ICMA
International Capital Market Association

Regulatory responses to the market impact of COVID-19

By Charlotte Bellamy

Introduction

International, EU and UK supervisors, market authorities, central banks and other official sector bodies have continued to pursue a range of measures in response to the crisis caused by the COVID-19 pandemic since we reported on the official responses to the market impact of COVID-19 in the last edition of this Quarterly Report.

Undoubtedly a central part of the response has been a suite of monetary and fiscal policy actions. ICMA's COVID-19 monetary policy webpage, first published in March and updated on a daily basis, summarises the key monetary policy actions taken by a range of different central banks and other bodies. In addition, ICMA made available a podcast on central bank support for the economy during the crisis, which also touches on fiscal responses from governments in mitigating and containing the economic fallout from the COVID-19 pandemic.

Complementary to this, ICMA's COVID-19 regulatory responses webpage provides links to regulatory-related announcements from various authorities, organised geographically.

This article seeks to provide a flavour of some of the key regulatory actions taken by international, EU and UK official bodies in Q2 2020 in response to the crisis caused by the COVID-19 pandemic, with a focus on the international bond market. It is not an exhaustive list, but seeks to provide an overview of regulatory responses and identify key themes, namely: (a) international cooperation; (b) adjustments to deadlines, work programmes and other timelines; and (c) actions in the area of prudential and accounting regulation. We also briefly summarise certain other relevant actions and announcements taken by international, EU and UK bodies outside of these key themes.

This article does not focus on the support measures introduced by governments in many jurisdictions to alleviate the financial and economic impact of COVID-19, including government guarantee programmes for bank loans and payment moratoria.

International cooperation

Global responses to the crisis continue to be coordinated via bodies such as the G20, the FSB, IOSCO and the Basel Committee on Banking Supervision (BCBS). In the EU, ESMA and other EU bodies have played an important role in coordinating across EU countries and national competent authorities. In addition, there has been coordinated messaging on certain key issues by central banks, regulators and other authorities.

In mid-April, the G20 set out an Action Plan for supporting the global economy through the COVID-19 pandemic, setting out the key principles guiding the G20's response. Among other things, this included support for a time-bound suspension of debt service payments for the poorest countries that request forbearance. Related to this, the FSB reported on the financial stability implications and policy measures taken in response to the COVID-19 pandemic on 15 April, setting out five principles underpinning the official community's response. In summary, the principles are: (i) to monitor and share information on a timely basis to assess and address financial stability risks from COVID-19; (ii) to recognise and use the flexibility built into existing financial standards to support the response; (iii) to seek opportunities to temporarily reduce operational burdens on firms and authorities; (iv) to act consistently with international standards and not to roll back reforms or compromise the underlying objectives of existing international standards; and (v) to coordinate on the future timely unwinding of the temporary measures taken.

The FSB also coordinated with trade associations (including ICMA) and later with the private sector, emphasising that it is supporting international coordination and cooperation on the COVID-19 response in three ways: (i) information exchange, (ii) risk assessments and (iii) coordinating global policy responses. The G20 and FSB have continued to provide a forum for policy discussions and information sharing since then.

IOSCO has also played an important role in coordinating actions and guidance on various matters. In Q2 2020, this included: (a) announcing jointly with the BCBS a deferral of the final implementation phases of the margin requirements for non-centrally cleared derivatives; (b) issuing a statement on the application of accounting standards during the COVID-19 outbreak; and (c) encouraging fair disclosure of COVID-19 related impacts by issuers.

Similarly, the BCBS took a series of actions to support coordination of efforts in responding to COVID-19, following those reported in the last edition of this Quarterly Report. This involved, among other things, a review of the domestic regulatory and supervisory measures taken by its members in response to the crisis. Other actions taken by the BCBS are summarised in the section entitled *Prudential and accounting regulation* below.

In the EU, ESMA has played an important role in coordinating EU national competent authorities' responses to the crisis and cooperating with the other EU supervisory authorities (EBA and EIOPA) across various different areas. ESMA's announcements related to COVID-19 are compiled on its COVID-19 webpage and some of its actions that are most relevant for the international bond market are summarised in the section entitled *Selected other regulatory developments* below.

There have also been several examples of coordinated or aligned action by central banks, regulators and other bodies in the EU and the UK. The FCA, for example, is working closely with the UK Government, the Bank of England and other relevant bodies and several of its statements related to COVID-19 align with or support statements by EU bodies such as ESMA. Some specific examples of this coordination can be seen below.

Adjustments to deadlines, work programmes and other timelines

General re-prioritisation: Many official sector bodies announced re-prioritised work programmes for 2020 and beyond in order to reflect the impact of COVID-19. For example:

- IOSCO announced on 8 April that it was re-prioritising its work and that substantial resources would be devoted to areas impacted by COVID-19. This would include examining investment funds and margin and other risk management aspects of central clearing for derivatives and other securities. A limited number of other workstreams that are close to completion or align with FSB work would continue, but other work, for example in relation to artificial intelligence and the impact of the growth of passive investing, will be de-prioritised.
- The European Commission adjusted its work programme for 2020, noting that the priorities that were set at the beginning of the mandate and presented in January 2020 (including the European Green Deal and the European Digital Strategy) remain valid in addressing the current challenges, but the Commission's adjusted work programme responds to the coronavirus pandemic by prioritising the actions needed to propel Europe's recovery and resilience. Amongst other things, the Commission delayed the adoption of both its Action Plan on the Capital Markets Union and its Renewed Sustainable Finance Strategy from Q3 to Q4 2020.
- ESMA published a revised version of its *2020 Annual Work Programme* on 15 June, including additional work on its immediate reaction to the crisis and indicating potential deprioritisation regarding ongoing and future mandates.
- In the UK, the FCA's business plan for 2020/21 issued on 7 April 2020 was heavily influenced by COVID-19 and it announced at the end of April that it was reviewing its work plans to delay or postpone activity that is not critical to protecting consumers and market integrity in the short term.
- The PRA also announced a re-prioritisation of its work in light of COVID-19. The re-prioritisation entailed, among other things, postponement of various PRA activities in relation to climate change, LIBOR transition and the Insurance Stress Test 2019.

Consultation deadlines: Various consultation deadlines were extended. For example, the European Commission delayed deadlines for several open consultations, ESMA extended all deadlines for consultations with a closing date on or after 16 March and deadlines for several open FCA consultations were extended to 1 October 2019.

MiFID II/R: In particular, deadlines for open consultations on MiFID II/R were extended. This included the European Commission MiFID II/MiFIR review consultation and ESMA's consultation on the non-equity transparency regime. ICMA responded to both consultations. ESMA also postponed the publication dates for annual non-equity transparency calculations and quarterly SI data. For further information, see Elizabeth Callaghan's articles in the Secondary Markets section of this Quarterly Report. In addition, ESMA encouraged national competent authorities not to prioritise supervisory action against execution venues and firms in respect of the deadlines for best execution reports.

SFTR: An important delay for many ICMA members was the Statement made by ESMA on 19 March announcing a three month delay to the first phase of the SFTR go-live, and then a subsequent announcement on 26 March giving forbearance on backloading. ICMA published a summary of the ESMA statements offering clarity on this after discussions among the ICMA SFTR Taskforce and then released an updated version of its SFTR recommendations. See further the update on SFTR implementation by Alexander Westphal in this Quarterly Report.

Margin requirements for non-centrally cleared derivatives: The BCBS and IOSCO announced a deferral of the final two implementation phases of the framework for margin requirements for non-centrally cleared derivatives by one year. The FCA welcomed the delay and announced it would be considering, together with other authorities, how to implement it in the UK. The ESAs subsequently proposed joint draft Regulatory Technical Standards on amendments to the bilateral margin requirements under EMIR on 4 May.

IBOR transition and benchmarks: The FCA supplemented its statement of 25 March that the central assumption that LIBOR will cease to be published at the end of 2021 remains, by announcing adjustments to interim milestones. The Bank of England also pushed back the dates from which haircut add-ons would be applied to LIBOR linked collateral. The Working Group On Euro Risk-Free Rates also agreed to delay certain deliverables due to COVID-19 and postponed the CCP discounting switch date from around 22 June to around 27 July. On 9 April, ESMA issued a Public Statement to promote coordinated action by NCAs regarding the timeliness of fulfilling external audit requirements for interest rate benchmark administrators and contributors to interest rate benchmarks in the context of the COVID-19 pandemic. For other articles relating to IBOR transition and benchmarks in this Quarterly Report, see *From LIBOR to SONIA in the Bond Market*, by Paul Richards, and *Transition to Risk-Free Rates in the Euro Area* by Katie Kelly.

Filing financial reports: Following its public statement recommending NCAs to apply forbearance powers towards issuers who need to delay publication of financial reports beyond the statutory deadline in light of the pandemic at the end of March, ESMA acknowledged on 20 May that some issuers may consider setting the timing of publication of their half-yearly financial reports later than usual within the available time-span, without prejudice to compliance with the Market Abuse Regulation. Similarly, the FCA extended deadlines for the filing of annual company accounts and half yearly financial reports for listed companies in the UK.

Publication of investment funds' periodic reports: ESMA issued a public statement on 9 April directed at fund managers concerning their obligations to publish yearly and half-yearly reports, noting that it expects NCAs to adopt a risk-based approach and not prioritise supervisory actions against these market participants in respect of reporting deadlines. In the UK, the FCA extended deadlines to publish fund reports and accounts.

Supervision and regulatory reporting for financial institutions: The ECB, EBA, EIOPA, the Bank of England, PRA and FCA made various announcements in Q2 2020 relating to extensions to submission deadlines for reports due under prudential or resolution regulation applicable to banks, insurers and pension funds. However, on 26 June, the PRA announced that it would expect, in general, on-time submission for future regulatory reporting going forward, and that the publication timeline for Pillar 3 disclosures should not be affected by COVID-19 in most cases, because firms have now had time to adjust to new ways of working. The FCA made a similar announcement in respect of certain regulatory returns on 26 June. At a global level, the BCBS announced that it will conduct the 2020 G-SIB assessment exercise as planned based on end-2019 data, but it agreed not to collect certain additional data. The BCBS also decided to postpone the implementation of the revised G-SIB framework by one year, from 2021 to 2022, to provide additional operational capacity for banks and supervisors.

Prudential and accounting regulation

Some of the early and important actions taken by EU and UK authorities when the virus started to spread in Europe were to (i) encourage the use of capital and liquidity buffers to support the economy, (ii) provide guidance on the application of accounting rules and (iii) provide flexibility in the application of prudential requirements, with a view to supporting banks to continue lending to businesses through the crisis caused by the COVID-19 pandemic.

Linked to this, there were several calls for banks and other financial institutions to refrain from paying dividends or making distributions in order to ensure that all available capacity was targeted at lending to businesses.

Certain key actions taken by international, EU and UK bodies in this area in Q2 2020 are summarised below.

International bodies

In early April, the BCBS took additional measures to alleviate the impact of COVID-19 such as issuing: (i) technical clarifications designed to ensure banks reflect the risk-reducing effect of governments' extraordinary support measures to alleviate the financial and economic impact of COVID-19 when calculating their regulatory capital requirements; (ii) an encouragement to banks to use the flexibility inherent in expected credit loss accounting frameworks to take account of the mitigating effect of the extraordinary support measures related to COVID-19; and (iii) adjustments to transitional arrangements for the regulatory capital treatment of expected credit loss accounting. Other international organisations, such as IOSCO, made similar statements in relation to the application of accounting standards during the COVID-19 outbreak.

In May, the IMF Managing Director called for bank dividends and buybacks to be halted, suggesting that shareholders who sacrifice now will prosper when growth restarts.

In mid-June, the BCBS met again to discuss the impact of COVID-19. The BCBS (i) reaffirmed its expectation of full, timely and consistent implementation of all Basel III standards based on the revised timeline agreed in March and (ii) confirmed its view that a measured drawdown of banks' Basel III buffers as both anticipated and appropriate in the current period of stress and highlighting that supervisors will provide banks sufficient time to restore buffers taking account of economic and market conditions and individual bank circumstances.

EU

In the EU, Ministers of Finance issued a press release in mid-April noting that it is crucial that banks continue financing households and corporates, including SMEs experiencing temporary difficulties amid the COVID-19 pandemic and, to this end, making full use of the flexibility provided for in the prudential and accounting framework is essential at a time when sufficient financing to cover financial pressures is vital for the economy. They also welcomed actions taken in relation to regulatory and accounting requirements for financial institutions in the current exceptional circumstances and in the area of supervision, and urged all banks that have not already decided to do so to refrain from making distributions and to use the freed capital and available profits to extend credit or other urgent financing needs arising from the ongoing crisis. This statement followed a similar statement that had been made at the end of March by the Chair and political coordinators of the European Parliament's Economic and Monetary Affairs Committee. It was also released on the same day that ECB Banking Supervision announced that it would temporarily allow lower capital requirements for market risk, in a move aimed at maintaining market-making activities and market liquidity. The Chair of the Supervisory Board of the ECB also encouraged banks to use liquidity and capital buffers and said there should be no stigma associated with that in an interview published on 20 April. That message has been repeated in other interviews and publications by the ECB.

Shortly afterwards, on 28 April, the European Commission published an *Interpretative Communication* confirming the statements on using flexibility within accounting and prudential rules made by various EU bodies and encouraging banks and supervisory authorities to make use of the flexibility in the EU's accounting and prudential frameworks. The Commission also proposed a set of "quick fixes" to the CRR, which were adopted by the European Parliament and Council in mid-June and took effect on 26 June following publication in the *Official Journal*.

In an interview with Il Sole 24 Ore on 23 June, Andrea Enria, Chair of the Supervisory Board of the ECB, stated, among other things, that: (i) the relaxation of prudential requirements in response to the COVID-19 crisis, in combination with timely support measures on the part of monetary policy and banking supervision, appeared to be effective; (ii) the ECB would allow sufficient time for banks to re-build their capital positions and the ECB would likely give an indication of the path to post-crisis adjustment in July; and (iii) the suspension of dividends and share buy-backs are temporary and exceptional measures that are designed to be removed as soon as there is greater certainty.

The EBA also took a series of actions including introducing (and subsequently extending) guidelines on legislative and non-legislative moratoria on loan repayments applied in the light of the COVID-19 crisis, guidance on the use of flexibility in certain areas related to the impact of COVID-19 such as supervisory approaches in relation to market risk, the Supervisory Review and Evaluation Process, recovery planning, digital operational resilience and the application of the guidelines on payment moratoria to securitisations. It also introduced guidelines to address gaps in reporting data and public information in the context of measures introduced by authorities in the EU banking sector in the context of COVID-19 in early June.

The European Systemic Risk Board took two sets of actions in May targeted at five priority areas: (i) implications for the financial system of guarantee schemes and other fiscal measures to protect the real economy; (ii) market illiquidity and implications for asset managers and insurers, (iii) impact of large scale downgrades of corporate bonds on markets and entities across the financial system; (iv) system-wide restraints on dividend payments, share buybacks and other pay-outs; and (v) liquidity risks arising from margin calls. The ESRB's actions were supported by ESMA.

UK

In the UK, the PRA published a variety of statements and information regarding various aspects of prudential and accounting regulation in Q2 2020 including the usability of liquidity and capital buffers and various other aspects. It also welcomed decisions by the boards of the large UK banks to suspend dividends and buybacks on ordinary shares until the end of 2020, and to cancel payments of any outstanding 2019 dividends in response to a request from the PRA and published various related publications relevant to insurers as well as banks.

The PRA announcements were supported by updates to an FCA statement regarding its expectations on financial resilience for FCA solo-regulated firms in which the FCA emphasised, amongst other things, that it expects firms to plan ahead, conserve capital and to consider whether discretionary distributions of capital for the purposes of dividends, share buy-backs or remunerations are prudent. The FCA stated that firms may use capital and liquidity buffers to support the continuation of their activities if needed but must keep the FCA or named supervisor informed. It also reminded non-bank lenders subject to IFRS9 that the standard requires that any forward-looking information used in expected credit loss estimates is both reasonable and supportable, and that they should take into account the impact of the coronavirus crisis and state support.

Selected other regulatory developments

In addition to the actions taken under the key themes identified above, a number of other relevant regulatory actions have been taken in Q2 2020.

Alternative Performance Measures: On 17 April, ESMA issued a Q&A to provide guidance to issuers on the application of the ESMA Guidelines on Alternative Performance Measures (APM Guidelines) in the context of the COVID-19 pandemic.

Expectations of funds: Throughout April, the FCA communicated its expectations of funds, including issues relating to virtual general meetings, ensuring compliance with VaR limits and various other points.

MiFID II conduct of business obligations and retail investors: On 6 May, ESMA reminded firms of their conduct of business obligations under MiFID II when providing services to retail investors, issuing a statement on the risks for retail investors when trading under the highly uncertain market circumstances due to the COVID-19 pandemic.

CLO ratings: On 13 May, ESMA highlighted the challenges associated with rating CLOs in a thematic report on CLO credit ratings in the EU.

Disclosure: On 29 May, IOSCO published a statement highlighting the importance to investors and other stakeholders of having timely and high-quality information about the impact of COVID-19 on issuers' operating performance, financial position and prospects. Related to this, ESMA called for transparency on COVID-19 effects in half-yearly financial reports and the FCA's *Primary Market Bulletin No. 28* of 27 May had included, among other things, a statement on market practice on going concern assessments.

Market conduct and transaction reporting issues: The FCA's *Market Watch 63*, published in May, set out the FCA's expectations of market conduct in the context of increased capital raising events and alternative working arrangements due to coronavirus.

MiFIR open access: On 11 June, ESMA issued a public statement to clarify the application of the MiFIR open access provisions for trading venues and CCPs in light of the recent adverse developments related to COVID-19. The FCA supported the ESMA statement.

Conclusion

The actions taken by official sector bodies in response to the market impact of the COVID-19 pandemic have been numerous and wide ranging. It has been encouraging to see international coordination, as well as coordination between central banks, regulators and other bodies within jurisdictions, and alignment on some of the key themes such as adjustments to deadlines and timetables and prudential and accounting regulation. The speed with which certain adjustments have been proposed, agreed and implemented (eg adjustments to the EU Capital Requirements Regulation) is also interesting to note. As noted recently by the Secretary General of the FSB, it is still too early to draw definitive conclusions on the effect of these actions with the pandemic still unfolding, although the financial system seems to have proven more resilient and better placed to sustain financing to the real economy as a result of the G20 regulatory reforms in the aftermath of the 2008 global financial crisis.

Going forward, as the immediate shock of the outbreak of the COVID-19 pandemic subsides and lockdown restrictions ease, it will be important to see whether regulatory measures in areas that are not directly related to the COVID-19 pandemic such as sustainable finance, the EU's Capital Markets Union initiative and digitalisation will be further impacted. ICMA will continue to monitor and discuss regulatory and other developments that impact international bond markets with members. ICMA welcomes feedback from members on our activities in this area. In addition, the ICMA COVID-19 webpages will continue to be updated.

Contact: Charlotte Bellamy
charlotte.bellamy@icmagroup.org