

Clients & Friends Memo

COVID-19 Update: The UK Government and Regulators Respond to the COVID-19 Pandemic

30 March 2020

Background

On 25 March 2020, the UK Government published a letter sent by the Chancellor of the Exchequer, the Governor of the Bank of England and the CEOs of the UK Prudential Regulation Authority (“**PRA**”) and the UK Financial Conduct Authority (“**FCA**”) to leaders of UK banks (the “**Joint Letter**”), addressing the impact of COVID-19 on the UK economy and bank lending. The letter highlighted action taken in concert between the UK Government, the regulators and banks to address the economic impact of the COVID-19 pandemic. In particular, the letter mentions the key measures taken so far, including:

- The COVID Corporate Financing Facility (“**CCFF**”), designed to support larger and investment grade businesses through the crisis;
- The Corona Business Interruption Loan Scheme (“**CBILS**”), a lending scheme delivered by the government-backed British Business Bank (“**BBB**”), designed to support small and medium sized businesses (“**SMEs**”);
- Measures taken by PRA and the FCA, including the relaxation of some regulatory capital standards, and measures to protect UK financial services consumers in financial difficulty; and
- Tax measures including permitting the deferral of Value Added Tax (“**VAT**”) payments.

This memorandum addresses the CCFF, CBILS, and the key tax and regulatory measures taken so far. We expect that the UK Government, the regulators and the banks may need to take further unprecedented measures in the coming months in order to address the extreme economic dislocation produced by the COVID-19 pandemic. In particular, the Joint Letter makes clear that the UK authorities will require the financial sector to “maintain and extend lending despite the uncertain economic conditions”.

We also briefly describe the guidance, issued by the FCA, Financial Reporting Council (“**FRC**”) and PRA on 26 March 2020, on reporting obligations in the current climate, including the FCA’s announcement that it will permit an extra 2 months for listed companies to file their

Cadwalader, Wickersham & Taft LLP (Cadwalader) is a registered limited liability partnership established under the laws of the State of New York. The personal liability of our partners is limited to the extent provided in such laws. Additional information is available upon request or at www.cadwalader.com. A list of our partners, who are Solicitors or Registered Foreign Lawyers in England and Wales, is available for inspection at the above address. Regulated by the Solicitors Regulation Authority.

This memorandum has been prepared by Cadwalader for informational purposes only and does not constitute advertising or solicitation and should not be used or taken as legal advice. Those seeking legal advice should contact a member of the Firm or legal counsel licensed in their jurisdiction. Transmission of this information is not intended to create, and receipt does not constitute, an attorney-client relationship. Confidential information should not be sent to Cadwalader without first communicating directly with a member of the Firm about establishing an attorney-client relationship. ©2020 Cadwalader, Wickersham & Taft LLP. All rights reserved.

audited financial statements (which otherwise would have been required within 4 months of financial year end).

CCFF

CCFF launched on 23 March 2020 and is operated by the Bank of England (“**BoE**”) via a special purpose vehicle, COVID Corporate Financing Facility Limited (“**CCFFL**”). CCFFL will purchase commercial paper (“**CP**”) issued by firms making ‘a material contribution to the UK economy’ (as described below).

It is not necessary for a company to have any prior experience of issuing CP to access CCFF funding, but it must:

- Make a ‘material contribution’ to the UK economy. While the BoE retains discretion, firms will generally be accepted where they: are UK-incorporated (irrespective of their parent’s place of incorporation) with a genuine business in the UK; have significant employment in the UK; or are headquartered in the UK. The BoE will also consider whether a company generates significant revenues, serves a large number of customers or has a number of operating sites in the UK.
- Be able to demonstrate sound financial health prior to the economic fallout of the COVID-19 pandemic. Companies with investment ratings must have been rated as investment grade at 1 March 2020; other companies should consult the BoE’s [advice pages](#) which set out alternative measures for evidencing financial health.
- Not operate in financial sectors regulated by the BoE or the FCA. Leveraged investment vehicles and companies within groups that primarily operate in the regulated financial sector will also be ineligible.

Any CP to be purchased under CCFF must have the following properties:

- A maturity period of one week to twelve months.
- A credit rating of A-3 / P-3 / F-3 / R-3 from at least one of Standard & Poor’s, Moody’s, Fitch and DBRS Morningstar as at 1 March 2020 (where available).
- Issued directly into Euroclear and/or Clearstream.
- Absence of non-standard features such as extendibility and subordination.

CP will be bought in the primary market at a spread above a reference rate, based on the sterling overnight index swap rate. In the secondary market, CCFFL will buy CP at the lower of (i) amortised cost from the issue price and (ii) the price given using the method for primary market purchases. A fee (currently 5bps) will be charged for use of the secondary facility.

CCFF funding is now live and will be available for at least twelve months, but as long as necessary to ease cash flow strains on firms. Six months’ notice will be given prior to any withdrawal of CCFF funding.

CBILS

CBILS provides funding for small- to medium-businesses in the UK whose cashflows are disrupted by lost or deferred revenues following the COVID-19 pandemic. Funding may take the form of term facilities, overdrafts, asset-financing facilities and invoice-financing facilities, provided by government-accredited lenders and guaranteed by HM Government.

Funding under CBILS has the following characteristics:

- Facilities of up to £5 million, available on repayment terms for a period of up to six years (three years in the case of overdrafts and invoice-financing facilities).
- 80% government guarantee against the outstanding facility balance (capped per lender).
- No access or guarantee fees for borrowers: lenders will pay a fee to access the scheme and may charge borrowers their own fees such as exit fees.
- First 12 months' interest and fees paid for by the Government: the borrower will nevertheless remain liable for the full amount of the debt at all times.
- Security: funding up to £250,000 may be unsecured. Above this, security is required unless the lender establishes a lack of assets prior to the borrower using CBILS.

Financing under CBILS will be made available to borrowers that:

- Have a maximum £45 million turnover per annum.
- Have a borrowing proposal which cannot be financed on normal commercial terms but which the lender would ordinarily consider viable, and which the lender believes will enable the business to trade out of short-to-medium term difficulties.
- Do not operate in restricted sectors, at present, these are, financial institutions including insurers and reinsurers (but not insurance brokers); the public sector; employer, professional, religious or political organisations and trade unions.

The CBILS programme is now live. Further information for [borrowers](#), [lenders](#), and [prospective lenders](#) is available from the BBB's webpage.

Regulatory Responses to the COVID-19 Crisis

The PRA and the FCA have also been very active in responding to the crisis.

The BoE/PRA have taken the following prudential and policy measures, available [here](#), in respect of UK banks and building societies:

- Cancellation of the 2020 stress test for the eight major UK banks and building societies.
- The BoE's Financial Policy Committee ("FPC") announced a reduction of the UK countercyclical capital buffer rate to 0% of banks' exposures to UK borrowers with immediate effect from March 11, 2020. The FPC has indicated that it expects to maintain

the 0% rate for at least 12 months. In a separate statement, the PRA made clear that its firm expects banks not to increase dividends and other distributions in response to this reduction and will monitor firms' distributions against this expectation.

- The PRA [wrote](#) to the CEOs of authorised banks providing guidance on the interpretation of IFRS 9 requirements on forward-looking expected credit loss estimates, capital requirements and loan covenant breaches.
- The BoE and the PRA have altered their work plans for the supervision of firms and financial market infrastructures (such as clearing houses). In particular, the PRA will suspend or otherwise delay non-critical data requests, on-site visits and deadlines, including s.166 FSMA skilled person's reports due to be conducted this year. The PRA is also reviewing its approach for considering and processing bank and insurer Senior Manager Function applications to reduce the burden on firms and the regulator.
- The BoE and the PRA have extended their deadline for open consultations on outsourcing and operational resilience until 1 October 2020.
- The PRA has extended the period for implementing the EBA IRB roadmap of regulatory products with the aim of reducing unwarranted variability in the risk-weighted assets calculated using IRB models. The PRA has delayed the following aspects until 1 January, 2022:
 - Proposals related to the definition of default, probability of default and loss given default estimation;
 - The requirement to move to hybrid IRB models; and
 - In addition, banks using the standardised approach to credit risk will also benefit from a delay to changes they need to make as part of guidelines on definition of default.

The FCA has also taken action in a number of areas, including that set out in the following statements and guidance:

- The FCA has set out its expectations in respect of contingency and business continuity planning, and a number of other areas, to help FCA regulated firms navigate the crisis. This information is contained on a new FCA COVID-19 page, which can be found [here](#).
- For firms authorised by the FCA (rather than banks and insurers authorised by the PRA), it has set out its [expectations](#) in respect of firms in relation to regulatory capital and financial resources during the crisis, explaining that it expects firms to use capital and liquidity buffers where appropriate, and to keep the FCA informed regarding financial difficulties or any plans by firms to exit the market.
- The FCA has [extended](#) the closing dates for its open consultations and calls for input to 1 October 2020.

- The FCA has issued a [statement](#) on property fund suspensions, recognising valuers have determined that there is currently material uncertainty over the value of commercial real estate (“**CRE**”). Where a fair and reasonable valuation of CRE funds cannot be established, the FCA considers it appropriate for managers of open-ended CRE funds to suspend dealing in units of these funds, and recognises this as being likely to be in the best interests of investors.
- The FCA has published [guidance](#) for banks, other lenders and mortgage administrators on their treatment of residential mortgage customers during the COVID-19 pandemic. The guidance provides help for firms to interpret Principle 6 of the FCA's Principles for Businesses and MCOB 2.5A.1R, which relate to treating customers fairly and acting in the best interests of customers respectively. Although these statements are nominally guidance, the FCA has made clear that in an enforcement context, a firm is likely to be found to have contravened Principle 6 and MCOB 2.5A.1R if it acted in a manner inconsistent with this guidance.

The new guidance makes clear that firms should:

- Grant customers a payment holiday for an initial period of 3 months, where customers experience payment difficulties as a result of the COVID-19 pandemic and where they have indicated they wish to receive one. A firm should not refuse such a request unless it can demonstrate it is reasonable and in the customer's best interest. A firm may decide to put in place an option other than a 3 month payment holiday, if it is appropriate to do so in the individual circumstances of the case and the firm reasonably considers it as being in the best interests of the customer;
- Ensure that there is no additional fee or charge (other than additional interest) as a result of the payment holiday; and
- Take steps to ensure the overall effect of the payment holiday on monthly payments and the term of the mortgage is fully explained to the borrower, including where the firm arranges to capitalise these amounts. The information given should be provided in good time before any capitalisation takes place, and make clear that the customer could pay more over the lifetime of the mortgage as a result of capitalisation, compared to an alternative means of repaying these amounts, such as in a lump sum.

The FCA has also made it clear that during the pandemic, it does not consider that repossession will be in the best interests of the customer. As a result, repossession should not be commenced or continued with unless the firm can demonstrate clearly that the customer has agreed it is in their best interest.

- The FCA has published [guidance](#) on FCA regulated firms participating in CBILS, noting that loans of up to £25,000 to sole traders and unincorporated enterprises can fall within the scope of FCA regulation of consumer credit. During the current crisis, the FCA has

indicated that it will loosen some of the consumer credit rules relating to affordability; the fact that the customer may, at the time of the application, be temporarily experiencing exceptional financial pressures does not mean that the firm is prevented from making the loan. The guidance also indicates that firms should be willing to exercise forbearance in some circumstances; for example, where forecast income to repay the loan does not arise, lenders should consider deferring repayments until it does.

- In line with ESMA's decision to delay Securities Financing Transaction Regulation ("**SFTR**") reporting, the FCA [confirmed](#) that it will not prioritise supervisory activity towards firms' compliance with the SFTR reporting obligation between 13 April 2020 and 13 July 2020.
- The FCA published a [statement](#) on the impact of the COVID-19 pandemic on firms' preparation for LIBOR transition. Although the FCA did not alter its central assumption that firms cannot rely on LIBOR being published after the end of 2021, it recognised that the pandemic has impacted the transition programmes of many firms. The FCA recognised that in some markets where the transition from LIBOR is still at a relatively early stage, some of the intended milestones set by the FCA and the Working Group on Sterling Risk-Free Reference Rates (the "**Working Group**") could be missed. The FCA, the Working Group and BoE have undertaken to monitor and assess the impact of COVID-19 on transition timelines and are expected to update the market again soon.

UK Company Reporting and Audit Obligations

In a [joint statement](#) on 26 March 2020 from the FCA, FRC and PRA, these agencies acknowledge that in these extraordinary circumstances, previous market practice relating to timing and content of financial information and related audit work must change. The emphasize, however, the ongoing importance of the capital markets in providing finance to business as an aid to economic recovery, and that capital markets rely on timely, accurate information.

Key points from this statement include¹:

- *2 Month Delay of Annual Reporting Deadline for Listed Companies.* As a temporary measure during the extreme disruption of the coronavirus pandemic, the FCA will forbear from suspending the listing of any company that fails to meet the Transparency Directive deadline to publish audited financial statements (4 months from financial year end) if they publish those financial statements within 6 months from financial year end.
- *3 Month Delay to Companies House Accounts Filing Obligations.* All UK registered companies separately have an obligation to file their accounts at Companies House within 6 months (for public companies) or 9 months (for private companies) from financial year end. Companies House has [announced](#) it will grant a 3 month extension for filing of accounts to

¹ The joint statement references several other recent publications by these entities including an [FCA Policy Statement](#), [Guidance for Companies](#) and [Guidance for Auditors](#) from the FRC

any applicant that cites issues around COVID-19. For example, this will permit applications for delayed filing of financial statements for subsidiary companies of listed entities.

- *Preliminary Statements of Account.* The [previously-announced](#) moratorium on preliminary financial statements will end on 5 April 2020. However, the FCA reiterates its belief that the practice of issuing preliminary financial statements well in advance of the deadline for final financial statements adds unnecessary pressure to companies and auditors, and they are hopeful of a shift in market practice.
- *Obligation to Disclose Inside Information Unchanged.* Companies' obligations under the Market Abuse Regulation remain in force, and companies must carefully consider what information constitutes inside information, recognising that the global pandemic and policy responses to it may alter the nature of information that is material to a business's prospects. Companies the global pandemic and policy responses to it may alter the nature of information that is material to a business's prospects.

The FRC has issued guidance for companies dealing with unprecedented uncertainty about their prospects. They advise boards to focus on:

- Reviewing control and reporting procedures, to ensure that they remain effective, noting that what has worked in the past may not be effective in the current circumstances;
- Determining how to secure reliable and relevant information from their organization; and
- Paying attention to capital maintenance, in particular ensuring sufficient reserves for payment of dividends exist at the time the dividend is paid (not just proposed).

The guidance notes that investors are seeking key information on liquidity, viability and solvency of companies and that companies must articulate their expectations of possible impacts on their specific business. They provide guidance on likely reporting issues companies are facing now, reiterating that disclosure must be specific to the entity, including:

- Viability Statement. The FRC notes that fuller disclosure is paramount, and gives some specific guidance for companies in describing the assumptions and qualifications, limits of predictions and level of confidence underlying their statement that they have a "reasonable expectation" that the company will be able to continue in operation and meet its liabilities as they fall due over a period of assessment.
- Going Concern and Material Uncertainties. IAS 1 requires financial statements to be prepared on a going concern basis unless management either intends to liquidate the entity or to cease trading or has no realistic alternative but to do so. The FRC thinks it is likely that more companies will disclose "material uncertainties" to going concern in current circumstances, and gives guidance for considering and disclosing the uncertainty and likely success of any realistically possible mitigating actions.
- Significant Judgments and Estimation Uncertainty. Companies must disclose significant judgments, including those made in applying accounting policies. Companies are encouraged to provide as much context as possible, and note that relevant judgments and assumptions may include (i) availability and extent of government support measures, (ii)

availability, extent and timing of sources of cash and (iii) duration of social distancing measures and their impacts. The FRC recognises that the assumptions of companies on COVID-related matters will likely be different, and therefore stresses the need for full disclosure.

- Events After the Reporting Date. There is a general consensus that the outbreak of COVID-19 in 2020 was a condition that arose after the balance sheet date (a non-adjusting event) for the vast majority of UK companies preparing financial statements for periods ended 31 December 2019. For subsequent reporting dates this will be highly dependent on the reporting date, the specific circumstances of the company's operations and the particular events under consideration
- Guidance for Auditors. The FRC has issued guidance to auditors including a non-exhaustive list of factors to be considered in carrying out audit engagements in the current circumstances, including guidance on how they may be addressed. It will issue additional guidance as the situation progresses, and will withdraw the guidance when circumstances return to normal. The guidance reiterates the fundamental importance of high quality, independently assured information, and that in order to be able to give an audit opinion that is not subject to a disclaimer or qualification due to a scope limitation, the auditor must always obtain sufficient, appropriate audit evidence.
- Replacement of Auditors and Audit Partners. In the current climate, companies are encouraged to consider delaying planned tenders for new auditors, including by applying the FRC to extend the mandate when mandatory rotation is due). In addition, while key audit partners are required to rotate every 5 years, where there are good reasons, for example to maintain audit quality in current circumstances, the rotation can be extended to no more than 7 years. This needs to be agreed with the audit committee of any affected entity and does not need to be cleared with or approved by the FRC.
- Reduction of FRC demands on companies and audit firms. The FRC will, where possible, delay or extend the deadlines for consultations; it has paused for at least one month writing new letters to companies following its review of their annual reports and accounts; it is considering how it can adjust its audit quality review work to reduce demands on audit firms; and it will pause for at least one month requests to firms on supervisory initiatives, such as operational separation of audit practices.

UK Taxation Measures

A number of important tax measures form part of the UK Government's program to deal with the economic impact of the COVID-19 pandemic.

As regards UK VAT, quarterly VAT payments will be deferred for all UK businesses from 20 March 2020 until 30 June 2020. This is an automatic offer made by the Government to all UK businesses, with no applications required to the UK tax authorities. Furthermore, the Government has announced that taxpayers will be given until 31 March 2021 to pay any liabilities that accumulate during the deferral period. VAT refunds and reclaims will, however, be paid by the Government as normal during the deferral period.

Payments of income tax, due from self-employed individuals on the 31 July 2020, can be deferred until 31 January 2021. This is another automatic offer made by the UK Government, with no need for self-employed individuals to apply to benefit from the income tax deferral. No penalties or interest for late payment will be charged on any income tax deferred until January 2021.

The UK Government has not yet announced any changes to the payment schedules for corporation tax applicable to UK companies.

Other tax-related stimulation measures might follow, however, in the short term, as have been seen in a number of other jurisdictions.

* * *

If you have any questions, please feel free to contact any of the following Cadwalader attorneys.

Michael Sholem	+44 (0) 20 7170 8545	michael.sholem@cwt.com
David Quirolo	+44 (0) 20 7170 8635	david.quirolo@cwt.com
Adam Blakemore	+44 (0) 20 7170 8697	adam.blakemore@cwt.com
Joanna Valentine	+44 (0) 20 7170 8640	joanna.valentine@cwt.com
Oliver Bond	+44 (0) 20 7170 8544	oliver.bond@cwt.com