

BANKING BRIEFING: Special Edition - Vol.3

## Latest Developments in Banking Sector: Urgent Measures Relating to the Covid-19 Pandemic

This Briefing provides an overview of Covid-19 pandemic emergency measures relating to the Banking Sector

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- A. EBA Guidance on the Application of Prudential and Supervisory Measures with a View to Addressing and Mitigating the Adverse Systemic Economic Impact of Covid-19 on the EU Banking Sector**

- 1. EBA Statement on the application of the prudential framework on targeted aspects in the area of market risk in the Covid-19 outbreak**

On 22 April 2020, the European Banking Authority (EBA) [provided clarifications](#) on a number of aspects of the prudential framework in the area of market risk and proposed amendments to

Delegated Regulation (EU) No 101/2016 on prudent valuation. In particular, EBA:

- a. proposed an amendment of its standards on prudent valuation by introduction of the use of a 66% aggregation factor under the core approach;
- b. announced its intention to delay reporting for the first FRTB-SA figures to September 2021 and to allow a deferral of the final implementation phases of the margin requirements for non-centrally cleared derivatives; and
- c. recognised that the review of the SVaR observation period, under Article 365(2) CRR, could be postponed to the end of 2020 and should not constitute a supervisory priority at the moment.

- 2. EBA Statement on additional supervisory measures in the Covid-19 pandemic**

On 22 April 2020, [EBA provided further explanation](#) on the proposed supervisory approaches in relation to the Supervisory review and Evaluation Process (SREP), recovery planning, digital operational resilience and the application of the Guidelines on payment moratoria to securitisations. In particular, EBA:

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- a. recognised the need for a pragmatic approach to SREP assessments in 2020, focusing on the most material risks and vulnerabilities driven by the crisis;
- b. urged institutions, with regard to recovery planning activities, to maintain a strong focus on effective crisis management and preparedness, to focus on understanding which recovery options are necessary and available under the current conditions, to review regularly and on an ad hoc basis their recovery plans and to keep the competent authorities updated in this respect, at the same time providing for level of operational relief for institutions in 2020;
- c. emphasised the importance of digital operational resilience by calling institutions to ensure business continuity, adequate ICT capacity and security risk management; and
- d. further clarified the prudential application of the definition of default and forbearance and the application of EBA Guidelines on legislative and non-legislative moratoria on loan repayments to securitisation.

### 3. EBA final draft RTS on prudent valuation under Article 105(14) CRR

On 22 April 2020, EBA published the [final amending Regulatory Technical Standards \(RTS\) on prudent valuation under Article 105\(14\) CRR](#).

In particular, EBA:

- a. introduced the use of a 66% aggregation factor to be applied until 31 December 2020 under the core approach, to mitigate the impact of volatility triggered by the Covid-19 pandemic on the prudential requirements for market risk; and
- b. requested the granting of a mandate for the EBA to specify the provisions to be applicable for prudent valuation purposes under exceptional circumstances, similar to the powers granted under Article 325az(5) CRR.

### 4. EBA new draft RTS on bilateral margin requirements under Article 11(15) EMIR

On 4 May 2020, EBA issued a [new draft RTS on the risk mitigation techniques for OTC derivative](#)

[contracts not cleared by a CCP \(bilateral margining\), as per Article 11\(15\) EMIR](#), taking into account the international framework agreed by the Basel Committee on Banking Supervision (BCBS) and the International Organisation of Securities Commissions (IOSCO). The proposed amendments include:

- a. the extension by one year of the final implementation deadline for the margin requirements for both counterparties above the €50bn threshold (due to start September 2020) and above the €8bn threshold (due to start September 2021);
- b. the permanent exemption of both physically settled FX forwards and swaps with respect to certain contracts entered into between institutions and end-users;
- c. the extension by one year of the current deferred application of the margin requirements for single-stock equity options or index options transactions in the EU framework; and
- c. the extension of the deferred date of application of the bilateral margin requirements relating to intragroup transactions with a third country entity in the absence of an equivalence decision of the European Commission pursuant to Article 13(2) EMIR until 21 December 2020.

### 5. EBA Guidelines on reporting and disclosure of exposures subject to measures applied in response to the Covid-19 crisis

On 2 June 2020, EBA has issued [Guidelines on additional reporting and disclosure requirements regarding exposures of the credit institutions subject to measures applied in response to the Covid-19 crisis](#), such as legislative moratoria introduced by the member-states on loan repayments granting the borrowers various forms of payment holidays on their existing loans or various forms of public guarantees applying to new lending. These guidelines cover the reporting and disclosure requirements on:

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- a. the use of payment moratoria and the evolution of the credit quality of the exposures subject to such moratoria;
- b. the new loans subject to specific public guarantees set up to mitigate the effects of the Covid-19 crisis; and
- c. other forbearance measures applied in response to the Covid-19 crisis.

Such reporting should be performed on a quarterly basis, with the first reference date being 30 June 2020 and for an expected period of 18 months.

To facilitate reporting on the basis of these guidelines and reduce the operational costs for institutions and competent authorities, the EBA intends to provide a relevant technical package and to fully integrate the new reporting into the EBA reporting framework, as well as to link the technical release of the new reporting requirements with the existing planned release (expected in June 2020).

## **B. ECB Temporary Measures to Mitigate the Impact of Covid-19**

### **1. Extension of the timeline for review of ECB's monetary policy strategy**

On 2 April 2020, the Governing Council of the European Central Bank (ECB) has decided to [extend the timeline for the review of its monetary policy strategy](#) from the end of 2020 to mid-2021. ECB decided to postpone:

- a. the listening events of the ECB and the Eurosystem's national central banks to the second half of 2020; and
- b. the annual ECB Forum on Central Banking to 10-12 November 2020.

### **2. ECB package of temporary collateral easing measures**

On 7 April 2020, ECB adopted [a package of temporary collateral easing measures](#) to facilitate the availability of eligible collateral for Eurosystem counterparties to participate in liquidity providing operations. In particular, ECB decided the following:

- a. the implementation of a set of collateral measures, including the expansion of the use of credit claims as collateral, through the expansion of the Additional Credit Claims (ACC) frameworks, in order to facilitate an increase in bank funding against loans to corporates and households, and for this purpose decided to:
  - i. accommodate the requirements on guarantees to include government and public sector guaranteed loans to corporates, SMEs and self-employed individuals and households in the ACC frameworks in order to also provide liquidity against loans benefiting from the new guarantee schemes adopted in euro area member-states as a response to Covid-19;
  - ii. enlarge the scope of acceptable credit assessment systems used in the ACC frameworks; and
  - iii. reduce the ACC loan level reporting requirements to allow counterparties to benefit from the ACC frameworks even before the necessary reporting infrastructure is put in place;
- b. the adoption of a series of temporary measures, including:
  - i. lowering the level of the non-uniform minimum size threshold for domestic credit claims from €25,000 to €0, to facilitate the mobilisation as collateral of loans from small corporate entities;
  - ii. increasing, from 2.5% to 10%, the maximum share of unsecured debt instruments issued by any single other banking group in a credit institution's collateral pool; and
  - iii. waiving the minimum credit quality requirement for marketable debt instruments issued by the Hellenic Republic for acceptance as collateral in Eurosystem credit operations;
- c. the temporary increase of its risk tolerance level in credit operations through a general

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reduction of collateral valuation haircuts by a fixed factor of 20%; and

- d. an adjustment of the haircuts applied to non-marketable assets, both in the general collateral and the ACC frameworks, additional to the temporary haircut reduction, by fine-tuning some of the haircut parameters, which leads on average to a further haircut reduction of this type of collateral by around 20%.

The above measures will apply until September 2021.

### 3. Extension of deadlines for the reporting of statistical information

By virtue of [Regulation \(EU\) 2020/533 of the European Central Bank of 15 April 2020 on the extension of deadlines for the reporting of statistical information \(ECB/2020/23\)](#), the Governing Council of the ECB delegated to the Executive Board the power to extend the deadlines for reporting of statistical information required pursuant to Regulations 1409/2013 on payments statistics, 2018/231 on statistical reporting requirements for pension funds and 1374/2014 on statistical reporting requirements for insurance corporations. Such extension may only relate to reporting that falls due on or before 31 December 2020 and the relevant deadlines may not be extended beyond 30 June 2021.

The above measures on the collection of statistical information [were communicated by the ECB](#) to the national central banks and reporting agents.

### 4. ECB Banking Supervision temporary relief for capital requirements for market risk

On 16 April 2020, ECB announced a [temporary reduction in capital requirements for market risk](#) by allowing banks to adjust the supervisory component of these requirements.

In particular, ECB is temporarily reducing the qualitative market risk multiplier set by supervisors and used to compensate for the possible underestimation by banks of their capital requirements for market risk, as compensation to

the currently observed increases of the quantitative multiplier due to the market volatility being higher than predicted by the bank's internal model.

### 5. ECB temporary measures to mitigate impact of possible rating downgrades on collateral availability

On 22 April 2020, ECB [adopted temporary measures to mitigate the effect on collateral availability of possible rating downgrades](#) resulting from the economic fallout due to the Covid-19 pandemic, by grandfathering the eligibility of marketable assets and the issuers of such assets that fulfilled minimum credit quality requirements on 7 April 2020 in the event of deterioration in credit ratings, as long as such ratings remain above a certain credit quality level. In particular:

- a. marketable assets and their issuers that met the minimum credit quality requirements for collateral eligibility on 7 April 2020 will continue to be eligible in case of rating downgrades, as long as their rating remains at or above credit quality step (CQS)5 on the Eurosystem harmonised rating scale;
- b. the assets need to continue to fulfil all other existing collateral eligibility criteria, in order for them to be grandfathered;
- c. future issuances from grandfathered issuers will also be eligible provided they fulfil all other collateral eligibility criteria;
- d. currently eligible covered bond programs will also be grandfathered, under the same conditions;
- e. currently eligible ABSs to which a rating threshold in the general framework of CQS2 applies will be grandfathered as long as their rating remains at or above CQS4; and
- f. assets that fall below the minimum credit quality requirements will be subject to haircuts based on their actual ratings.

Non-marketable assets are not part of the scope of the above temporary grandfathering.

The above measures will apply until September 2021, when the first early repayment of the third

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series of targeted longer-term refinancing operations (TLTRO-III) takes place.

## 6. ECB recalibration of targeted lending operations

On 30 April 2020, ECB decided on a number of [modifications to the terms and conditions of its targeted longer-term refinancing operations \(TLTRO III\)](#) by amending Decision ECB/2019/21, in order to support further the provision of credit to households and firms. In particular, the following modifications will apply:

- a. for the period between 24 June 2020 and 23 June 2021:
  - i. the interest rate on all TLTRO III operations will be 50 basis points below the average rate applied in the Eurosystem's main refinancing operations over the same period (currently 0%); and
  - ii. the interest rate for counterparties whose eligible net lending reaches the lending performance threshold on all TLTRO III operations will be 50 basis points below the average interest rate on the deposit facility prevailing over the same period (currently -0.5%), and in any case not higher than -1%;
- b. the start of the period over which banks' lending performance will be assessed in order to ascertain whether they qualify for this lower rate is brought forward to 1 March 2020, while the end of the assessment period remains unchanged at 31 March 2021;
- c. for banks that reach the lending threshold of 0% between 1 March 2020 and 31 March 2021, the most favourable conditions will apply throughout the entire life of the operations and the interest rate applied before 24 June 2020 and after 23 June 2021 will be the average interest rate on the deposit facility over the life of the respective operation; and
- d. for banks that do not reach such lending threshold, the original TLTRO III interest rates and lending threshold, evaluated over the period of between 1 April 2019 and 31 March 2021, will apply and the lending threshold that they need to meet over this longer

assessment period will be lowered from 2.5% to 1.15%.

## 7. ECB pandemic emergency longer-term refinancing operations (PELTROs)

On 30 April 2020, ECB implemented a series of [non-targeted pandemic emergency longer-term refinancing operations \(PELTROs\)](#), consisting of seven additional refinancing operations commencing in May 2020 and maturing in a staggered sequence between July and September 2021 in line with the duration of the collateral easing measures, while counterparties participating in PELTROs will be able to benefit in parallel from the collateral easing measures in place.

The PELTROs will be conducted as fixed rate tender procedures with full allotment and at highly accommodative terms. The interest rate will be 25 basis points below the average rate applied in the Eurosystem's main refinancing operations (currently 0%) over the life of the respective PELTRO.

The operations provide longer-term funding to counterparties with decreasing tenors, starting with a tenor of 16 months in the first operation and ending with a tenor of 8 months in the last operation.

## 8. ECB monetary policy decisions

On 30 April 2020, the Governing Council of the ECB reached *inter alia* the following [monetary policy decisions](#):

- a. to continue to conduct purchases under the pandemic emergency purchase program (PEPP) in a flexible manner over time, across asset classes and among jurisdictions, until the Covid-19 crisis phase is over, but in any case until the end of this year;
- b. to continue to conduct net purchases under the APP at a monthly pace of €20bn, together with the purchases under the additional €120bn temporary envelope, for as long as necessary to reinforce the accommodative impact of its policy rates, and to end shortly before it starts raising the key ECB interest



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rates, and in any case until the end of the year;

- c. to continue reinvestments of the principal payments from maturing securities purchased under the APP for an extended period of time past the date when the Governing Council starts raising the key ECB interest rates, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation; and
- d. to keep unchanged the interest rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility at 0.00%, 0.25% and -0.50% respectively, until the inflation outlook convergence reaches a level sufficiently close to, but below, 2% and such convergence is consistently reflected in underlying inflation dynamics.

On 4 June 2020, ECB further took the following [monetary policy decisions](#):

- a. to increase by €600bn the envelope for the PEPP to a total of €1,350bn, as a response to the pandemic-related downward revision to inflation over the projection horizon;
- b. to extend the horizon for net purchases under the PEPP until the Covid-19 crisis phase is over and at least until the end of June 2021; and
- c. to reinvest the maturing principal payments from securities purchased under the PEPP until at least the end of 2022.

## C. ESRB Set of Actions to Address the Covid-19 Emergency

On 6 May 2020, the General Board of the European Systemic Risk Board (ESRB) discussed a [first set of actions in five priority areas](#) identified to address the impact of the Covid-19 emergency on the financial system from a macroprudential perspective. In particular, ESRB:

- a. endorsed the measures implemented so far by member-states in order to support the real economy and to protect household incomes, and intends to set-up a framework for monitoring the

macroprudential implications of such measures for the financial system focusing on the cross-border and EU levels;

- b. adopted a Recommendation to ESMA to coordinate with the national competent authorities in undertaking a focused piece of supervisory engagement with investment funds that have significant exposures to corporate debt and real estate assets, in order to assess the current state of preparedness thereof to potential future redemption pressures, further declines in market liquidity or increased valuation uncertainty;
- c. highlighted the importance to ensure, from the macroprudential perspective, that impact of large-scale downgrades of corporate bonds on markets and entities across the financial system are well understood and do not impair the functioning of financial markets so that the negative effects on the real economy are minimised;
- d. supported the actions taken so far to restrain dividend payments, share buybacks and other pay-outs and stressed the value of applying such restrictions on a system-wide basis; and
- e. regarding the liquidity risks arising from margin calls, stressed the importance of mitigating procyclicality that could be linked to the provision of clearing services and to the exchange of margins in bilaterally cleared markets, enhancing central counterparty stress test scenarios for the assessment of liquidity needs and limiting excessive liquidity constraints related to margin collection.

## D. European Commission Banking Package to Facilitate Lending to Households and Businesses in the EU

On 28 April 2020, the European Commission proposed a series of targeted [amendments to CRR](#) in order to maximise the ability of banks to lend and absorb losses related to Covid-19, in order to alleviate the immediate impact of Covid-19-related developments, in particular by:

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- a. adapting the timeline of the application of international accounting standards on banks' capital;
- b. treating more favourably public guarantees granted during the Covid-19 crisis;
- c. postponing the date of application of the leverage ratio buffer;
- d. modifying the way of excluding certain exposures from the calculation of the leverage ratio; and
- e. advancing the date of application of several agreed measures that incentivise banks to finance employees, SMEs and infrastructure projects.

The European Commission, further, issued the [Commission Interpretative Communication on the application of the accounting and prudential frameworks to facilitate EU bank lending](#) towards businesses and households amid Covid-19.

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