



7 April 2020

**Dear CEO**

**Covid-19 update to firms – Expectations and Regulatory measures**

We are all facing an unprecedented set of circumstances as a result of the Covid-19 pandemic. We have been working closely with firms in these challenging times and will continue to do so. The GFSC has been closely following the regulatory developments issued by the European Banking Authority (EBA) and the European Securities and Markets Authority (ESMA) in light of the current economic situation. The measures communicated to date, and the additional measures set out below allow firms to concentrate their efforts on responding to the crisis and the consumers they serve.

One of our main expectations, is that firms must provide strong support and service to customers during this period. Firms should be clear and transparent and provide support as consumers and businesses face challenges at this time.

We also expect firms to manage their financial resilience and actively manage their liquidity. Firms should report to us immediately if they believe they will be in difficulty. We want to support firms operating in this environment.

A summary is set out below of our expectations and approach to a number of issues in order to assist firms, and ensure that where there is flexibility embedded in the regulatory frameworks we are able to consider how best to apply this to firms. More detail on each of the items can be found in Annex 1.

- We urge all banks to refrain from dividend distributions during 2020, in order to maintain robust capitalisation. Additionally, banks are asked to review their variable remuneration policies to ensure these are set at a conservative level.
  - Banks should note that in the case where a payment holiday is granted to a customer as a result of the measures being offered to support personal and business customers because of the Covid-19 lockdown, there should not be an automatic reclassification to default, forborne or in the IFRS9 status.
  - In line with the EBA recommendation, the GFSC will be granting a one month extension for the submission of some of the regulatory reporting originally due on 12 May 2020 to 12 June 2020. The Pillar 3 disclosure deadline is also extended in line with the reporting for Audited Financial Statements by two months to 30 June 2020.
  - We are providing some supervisory flexibility over the 10% depreciation notifications in portfolio and leveraged instruments values, provided that the criteria set out in Annex 1 is met.
  - We remind firms of their core obligations to achieve best execution for clients and to ensure fair order handling and allocations during current market volatility. In respect of the best execution
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# GIBRALTAR FINANCIAL SERVICES COMMISSION

PO Box 940, Suite 3, Ground Floor, Atlantic Suites, Europort Avenue, Gibraltar. [www.gfsc.gi](http://www.gfsc.gi) [Twitter@gibfsc](https://twitter.com/gibfsc)

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requirements, we are providing some supervisory flexibility over the RTS28<sup>1</sup> and Article 65(6)<sup>23</sup> reports which are due to be published by firms by 30 April 2020, provided that the criteria set out in Annex 1 is met.

We want to continue working with firms to understand how the impact of the pandemic is affecting them and the harm and challenges that consumers may face. We will keep the above measures under review especially as new issues arise.

We welcome the continuing open engagement we have had with firms on these matters.

Yours faithfully

Kerry Blight

Chief Executive Officer

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<sup>1</sup> Commission Delegated Regulation (EU) 2017/576 of 8 June 2016 supplementing the Financial Services (Markets in Financial Instruments) Act 2006 (Amendment) Regulations 2017 "MiFID II"

<sup>2</sup> Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing the Financial Services (Markets in Financial Instruments) Act

<sup>3</sup> (Amendment) Regulations 2017 "MiFID II"

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## **Annex 1**

### **Dividend distributions and remuneration**

Banks need to ensure that they maintain a sound capital base to ensure they are able to provide the needed support to the economy.

Following a communication from the EBA, we urge all banks to refrain from dividend distributions, in order to maintain robust capitalisation. This is not only in relation to dividend payments in 2020 but any remaining dividend distributions from 2019.

Banks are also asked to review their remuneration policies and practices. Remuneration, particularly the variable part (bonus payments and commissions) should be set at a conservative level; and a larger part deferred for a longer period to ensure appropriate alignment with the risks arising from the Covid-19 pandemic.

### **Classification of loans - Default, Forbearance and accounting treatment**

The EBA has now provided some clarity on a number of aspects of the prudential framework, to ensure a consistent approach to (i) the classification of loans in default, (ii) the identification of forbore exposures, and (iii) the accounting treatment to be applied.

The main principle behind the accounting treatment, identification of forbore exposures and the definition of default in the prudential framework is to ensure a sound identification of credit impaired assets on bank balance sheets.

Having said this, we understand that the operational capabilities of banks in making in-depth assessments may be limited under the current circumstances. Given the nature of the present shock, which may also have medium and longer-term implications, the flexibility embedded in the accounting and regulatory frameworks is to be fully utilised by banks. This will help to maintain soundness through the crisis and provide critical functions to the economy.

Banks should note that in the case where a payment holiday is granted to a customer as a result of the measures being offered to support personal and business customers because of the Covid-19 lockdown, there should not be an automatic reclassification to default, forbore or in the IFRS9 status.

Nevertheless, please note that it is important for banks to continue to adequately risk assess the client's ability to repay any credit facility. The starting point should be the customer's standing with the bank prior to this current situation, and whether the bank assesses the customer's future ability to pay as positive.

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## Prudential identification of default:

The prudential identification of default includes a number of mitigating factors to ensure that classification of default is considered where economic losses are likely to be taken. The current economic measures and debt payment moratoria need to be considered when assessing the mitigating factors provided for in the legislation.

In terms of past due criteria, defaults do not have to happen until 90 days past due on material credit obligations, providing sufficient time to restructure the loans where necessary. The EBA has announced that it will be providing further criteria and when this is published we will consider its content. In the meantime the following should be considered:

- Where loans can be renegotiated in a way that the financial position of the lender does not diminish, as the obligor remains likely to meet its obligations under the renegotiated contract, there is no need to classify the exposure as defaulted. Additionally, this type of restructuring should not be considered as distressed restructuring. On the contrary it has to be considered a suitable measure to give relief to borrowers, which are temporarily not able to serve their loan obligations due to COVID19 disruptions.
- In the case of payment moratoria permitting suspension or delay in payments, this impacts the 90 days past due criterion, as the delays are counted based on the modified schedule of payments. Where institutions assess that there are no concerns in regards to the obligors' ability to make future payments, the exposure may remain in performing status.

## Classification of forbearance:

In the current circumstances, the measures that governments and credit institutions are proposing to address the adverse systemic economic impact of the Covid-19 pandemic would not automatically lead to a reclassification under the definition of forbearance.

## IFRS9:

When applying the IFRS9 international accounting standard, firms are expected to use a certain degree of judgement and distinguish between borrowers whose credit standing would not be significantly affected by the current situation in the long term, and those customers who would be unlikely to restore their creditworthiness post the current environment.

## Consumer protection:

Whilst ensuring flexibility on the prudential side to support generalised payment delays, there is no flexibility in relation to consumer protection. We call on all lenders to act in the interest of consumers. In particular making sure that customers fully understand the implications of taking up any measures, without hidden charges.

We reminds banks to grant such measures in compliance with existing legislation, such as the Financial

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Services (Mortgage Credit) Regulations 2020 and the Financial Services (Consumer Credit) Act 2011 (Amendment) Regulations 2013, in particular, the importance of full information disclosure, especially of any potential charges and costs, and the transparency and clarity of terms and conditions.

### **Regulatory Reporting and Pillar 3 disclosures**

The GFSC has also considered the recommendations set out in the EBA's 'Statement on supervisory reporting and Pillar 3 disclosures in light of COVID-19', published on 31 March 2020. The GFSC will accept delayed submission for the following regulatory reporting, where the original deadlines fall on or before 31 May 2020.

For many reports, the original submission date is 12 May 2020. In applying the extension below for example, the GFSC will accept submission on or before 12 June 2020 for the following reporting:

- COREP Solvency
- Liquidity – Stable Funding
- Large exposures and concentration risk
- Leverage ratio
- Asset encumbrance
- Quarterly GFSC Supervisory Return

The submission dates for the following information will continue as set out in the Invoke calendar i.e. monthly – by the 15<sup>th</sup> day post month end:

- Information on liquidity coverage ratio, and
- the Additional Liquidity Monitoring Metrics;

Firms are able to submit at any time from the original submission period up to the end of the delayed submission window as set out above. Where reporting submissions are comparatively well-progressed, the GFSC encourages firms to submit them earlier in the windows to the extent possible.

The GFSC has also considered the EBA's recommendation that competent authorities are flexible in assessing compliance with deadlines for publication for the CRR<sup>4</sup> Pillar 3 disclosures. Article 433 CRR requires that firms publish these in conjunction with the financial statements. Therefore, as the deadline for publication of firm's financial statements has been delayed by up to two months, it follows that firm's Pillar 3 disclosures, which are published at the same time, will also be delayed compared to the usual publication date.

### **Additional Reporting**

Whilst we will do our best to keep requests to a minimum, to maintain the safety and soundness of authorised firms during this period, the GFSC may request the more frequent submission of particular reports and

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<sup>4</sup> Capital Requirements Regulation EU 575/2013

additional ad-hoc reporting on key prudential metrics. Firms affected will be advised directly by Supervisors if we require any additional information. At present we do not expect to require any particular reports, but this may change going forward, subject to how matters develop and the length of time the crisis continues.

### **Post 31 May 2020 reporting submissions**

We will continue to monitor the situation and consider in due course whether the above actions need to be extended to reporting due after the 31 May 2020.

### **Supervisory flexibility over 10% depreciation notifications<sup>5</sup> until the end of September**

Firms providing portfolio management services are required to inform clients where the overall value of the portfolio falls by 10% or more compared with its value in the last periodic statement, and for each subsequent 10% fall in value.

Firms holding retail client accounts that include positions in leveraged financial instruments or contingent liability transactions, are required to inform clients where the initial value of each instrument depreciates by 10% and for each subsequent 10% fall in value.

Some firms have raised concerns about the impact on consumers and the operational burden of this requirement in the current highly volatile market.

Please note that we have no intention of taking enforcement action where a firm:

- has issued at least one notification to a retail clients within a current reporting period, indicating their portfolio/instrument has decreased in value by at least 10%; and
- subsequently provides general updates through its website, other public channels (such as social media) and/or generic, non-personalised client communications. These communications should update clients on market conditions, explain how clients can check their portfolio value and invite clients to contact the firm if they wish; or
- chooses to cease providing 10% depreciation reports for any professional clients

We will adopt this approach for a period of 6 months (to 1 October 2020).

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<sup>5</sup> Article 62 Commission Delegated Regulation (EU) 2017/565

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### **Supervisory flexibility over Best Execution until the end of June**

We remind firms of their core obligations to achieve best execution for clients and to ensure fair order handling and allocations during current market volatility. We would expect firms to consider the importance of the venues or brokers they rely upon to achieve best execution, and expect firms to manage risk during market volatility through the use of different types of orders.

We are aware of the obligations firms are facing to meet the requirements set out in RTS 28<sup>6</sup> and Article 65(6)<sup>7,8</sup> which has a reporting date of 30 April 2020 concerning the reporting period 2019.

The information published in accordance with RTS 28 and Article 65(6) is intended to provide the public and customers with the necessary details to evaluate the quality of a firm's execution practices by requiring the publication of valuable information about how and where the firm has executed client orders.

We are aware of the operational difficulties that firms may be facing at present in preparing these reports. ESMA has also recognised that as a result of the exceptional circumstances created by the Covid-19 outbreak, firms may need to deprioritise efforts for the publication of these general reports concerning 2019.

Please note that we have no intention of taking enforcement action where a firm:

- Does not publish its RTS 28 and Article 65(6) report by 30 April 2020, provided they are published by no later than 30 June.

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<sup>6</sup> Commission Delegated Regulation (EU) 2017/576 of 8 June 2016 supplementing the Financial Services (Markets in Financial Instruments) Act 2006 (Amendment) Regulations 2017 "MiFID II"

<sup>7</sup> Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing the Financial Services (Markets in Financial Instruments) Act

<sup>8</sup> (Amendment) Regulations 2017 "MiFID II"

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