re)insurance companies that consider that they cannot comply with the new recommendations are required promptly to explain their reasons to the CAA. The CAA has emphasised that these recommendations apply until 1 January 2021. Given their temporary nature, the regulator will further evaluate the economic situation and, in light of potential future recommendations from EU authorities, consider whether this deadline should be extended beyond 1 January 2021.

United Kingdom

The Financial Conduct Authority (FCA) has published a feedback statement and its finalised updated guidance for insurance and premium finance firms on coronavirus and customers in temporary financial difficulty. The guidance sets out the FCA's expectations for firms when considering the fair treatment of existing customers in financial difficulty due to circumstances arising from coronavirus.

The FCA has also written to the CEOs of firms who provide a non-discretionary investment service, noting that a number of firms who hold client money have reported an increase in client money balances, in some cases significantly so, in their reporting from January to June 2020, as a result of clients rebalancing their portfolios to mitigate volatility during the pandemic. In its letter, the FCA calls on relevant senior managers to consider whether their firm needs to hold client money balances which are unlikely to be reinvested, or whether it would be in their clients' better interests to place these balances directly with their own current or savings account providers. The FCA considers it good practice in this period for firms to communicate with clients about increased client money balances to ascertain whether these should be returned to them or continue to be held by the firm to facilitate further investment in the short term. If it is in clients' better interests during this period, the FCA expects firms to return client money balances which are unlikely to be reinvested in the short term.

The FCA is also seeking feedback on proposals for the next stage of its support for mortgage borrowers who are facing payment difficulties due to the pandemic. The proposals supplement the FCA's guidance on mortgages and coronavirus which was published in June and is expected to expire on 31 October 2020. The additional draft guidance focuses on how firms should support customers who have already benefitted from payment deferrals under the June guidance and who still require further support, or those whose financial situation may be newly affected by coronavirus after the current guidance ends. It proposes that firms should consider the appropriateness of a range of short and long-term support options according to the specific circumstances of their customers. These options include extending the repayment term, restructuring the mortgage or offering short-term periods of reduced or no repayments. Comments on the proposed guidance are due by 1 September 2020.

In response the FCA's proposals to supplement its guidance, the Prudential Regulation Authority (PRA) has published a statement on the treatment of COVID-19 related payment deferrals in the context of IFRS 9 and the Capital Requirements Regulation (CRR). The statement notes that a borrower's use of COVID-19 related payment deferrals under the FCA's original guidance would not necessarily be deemed an indicator of a significant increase in credit risk (SICR), credit impairment, or default. However, if a borrower requires tailored forbearance provided in accordance with the FCA's draft updated guidance, this may be deemed as good an indicator of SICR, credit impairment or default as forbearance was prior to the pandemic. The PRA notes that the framework for making holistic assessments of loans subject to payment deferrals for indicators of SICR or credit impairment, published in its June letter to the chief executive officers of UK deposit takers, will be relevant when making that judgement.

The PRA has also published a policy statement providing feedback on its consultation on temporarily extending coverage under the Financial Services Compensation Scheme (FSCS) for temporary high balances (THBs) from six months to twelve months from the date of deposit or the first date the THB becomes legally transferable to the depositor. The extension of coverage is in response to the impact of COVID-19 on residential property and investment markets, and access to banking services for some depositors. The policy statement also includes final policy in the form of amendments to:

- the Depositor Protection Part of the PRA Rulebook (Appendix 1); and
- the updated Statement of Policy 'Deposit Guarantee Scheme' (Appendix 2).

The rule change and updated Statement of Policy will be effective on 6 August 2020. Coverage for THBs will revert to six months from 1 February 2021.

Finally, the PRA has published a statement setting out its decision to terminate its temporary approach to VAR back-testing exceptions from 30 September 2020. From Thursday 1 October 2020 onwards, firms should no longer apply any commensurate reduction in risks-not-in-VAR (RNIV) capital requirements. The decision has been made in light of the amendments made to the Capital Requirements Regulation (CRR 'Quick Fix') in response to the pandemic.

Australia

The Australian Securities and Investments Commission (ASIC) has announced new relief measures for operators of managed funds to facilitate withdrawals by members facing financial hardship during the COVID-19 pandemic. The conditional relief is available through a legislative instrument, which applies to all responsible entities (REs) of registered managed investment schemes that have become 'frozen funds'.

ASIC has also issued Information Sheet 249: Frozen funds – Information for responsible entities (INFO 249) and revised Regulatory Guide 136 Funds management: Discretionary powers to provide updated guidance to REs of frozen funds on its available relief during the COVID-19 pandemic.

Hong Kong

The Hong Kong Monetary Authority (HKMA) and the Banking Sector SME Lending Coordination Mechanism have announced a 90-day repayment deferment for trade facilities under the pre-approved principal payment holiday scheme, in order to ease corporate customers' short-term cash-flow pressure due to the pandemic. The deferment will cover trade loans both currently subject to the scheme as well as those drawn between 1 May 2020 to 31 July 2020 by eligible corporate customers with no outstanding payments overdue for more than 30 days as at 1 August 2020. For facilities which are self-liquidating in nature, authorised institutions may require the loan to be settled when the underlying payment has been received by the customer. All other terms of the scheme stated in the annex to the HKMA's circular on 17 April 2020 will continue apply. The HKMA notes that, since the launch of the scheme in May 2020, only between 10% to 20% of eligible corporate customers have chosen to take up the scheme. The HKMA considers that rather than requiring authorised institutions to inform all eligible customers with trade loans of the extension, customers in need of relief should contact their authorised institutions to request the detailed terms of the 90-day deferment, including the financial implications. The HKMA has indicated that it will continue to engage banks and the commercial sector through the Banking Sector SME Lending Coordination Mechanism and arrive at a decision regarding follow-up arrangements for the scheme. The scheme is due to end in October 2020.

RECENT CLIFFORD CHANCE BRIEFINGS

Coronavirus and financial stability risks for UK and EU insurers

In July 2020, the European Insurance and Occupational Pensions Authority (EIOPA) published its 2020 financial stability report for insurers and occupational pensions schemes in the EU, providing a quantitative and qualitative assessment of potential risks in the sector. While the report acknowledges the industry was well capitalised to manage the initial effects of the COVID-19 pandemic as a result of the risk-based approach adopted in the Solvency II regulations, it has identified a number of risks insurers will need to consider as the long-term implications of the pandemic continue to unfold.

This briefing discusses the report's findings as well as implications for UK and EU insurers.

https://www.cliffordchance.com/briefings/2020/08/coronavirus-and-financial-stability-risks-for-uk-and-eu-insurers.html

Coronavirus – Prudential treatment of payment moratoria in Luxembourg

As a consequence of the COVID-19 pandemic, many businesses and private individuals now face liquidity shortages and difficulties in timely payment of their financial and other commitments. This in turn impacts credit institutions, as delays in the repayment of credit obligations lead to a larger number of defaults and increased own fund requirements.

In this context, Member States and/or institutions have introduced moratoria on payments of credit obligations, with the aim of easing the operational and liquidity challenges borrowers are facing. Such measures have however raised questions regarding their legal effect on the current prudential framework, especially in the context of the application of the definition of default and classification of forbearance. In order to provide clarification, the European Banking Authority (EBA) has published statements, guidelines and a report, and the CSSF has followed by updating its Covid-19 FAQ and issuing circulars to adopt and implement the EBA's publications.

This briefing discusses the regulatory guidance.

https://www.cliffordchance.com/briefings/2020/06/coronavirus--prudential-treatment-of-payment-moratoria-in-luxemb.html

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