

Clients & Friends Memo

COVID-19 Update: Prudential Regulatory Treatment of UK Business Interruption Loan Schemes (CBILS & CLBILS)

1 May 2020

On 27 April 2020, the UK Prudential Regulation Authority (“**PRA**”) published a statement (the “**statement**”) on whether the guarantees provided by the UK Government (through the British Business Bank) under the Coronavirus Business Interruption Loan Scheme (“**CBILS**”) and the Coronavirus Large Business Interruption Loan Scheme (“**CLBILS**”) are eligible for recognition as unfunded credit risk mitigation (“**CRM**”) under the EU Capital Requirements Regulation (the “**CRR**”). The CRR continues to apply in the UK until the end of the Brexit transition period (currently scheduled to end on 31 December 2020).

Unfunded Credit Protection Under the Capital Requirements Regulation

A guarantee is one form of unfunded credit protection which, where it meets the conditions in Articles 194 and 213-215 CRR, may allow a firm to adjust risk weights and expected loss amounts. The statement reminds firms that they should review relevant articles of the CRR, and any relevant PRA rules and guidance (including expectations set out in the PRA’s Supervisory Statement on credit risk mitigation – SS17/13 ‘Credit risk mitigation’), when determining the risk weighted exposure amounts, and seek independent advice where necessary.

The PRA considers that the terms of the guarantees provided by the Government under CBILS and CLBILS do not contain features that would render these guarantees ineligible for recognition as unfunded credit risk protection, and the effects of these guarantees would appear to justify such treatment under the relevant provisions of the CRR. The statement also notes that some of the CBILS guarantees exclude cover for interest and fees. In accordance with the CRR, the PRA considers that firms recognising the CBILS guarantees as eligible unfunded protection in relation to an exposure are required to adjust the exposure amount to exclude elements not covered by the CBILS guarantees.

Additional Guidance on Loan Underwriting

The statement also provides some limited extra guidance for firms on their loan underwriting processes during the COVID-19 pandemic. The PRA recognises that it will be challenging for many businesses to provide forecast financial information with a high degree of confidence to

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support firms' loan underwriting processes. When lenders are making a credit decision, the statement reminds them that they should consider the full range of information available to them including (but not limited to):

- the performance of the proposed borrower business prior to the COVID-19 outbreak;
- a view of how the loan will be repaid in due course, relying on judgement in the absence of financial forecast information; and
- the general prospects for the sector in which the business operates once the effects of the pandemic have receded.

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