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Relief and Rescue: Suspensions and Elasticity in Financial Regulation, and Lessons from the UK's Management of the COVID-19 Pandemic Crisis

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RELIEF AND RESCUE: SUSPENSIONS AND ELASTICITY IN FINANCIAL REGULATION, AND LESSONS FROM THE UK'S MANAGEMENT OF THE COVID-19 PANDEMIC CRISIS

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ABSTRACT

This Article analyzes the UK's approach to handling the economic impact of COVID-19, offering insight for developed financial jurisdictions embarking on regulatory suspensions. When existing law no longer meets overarching policy goals such as financial stability, regulators resort to the theorization of legal elasticity. This Article situates regulatory suspension within this theory analyzing the tensions, hazards, and accompanying decision-making frameworks. The authors make three proposals for deployment of legal elasticity by regulators: (1) evaluate institutional stability; (2) engage in relational paradigms with relevant agencies, entities, and stakeholders; and (3) establish *ex ante* frameworks for crisis management and the potential use of legal elasticity.

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INTRODUCTION

The outbreak of the COVID-19 pandemic severely impacted economic activity as lockdowns were imposed in many countries.[1] In the UK, economic impact has been severe, as output was reduced by more than 20% in April 2020 compared to the previous month.[2]

The financial implications of economic lockdown in multiple sectors were immediate as the corporate sector is heavily financialized.[3] The freezing of business activity has implications for business' cash flow, servicing of debt, potential insolvency and their market valuation and credit rating assessments. Further, the decline of market appetite triggers investors' behavioural bias towards cash (using Lo's adaptive capital markets hypothesis),[4] and adversely affects levels of private investment in the corporate sector.[5] The economic woes for businesses and corporations are inevitably also financial woes. Besides public finance packages for emergency help, such as furloughing,[6] policymakers have turned to the private sector to alleviate the financial stresses and hardships caused to households and corporations. Private sector finance is being relied on to a significant extent to meet the policy goals of 'relief' and 'rescue' for households and corporations. 'Relief' refers to the policy goal of giving corporations and households temporary release from the pressures of debt which would be exacerbated in the weak economic conditions during the

1. Daniel Dunford et al., *Coronavirus: The World in Lockdown in Maps and Charts*, BBC NEWS (Apr. 7, 2020), https://www.bbc.co.uk/news/world-52103747 [https://perma.cc/XW5G-5RVY].

2. Richard Partington, *UK GDP Falls by Record 20.4% in April as Lockdown Paralyses Economy,* THE GUARDIAN June 12, 2020, 5:06 AM), https://www.theguardian.com/business/2020/jun/12/britains-gdp-falls-204-in-april-as-economy-is-paralysed-by-lockdown [https://perma.cc/ERV5-YE9F].

3. Karen Ho, *Corporate Nostalgia? Managerial Capitalism from a Contemporary Perspective*, *in* CORPS. & CITIZENSHIP 267 (Greg Urban ed., 2014).

4. Andrew W. Lo, *The Adaptive Markets Hypothesis: Market Efficiency from an Evolutionary Perspective,* 30 J. OF PORTFOLIO MGMT. 15 (2004).

5. Attracta Mooney & Peter Smith, *Investors Pull Record €250bn from European Funds*, FIN. TIMES (Apr. 22, 2020, 12:30 PM), https://www.ft.com/content/29d69ff6-749b-45dc-b53e-85a236186983 [https://perma.cc/V4LB-EBAG] (last visited Aug. 19, 2020); David Ricketts, *UK IFlee Equity Funds on Coronavirus Fears*, FIN. NEWS (Feb. 27, 2020, 12:01 AM), https://www.fnlondon.com/articles/uk-investors-flee-equity-funds-on-coronavirus-fears-20200227 (last visited Aug. 19, 2020).

6. HM Revenue & Customs, *Claim for Wages Through the Coronavirus Job Retention Scheme*, UK GOV'T (Sept. 16, 2020), https://www.gov.uk/guidance/claim-for-wages-through-the-coronavirus-job-retention-scheme (last visited Aug. 30, 2020).

pandemic. 'Rescue' refers to facilitating the access of corporations to essential finance to keep them afloat by to covering day-to day expenses, absorbing losses and shoring up capital for the future.

These policies are not dissimilar to those undertaken by many countries.[7] In the UK, which is the focus of the article, the policy goals of relief and rescue were carried out by the enactment of emergency legislation,[8] as well as by regulatory actions under the leadership of financial regulators, i.e. the Prudential Regulation Authority (PRA)[9] and Financial Conduct Authority (FCA).[10] The PRA and FCA suspended the application of certain regulatory laws and private contractual laws applicable to their regulated entities. Regulatory suspension can be seen as one of the ways the 'elasticity' of law is realized in order to cater for wider political, social and economic needs.[11]

In Pistor's legal theory of finance, legal elasticity is treated as a policy instrument to overhaul existing law[12] when overarching policy goals such as financial stability are undermined in extraordinary circumstances, such as a financial crisis, by the ordinary outworking of existing law.[13] Hence, legal elasticity can be implemented to produce structural effects, such as institutional dissonance and change.[14]

In this article, we situate the regulatory suspensions introduced by UK financial regulators during the COVID-19 crisis within the theorization of legal elasticity in Pistor's legal theory of finance. Further, our study, although focused on the UK, offers lessons and insights for developed financial jurisdictions that have also embarked financial regulatory suspensions.[15] We argue that regulatory suspensions should be perceived as

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7. *Policy Responses to COVID-19*, INT'L MONETARY FUND, https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19 [https://perma.cc/JH7K-MAD7].

8. Corporate Insolvency and Governance Act 2020, c. 12 (UK).

9. The prudential regulator oversees 1,500 banks, insurers and systemically important financial institutions. *See Prudential Regulation*, BANK OF ENG. (Sept. 2, 2020), https://www.bankofengland.co.uk/prudential-regulation [https://perma.cc/E3LA-ATF9].

10. The conduct regulator oversees all financial institutions in the UK, including the institutions overseen by the PRA, in respect to business conduct. *See About the FCA*, FIN. CONDUCT AUTH. (Sept. 2, 2020), https://www.fca.org.uk/about/the-fca [https://perma.cc/4CGG-A3X4].

11. Katharina Pistor, *A Legal Theory of Finance*, 41 J. OF COMP. ECON. 315 (2013).

12. *Id.* at 317.

13. *Id.*

14. *Id.* at 320, quoting Minsky (1986).

15. Many jurisdictions in Europe have introduced 'relief' measures like debt payment moratoria,

going beyond merely being instrumental. It is imperative to explore the nature of regulatory suspensions within the framework of legal elasticity as a fully theorized account so regulators can perceive more fully the implications of their deployment.

Section II explores the concept of legal elasticity as theorized in the wake of the global financial crisis of 2007–09. We argue that this concept can be extended to encompass regulatory suspensions introduced in the COVID-19 crisis, being equally applicable to regulatory suspensions triggered by endogenous financial sector problems or exogenous shocks. Legal elasticity has been deployed as the policy agenda of 'relief and rescue' which represent welfarist and public interest objectives which are not easily accommodated in financial regulation, due to the efficiency-dominated paradigm of financial regulation.[16]

However, in its application to credit laws and regulation examined in Section III, and capital markets regulation explored in Section IV, legal elasticity challenges the institutional coherence of regulatory regimes and this tension has resulted in a number of unanswered questions and unintended consequences. Sections III and IV examine the hazards such regulatory suspensions could entail to regulators, banks, markets and the intended beneficiaries themselves- i.e. households and corporations.

Section V argues that regulators' deployment of legal elasticity can be better supported by decision-making frameworks that are based on a fully theorized understanding of legal elasticity. We make three proposals for improving regulators' decision-making in deploying legal elasticity. This article does not argue that by more optimally deploying legal elasticity, substantive policy agendas such as 'relief and rescue' would also be optimal. What we argue is that whatever the substantive policies in place, where financial regulatory suspensions are regarded as part of the policy mosaic, the use of legal elasticity should be a fully apprised one and should not add to existing substantive challenges. This is important as for a second time, financial regulators in many jurisdictions have looked to legal

supported by prudential regulation suspensions. *See Our Response to Coronavirus (COVID-19)*, EUR. BANKING AUTH., https://eba.europa.eu/coronavirus [https://perma.cc/Q482-WX5J]. In the U.S., a relief measure with forbearance and moratoria was passed. *See* Coronavirus Aid, Relief, and Economic Security Act (CARES) Act, Pub. L. No. 116-136 (2020).

16. Zanna Iscenko et al., *Occasional Paper No. 13: Economics for Effective Regulation*, FIN. CONDUCT AUTH. (Sept. 2, 2016), https://www.fca.org.uk/publications/occasional-papers/occasional-paper-no-13-economics-effective-regulation [https://perma.cc/E6J2-AL6B].

elasticity at a significant scale for crisis management, even if this is not a financial sector originated crisis. However, we confine our proposals on the optimal use of legal elasticity in finance, as Section II explains how legal elasticity is anchored in the legal theory of finance. Other regulatory areas may not be susceptible to as much legal construction as in finance. We do not discount the possibility that other regulatory 'enterprises'[17] can benefit from this study, but we do not claim direct applicability within the confines of this article.

I. LEGAL ELASTICITY IN FINANCIAL REGULATION

Legal elasticity is argued to be a function of the legal theory of finance posited by Pistor.[18] The legal theory of finance frames finance in legal terms because financial transactions and obligations are constructed as legal structures in order to work as intended.[19] In particular, finance is underpinned by the crucial qualities of certainty and enforceability that law supplies. However, in the global financial crisis, it was observed that the qualities of certainty and strict enforceability of financial obligations and transactions in various markets would collectively lead to damaging consequences, a manifestation of systemic risk.[20] As such, the solution is also found in law. For example, by resorting to legal elasticity to suspend and mitigate the adverse impacts driven by law in order to meet the needs of crisis management.

In this theoretical framework, legal elasticity served an unwinding purpose—to unwind the adverse effects caused by its very own legal nature in the first place, when the broader policy goals sought to be achieved are shifted. Elasticity also redeems financial law or regulations and paves the way for law reform. The post-crisis reforms to the banking and financial sector reflected this conceptualization of legal elasticity. For example, where banks had been unable to absorb their losses during the global financial crisis, legal elasticity was applied so that regulatory discipline was

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17. This term refers to different regulatory areas warranting different approaches taken by relevant respective regulatory agencies. TONY PROSSER, THE REGULATORY ENTERPRISE: GOVERNMENT, REGULATION, AND LEGITIMACY 1–20 (2010).
18. Pistor, *supra* note 11, at 320.
19. *Id.* at 317–18.
20. Steven Schwarz, *Systemic Risk*, 97 GEO. L. J. 193 (2008).

not meted out to them for being inadequately capitalized.[21] Instead, many jurisdictions bailed out their banks by injecting state capital[22] and then proceeded to reform capital rules to tie banks to higher and more robust levels of capitalization.[23]

The application of legal elasticity by UK policymakers and regulators to credit and capital markets during the COVID-19 crisis seemed arguably not in the same vein, as regulatory suspensions were articulated to be temporary, as will be discussed in detail in Section III. This near-term perception of regulatory suspensions can be attributed to the sophisticated development of financial regulation after the crisis, which includes inherently flexible regulations.[24] Regulators constructed an increasingly prescriptive regime for prudence[25] and conduct[26] by banks and financial institutions—and also carved out particular measures of inherent flexibility.[27] This juristic development suggests that legal elasticity in finance may have been theoretically enriched by the provision of *ex ante*

21. Pistor, *supra* note 11. For example, the UK government bailed out stricken UK banks during the 2008 global financial crisis, injecting in equity capital to absorb the banks' losses during that time, *see* Graeme Wearden, *British government unveils £37bn banking bail-out plan*, GUARDIAN (Oct. 13, 2008), https://www.theguardian.com/business/2008/oct/13/marketturmoil-creditcrunch [https://perma.cc/6E2S-UJMB].

22. *Rescue Packages: What Governments Have Offered*, THE TELEGRAPH (Oct. 20, 2008, 3:47 PM), https://www.telegraph.co.uk/finance/3229434/Rescue-packages-what-governments-have-offered-financial-crisis.html [https://perma.cc/PC2B-BU5F].

23. BASEL COMMITTEE ON BANKING SUPERVISION, BASEL III: A GLOBAL REGULATORY FRAMEWORK FOR MORE RESILIENT BANKS AND BANKING SYSTEMS (June 2011), http://www.bis.org/publ/bcbs189.pdf [https://perma.cc/JAM9-CNG8]; BASEL COMMITTEE ON BANKING SUPERVISION, BASEL III: FINALISING POST-CRISIS REFORMS (Dec. 2017), https://www.bis.org/bcbs/publ/d424.pdf [https://perma.cc/CF8K-9ARG]. The European Union introduced additional rules in Directive 2013/36, of the European Parliament and of the Council of 26 June 2013 on Access to the Activity of Credit Institutions and the Prudential Supervision of Credit Institutions and Investment Firms, Amending Directive 2002/87/EC and Repealing Directives 2006/48/EC and 2006/49/EC; Regulation 575/2013 of the European Parliament and of the Council of 26 June 2013 on Prudential Requirements for Credit Institutions and Investment Firms and Amending Regulation 648/2012 (EU), Preamble 41.

24. "Embedded flexibility" was mentioned by the European Banking Authority. Press Release, European Banking Auth., Statement on Actions to Mitigate the Impact of COVID-19 on the EU Banking Sector (Mar. 12, 2020), https://eba.europa.eu/sites/default/documents/files/document_library/General%20Pages/Coronavirus/EBA%20Statement%20on%20Coronavirus.pdf [https://perma.cc/PQ7K-64Q5].

25. IRIS H-Y CHIU & JOANNA WILSON, BANKING LAW AND REGULATION 329–678 (2019); Iris H-Y Chiu, *Rethinking the Law and Economics of Post-Crisis Micro-Prudential Regulation: The Need to Invert the Relationship of Law to Economics?*, 38 REV. OF BANKING & FIN. L. 639 (2019).

26. CHIU & WILSON, *supra* note 25, at 52–54, 517–534.

27. *See infra* Section III.A for counter-cyclical buffer in microprudential regulation.

discretion and flexibility, and not just *ex post* discretion argued in Pistor's legal theory of finance.

However, we observe in Sections III and IV that during the COVID-19 crisis, regulators exhausted inherently flexible measures and moved to relax unexpected regulatory rules, in order to advance the policy demands of relief and rescue. These are framed to be bundled with the inherently flexible rules, arguably showing hesitation and ambivalence in deploying legal elasticity.[28] This *ex post* exercise of legal elasticity raises a new question: can legal elasticity take place within institutional stability? The post-crisis conceptualization of legal elasticity is structural in nature, and a pathway to institutional change. Is legal elasticity during the COVID-19 crisis temporary?

Figure 1: Spectrum of Regulatory Elasticity- A Hypothesis

This question is of importance, as regulators wish to avoid an application of legal elasticity whose effects then take them by surprise. However, our examinations in Sections III and IV suggest that signs of unintended *structural* effects are already occurring. Even if legal elasticity encompasses 'degrees' of elasticity, regulators should not assume that no institutional dissonance would result. In this manner, we may be able to add

28. *See infra* Sections III.B, IV.B, and IV.C.

to the conceptualization of legal elasticity in Pistor's legal theory of finance, in hypothesising the structural nature of legal elasticity, beyond merely instrumental. Such a spectrum of structural effects can be dependent on *legal* factors such as how far legal effects are suspended, and for how long, and *other* factors such as the nature of policy rhetoric in which regulatory suspensions are framed. These are issues that can be further explored empirically in future work.

It is fully understandable that the financial regulators in the UK wish to secure institutional consistency despite the application of legal elasticity. The post-crisis financial regulatory reforms have taken more than a decade,[29] and we would argue that regulators have no appetite for major institutional changes. Further, the COVID-19 crisis is regarded as a crisis exogenous to the financial sector and should not entail existential consequences for the substance of laws/regulations.

Our call to fuller theorization and appraisal of legal elasticity is not intended to 'create more work' for regulators during this stressful time. This exercise would do much to spare regulators from unexpected and longer-term challenges down the road. At a broader level, a fully theorized understanding of legal elasticity allows this regulatory tool to be used more optimally in crisis management. More general application of legal elasticity as a regulatory tool can also be theoretically anchored in responsive regulation.[30] Although Ayres' and Braithwaite's work in 'responsive regulation' was most famous for its enforcement pyramid, it more broadly redefined the nature and directions for modern regulation.[31] It provides a vision of regulatory dynamism for substantive purposes[32] and purposes

29. For Basel Committee's reforms between 2009-2019, *see Basel III: International Regulatory Framework for Banks*, BANK FOR INT'L SETTLEMENTS, https://www.bis.org/bcbs/basel3.htm [https://perma.cc/U3HY-26RD]; and for the EU's regulatory regime finalized in 2013, amended 2019, *see Implementing Basel III in Europe*, EUR. BANK AUTH., https://eba.europa.eu/regulation-and-policy/implementing-basel-iii-europe [https://perma.cc/AKH4-KPPN].

30. *See generally* IAN AYRES & JOHN BRAITHWAITE, RESPONSIVE REGULATION: TRANSCENDING THE DEREGULATION DEBATE (1992).

31. Christine Parker, *Twenty Years of Responsive Regulation: An Appreciation and Appraisal*, 7 REGUL. & GOVERNANCE 2 (2013).

32. *E.g.*, CRISTIE FORD, INNOVATION AND THE STATE: FINANCE, REGULATION AND JUSTICE 139–217 (2017) (discussion of regulatory aims to promote innovation).

relating to regulatory participation,[33] processes[34] and implementation.[35] Legal elasticity is more richly based if regarded as an extension of the responsive regulatory paradigm.

We turn to examine the use of regulatory suspensions in the credit and capital markets in the UK.

II. REGULATORY SUSPENSION IN CREDIT LAWS AND REGULATION: ADVANCING 'RELIEF AND RESCUE'

During the COVID-19 crisis in the UK, a key policy concern is how credit arrangements would affect households and corporations that are in debt and/or need additional financing by debt. First, borrowers, both households and corporations, need temporary relief from the pressures of debt while regrouping themselves during the crisis. Second, access to finance and credit to businesses should continue in order to avoid key social losses such as protecting jobs and business suppliers from knock-on effects.[36] In the US, personal finance forbearance is devolved to the private sector,[37] possibly with state regulatory guidance. Under the FCA consumer protection mandate,[38] measures on personal finance were introduced from the early stages of the pandemic. Relief for corporate borrowers is explicit in both the US[39] and UK.[40]

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33. *E.g.*, Julia Black, *Decentring Regulation: Understanding the Role of Regulation and Self-Regulation in a 'Post-Regulatory' World*, 54 CURRENT LEGAL PROBLEMS 103 (2001).

34. *E.g.*, Colin Scott, *Regulating Everything* (UCD Geary Inst., Working Paper No. 24, 2008) (discussion of meta-regulation).

35. *E.g.*, EXPLAINING COMPLIANCE: BUSINESS RESPONSES TO REGULATION (Christine Parker & Vibeke Lehmann Nielsen eds., 2011).

36. Thomas Huertas, *Here is How Banks Can Help Save the Economy*, FIN. TIMES (May 10, 2020, 2:00 PM), https://www.ft.com/content/f02df444-8f78-11ea-bc44-dbf6756c871a (last visited Aug. 19, 2020).

37. Matt Higginson et al., *What Next for US Credit Card Debt?*, MCKINSEY & CO. (May 13, 2020), https://www.mckinsey.com/industries/financial-services/our-insights/what-next-for-us-credit-card-debt# [https://perma.cc/B87E-RREF]. There seems to be some forbearance for student debt and mortgage debt that is underwritten by Fannie Mae and Freddie Mac. Susan Tompor, *Personal Finance Tips: How to Pay the Bills During the Coronavirus Pandemic*, USA TODAY (Mar. 23, 2020, 5:00 AM), https://www.usatoday.com/story/money/2020/03/23/mortgage-bills-student-loan-moratorium-COVID-19-coronavirus-personal-finance/2894392001/ [https://perma.cc/DD7F-H5P3].

38. Financial Services and Markets Act 2000, c.8, § 1C (UK).

39. CARES Act §§ 1102, 1105.

40. *See* Corporate Insolvency and Governance Act 2020, c. 12 (UK).

A. Relief for Borrowers

Explicit loan forbearance was introduced in the UK in March 2020 suspending the operation of contractual obligations for FCA-regulated lenders in consumer credit and household mortgages.[41] Because the FCA does not have regulatory perimeter over business lending, an Act of Parliament was passed to give temporary relief for business borrowers.[42]

Regulators require mortgage lenders to grant a payment holiday, originally for three months, but subsequently extended until the end of October, to any customer who indicates they will potentially experience difficulties.[43] In view of the UK's second lock-down between 3 November to 2 December 2020, the FCA has extended the period for deferral requests up to 31st January 2021 for any customer yet to make such a request.[44] This measure does not affect the accrual of interest on the loan and lenders need not investigate the individual circumstances of each customer who requests for the payment holiday.[45] The balance achieved is that customers are not burdened with proving that they can afford a payment holiday, but lenders are not asked to forego their expected earnings. If mortgage customers are already in default at the commencement of the FCA's guidance for payment deferral, they would enjoy temporary relief from enforcement against the debt.[46]

Other consumer credit customers enjoy similar relief in payment

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41. *See infra* notes 45–48.
42. *Id.*
43. *Mortgages and Coronavirus: Information for Consumers,* FIN. CONDUCT AUTH. (Aug. 26, 2020), https://www.fca.org.uk/consumers/mortgages-coronavirus-consumers [https://perma.cc/K923-4JRN].
44. Customers, however, cannot enjoy more than a 6-month period of deferment. See *FCA Confirms Support for Mortgage Borrowers Impacted by Coronavirus,* FIN. CONDUCT AUTH. (Nov. 17, 2020), https://www.fca.org.uk/news/press-releases/fca-confirms-support-mortgage-borrowers-impacted-coronavirus [https://perma.cc/LL5U-ME3B].
45. *Mortgages and Coronavirus: Updated Guidance for Firms,* FIN. CONDUCT AUTH. (Nov. 17, 2020), https://www.fca.org.uk/publications/finalised-guidance/mortgages-and-coronavirus-updated-guidance-firms, "There is no expectation under this guidance that the firm investigates the circumstances surrounding a request for a payment deferral before agreeing one for up to 3 months. Firms can choose to make the enquiries they consider necessary in order to offer an alternative to a payment deferral that is in the customer's best interests, provided this does not cause undue delay."
46. *Id.* "Firms should not commence or continue repossession proceedings against customers before 31 October 2020, given the unprecedented uncertainty and upheaval they face, and Government advice on social distancing and self-isolation. This applies irrespective of the stage that repossession proceedings have reached and to any step taken in pursuit of repossession. Where a possession order has already been obtained, firms should refrain from enforcing it."

holidays, including personal loans and credit cards. Consumers with an arranged overdraft can request an additional interest-free overdraft facility of £500 for a three-month period.[47] High-cost short-term credit customers,[48] motor finance, and 'buy-now-pay-later' or 'rent-to-own' borrowers also benefit from deferred payment requests, which were initially available until 31 October 2020,[49] but were extended up to 31 January 2020 in view of the UK's second lock-down.[50]

As business lending is not regulated by the FCA, fast-tracked legislation was passed to allow indebted companies to apply for a moratorium.[51] Directors can make such applications if they believe that the company is unable to pay its debts.[52] They need to appoint an insolvency practitioner as 'monitor' to verify that rescue for the company is possible.[53] A successful application for moratorium allows the company to enjoy relief, except from specified obligations such as rent and employees' wages, for an initial 20 days with a possible extension.[54] During the period of the moratorium, no insolvency proceedings can commence against the company.[55] The company should seek arrangements with its creditors or explore avenues of

47. *FCA Confirms Further Support for Consumer Credit Customers,* FIN. CONDUCT AUTH. (July 1, 2020), https://www.fca.org.uk/news/press-releases/fca-confirms-further-support-consumer-credit-customers [https://perma.cc/5N3F-MVZB].

48. *Coronavirus: Information for Consumers on Personal Loans, Credit Cards, Overdrafts, Motor Finance and Other Forms of Credit,* FIN. CONDUCT AUTH. (July 15, 2020), https://www.fca.org.uk/consumers/coronavirus-information-personal-loans-credit-cards-overdrafts [https://perma.cc/5N3F-MVZB]; *High-Cost Short-Term Credit and Coronavirus: Temporary Guidance for Firms,* FIN. CONDUCT AUTH. (Apr. 24, 2020), https://www.fca.org.uk/publications/finalised-guidance/high-cost-short-term-credit-and-coronavirus-temporary-guidance-firms [https://perma.cc/F5CE-BZM5]. This is updated in *High-Cost Short-Term Credit and Coronavirus: Updated Temporary Guidance for Firms*, FIN. CONDUCT AUTH. (July 3, 2020), https://www.fca.org.uk/publications/guidance-consultations/high-cost-short-term-credit-coronavirus-updated-temporary-guidance-firms [https://perma.cc/RM5M-7AT3].

49. *FCA Announces Proposals to Further Support Motor Finance and High Cost Credit Customers*, FIN. CONDUCT AUTH. (July 3, 2020), https://www.fca.org.uk/news/press-releases/fca-announces-proposals-further-support-motor-finance-high-cost-credit-customers [https://perma.cc/DJ92-JHA8].

50. FCA, *High-Cost Short-Term Credit and Coronavirus: Further Updated Temporary Guidance for Firms* (Nov. 2020), https://www.fca.org.uk/publication/guidance-consultation/hcstc-and-coronavirus-further-updated-temporary-guidance-for-firms-november-2020.pdf, at para. 2.8.

51. Corporate Insolvency and Governance Act 2020, c. 12, §§ 3, 6, 7 (UK).

52. *Id.* at §§ 3, 6, 7 (UK).

53. *Id.*

54. *Id.* §§ 9, 10, 18, 20, 21.

55. *Id.* at §§ 3, 6, 7.

raising finance during this period.[56]

In order to support loan forbearance, powers were exercised to relax the microprudential regulatory measure called the countercyclical buffer.[57] The macro-prudential regulator in the UK, the Bank of England's Financial Policy Committee (FPC), has oversight of the systemic health of the financial system,[58] and is able to exercise an inherently flexible power to adjust a prudential regulatory measure known as the countercyclical buffer (CCyb).[59] The CCyb was introduced in the wake of the global financial crisis to allow the macroprudential regulator to impose capital cost on banks to dampen pro-cyclical creation of debt.[60] Imposing the CCyb moderates financial institutions' behaviour and markets' tendencies towards a cycle of Minskian instability.[61] Prior to the onset of the COVID-19 crisis, the CCyb was set at 1% for UK banks to be elevated to 2% by December 2020, as economic activity looked strong and banks should be prevented from excessive risk-taking. This was abruptly adjusted to 0% during the COVID-19 crisis, freeing up for banks an estimated capital cost of £190bn.[62] As Masur and Posner[63] argue, the CCyb is designed to shape the incentives of financial actors inherently biased towards procyclicality. In downturns, like

56. *Id.*

57. This power is exercised by the Financial Policy Committee of the Bank of England, as explained below.

58. Established by S9B-9C, Bank of England 1998 Act amended by Financial Services Act 2012, c. 21, §4 - 9B, 9C (UK), https://www.legislation.gov.uk/ukpga/2012/21/section/4 [https://perma.cc/AD2K-L6GV].

59. *See Financial stability*, BANK OF ENG. (Dec. 11, 2020), https://www.bankofengland.co.uk/financial-stability https://perma.cc/94JW-VRHY, including a description entitled 'Financial Policy Committee Powers'.

60. Council Directive 2013/36, art. 128(7), 2013 O.J. (L 176) 404.

61. According to Minsky, capitalist economies exhibit a tendency to fluctuate between periods of high debt expansion and debt contraction, thus endogenously generating financial crisis due to excessive debt expansion followed by the "Minsky moment" which is marked by a collapse of the market and credit squeeze. The CCyb directly addresses these problems by making lending more expensive for banks during times of economic growth. Hyman P. Minsky, *The Financial Instability Hypothesis* (Levy Econ. Inst., Working Paper No. 74, 1992), http://www.levyinstitute.org/pubs/wp74.pdf [https://perma.cc/5G4H-CB49].

62. *Bank of England Measures to Respond to the Economic Shock from COVID-19*, BANK OF ENG. (Mar. 11, 2020), https://www.bankofengland.co.uk/news/2020/march/boe-measures-to-respond-to-the-economic-shock-from-COVID-19 [https://perma.cc/J5SS-CRB2]; *Statement by the PRA Accompanying Measures Announced by the Financial Policy Committee*, BANK OF ENG. (Mar. 11, 2020), https://www.bankofengland.co.uk/prudential-regulation/publication/2020/statement-by-the-pra-accompanying-measures-announced-by-the-fpc [https://perma.cc/K7Y9-4K4C].

63. Jonathan S. Masur & Eric A. Posner, *Should Regulation be Countercyclical?*, 34 YALE J. ON REG. 857 (2017).

the one caused by the onset of the COVID-19 crisis, the relaxation of prudential regulation that is inherently adjustable is merely counter-cyclical regulation that counteracts excessively risk-averse behaviour.

Freeing up the cost of capital originally imposed by the CCyb does not automatically result in more lending or forbearance. During the COVID-19 crisis, borrowers' creditworthiness would be difficult to discern. Banks may be behaviourally inclined to refrain from lending due to risk aversion and impediments to efficient markets such as acute information asymmetry, and may hoard capital instead. Hence, the PRA and FCA supplemented the inherently flexible measure of the CCyb by suspending other regulations not inherently thought to be flexible, to send stronger incentive-based messages to banks.[64] Such bundling of inherently flexible and unexpected legal elasticity has the potential to give rise to unexpected institutional dissonance. Our analysis is, however, not to discourage policymakers from deploying legal elasticity, but to encourage towards deeper engagement with its effects.

As loan forbearance creates doubt as to banks' asset quality, banks may choose to conserve capital, or worse, raise capital to shore up against credit risks. In this manner, payment holidays would be contrary to banks' ability to lend or help their borrowers. To steer banks' behaviour towards 'relief and rescue', the PRA clarifies[65] that banks should not treat deferred payments as being in default. Even if deferred payments do not resume promptly, they should not mechanistically be treated as impaired assets. Banks should instead seek to understand individual financial situations. However, permitting ambiguity in whether deferred borrowers are in default poses hazards to regulatory objectives and banks' resilience.

After the global financial crisis, a forward-looking approach[66] to loan

64. *Q&A on the usability of liquidity and capital buffers*, BANK OF ENG. (July 6, 2020), https://www.bankofengland.co.uk/prudential-regulation/publication/2020/buffer-usability-qanda (last visited Aug. 29, 2020) [https://perma.cc/P9MQ-GE4H]. On the suspension of capital buffers and the liquidity ratio.

65. Letter from Sam Woods, Deputy Governor and CEO, Prudential Reg. Auth., to Chief Executive Officers of UK Banks (Mar. 26, 2020), https://www.bankofengland.co.uk/prudential-regulation/letter/2020/COVID-19-ifrs-9-capital-requirements-and-loan-covenants [https://perma.cc/5AN7-ZUB2]; *Statement by the PRA on Regulatory Capital and IFRS 9 Requirements for Payment Holidays,* BANK OF ENG. (May 22, 2020), https://www.bankofengland.co.uk/prudential-regulation/publication/2020/statement-on-application-regulatory-capital-ifrs9 [https://perma.cc/7334-8RQB] [hereinafter *Statement by the PRA*].

66. Rosa M. Lastra, *Defining Forward Looking, Judgement-Based Supervision*, 14 J. OF BANKING REGUL. 221, 222–23 (2013).

loss provision for banks was encouraged.[67] The International Financial Reporting Standard, IFRS 9, requires banks to account for debt instruments at fair value.[68] This measurement is intended to ensure that banks' capital provision is made against loans valued conservatively.[69] Payment holidays exacerbate information asymmetry in relation to borrowers' creditworthiness and banks may make increased loan loss provisions against these,[70] as part of the continuing assessment of borrowers' creditworthiness, paddling back against the capital liberation that has been offered. The PRA had to moderate banks' tendencies by encouraging[71] more discretionary assessment on borrowers' credit risks instead of risk aversion across the board. However, banks would suffer from uncertainty as to what extent the boundaries of existing regulations can be pushed.[72] The PRA has, in our view, 'delegated' to banks the implementation of such a balance at the micro level of evaluating their borrowers.[73] European regulators also face this similar difficulty in regulatory objective balancing.[74]

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67. This approach is accounting-based, based on the accounting standard IFRS 9. For a discussion of the application of this approach, *see* Mi Joo Lee, In Tae Hwang and Sun Min Kang, *The Effect of Forward-looking Criteria and IFRS on the Informativeness of Banks' Loan Loss Allowances: Evidence from Korea: Loan Loss Allowances in Banks* 30 Australian Accounting Review 85 (2018).

68. Unless they satisfy the contractual cash flow test and business model assessment requirement. The IFRS 9 provides a definition of fair value as 'the value that would be received if an asset is sold, or paid if a liability is transferred, between market participants in an orderly transaction'. *See* Samuel Knott et al., *Understanding the Fair Value of Banks' Loans* 8 (Bank of Eng. Fin. Stability, Paper No. 31, 2014), https://www.bankofengland.co.uk/financial-stability-paper/2014/understanding-the-fair-value-of-banks-loans [https://perma.cc/4UYD-JK8F].

69. Banks have to ensure that each loan made is supported by adequate capital, under capital adequacy regulation. This is to ensure that banks' credit risks are appropriately supported. The area of capital adequacy is discussed in CHIU & WILSON *supra* note 25 at 335.

70. Stephen Morris & David Crow, *European Bank Investors Brace for Loan-Loss Provisions*, FIN. TIMES (Apr. 27, 2020, 4:00 AM), https://www.ft.com/content/1d9d862a-df05-47c1-8245-cf798127165f (last visited Aug. 19, 2020); Stephen Morris et al., *BoE Warns Bank Loan Reserves Risk Choking Business Funding*, FIN. TIMES (Apr. 26, 2020, 9:00 PM), https://www.ft.com/content/75767049-edfb-4074-942c-f9ce4d07f861 (last visited Aug. 19, 2020); Jon Rees & Mohammad Taqi, *UK Banks' Loan Loss Provisions Soar in Face of Pandemic*, S&P GLOB. MKT. INTEL. (May 7, 2020), https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/uk-banks-loan-loss-provisions-soar-in-face-of-pandemic-58478176 [https://perma.cc/6GX9-YZJ6].

71. *Statement by the PRA, supra* note 65.

72. *See infra* Section V.

73. *Statement by the PRA, supra* note 65. The PRA does not encourage banks to treat deferred borrowers as raising increased credit risk for banks and encourages banks to investigate each debtors' circumstances before judgment is made as to whether they have become impaired credit risks for banks.

74. *See, e.g.*, EUR. BANKING AUTH., FINAL REPORT ON PAYMENT MORATORIA (Apr. 2, 2020), https://bit.ly/3kMSQxa [https://perma.cc/FSZ9-9DJZ]; Opinion of 20 May 2020 on Amendments to the

1. Unintended Adverse Consequences for Markets, Institutional Stability and Distributive Justice

Although well-intentioned, temporary payment holidays are not the same as permanent debt relief. Borrowers benefiting from this may behaviourally postpone their troubles, storing up arrears that may become even more unmanageable in the future.[75] The FCA's Chairman[76] is concerned that customers are incentivized into unsustainable debt levels and future financial fragility.[77] There is a lack of clear guidance to lenders and borrowers on negotiating the exact terms of debt servicing after payment holidays cease. The conduct of debt enforcement down the road is also a matter for concern from the point of view of social justice,[78] as lenders would be anxious to mitigate the impairments to their balance sheets. How will the return of efficiency and contractual discipline affect consumers and are they factoring these into account in their choices under stress during the pandemic? Would and should there be a difference between the treatment of retail and business borrowers, bearing in mind that business borrowers may be responsible for job creation?

Next, regulatory suspension can affect market mechanism chains that may in turn adversely affect consumers. This is experienced in the US mortgage markets where securitization is the norm for supporting mortgage underwriting.[79] Underwriters of mortgages seek to bundle mortgages into securitized assets usually after three months of such mortgages being

Union Prudential Framework in Response to the COVID-19 Pandemic, 2020 O.J. (C 180) 4–9.

75. Nicholas Megaw & Matthew Vincent, *Lenders Sound Warning on Mortgage Holidays*, FIN. TIMES (Mar. 25, 2020, 12:12 PM), https://www.ft.com/content/3a6b82b0-6e77-11ea-89df-41bea055720b (last visited Aug. 19, 2020).

76. Charles Randell, Chair, Fin. Conduct Auth. and Payment Sys. Reg., Speech at Virtual Roundtable of Bank Chairs Hosted by UK Fin: A Financial System to Support the Recovery (June 16, 2020), https://www.fca.org.uk/news/speeches/financial-system-support-recovery [https://perma.cc/KXV2-8YMU].

77. *Id.*

78. *See e.g.*, Nicholas Megaw & Matthew Vincent, *UK Loan Freeze Plan Leaves Customers Still Open to Arrears Letters*, FIN. TIMES (Apr. 5, 2020, 5:35 PM), https://www.ft.com/content/7a533dc5-8cd8-4ef3-9963-d1f43e76ff47 (last visited Aug. 19, 2020).

79. On securitization in the US market generally, *see* Miguel Segoviano et al, *Securitization: Lessons Learned and the Road Ahead*, INTERNATIONAL MONETARY FUND: Working Paper WP/13/255 https://www.imf.org/external/pubs/ft/wp/2013/wp13255.pdf [https://perma.cc/LA33-CADT].

written.[80] Payment holidays affect the information quality of such mortgages, as no reliable stream of income can be reported for securitized assets sales.[81] This can in turn freeze up mortgage markets, adversely affecting households that need mortgages or refinancing.[82]

Regulators also need to consider the distributive effects of regulatory suspensions. There may be a temporary distributive effect from lenders to borrowers as forbearance is implemented. The optimality of this redistributive effect depends on bank fragility and whether there is an increased chance of use of public funds to recapitalize them.[83] Post-crisis micro-prudential regulatory reforms have made banks more resilient,[84] but it remains uncertain how far banks can push their newly-built resilience.[85]

Finally, we raise the concern that regulatory suspensions do not apply equally to all credit markets, as payment deferrals mandated by the FCA do not apply to peer-to-peer lending arrangements.[86] 'Peer' lenders are not regulated entities and only the platform that facilitates peer-to-peer lending is regulated[87] in respect of their conduct of business vis-à-vis customers on

80. Laura Noonan, *Payment Holidays are Messing with America's $2.2tn Mortgage Machine*, Fin. Times (Apr. 17, 2020, 11:00 AM), https://www.ft.com/content/f6c218a1-358e-4564-9919-1a96da91fc94 (last visited Aug. 19, 2020).

81. *Id.*

82. *Id.*

83. EMILIOS AVGOULEAS & CHARLES GOODHART, *Bank Resolution a Decade After the Global Financial Crisis: A Systematic Reappraisal*, *in* SYSTEMIC RISK IN THE FINANCIAL SECTOR: TEN YEARS AFTER THE GREAT CRASH 31 (Douglas W. Arner eds., 2019); Patrick Jenkins, *Why Banks Should Raise Equity to Get Through this Stress*, FIN. TIMES (May 18, 2020 5:00 AM), https://www.ft.com/content/d57f3068-2953-4424-82e1-1ae3db1bc5bf (last visited Aug. 19, 2020).

84. *See* Peter Murphy et al., *CET1 Capital Ratios at Europe's Largest Banks, Q4*, S&P GLOB. MKT. INTEL. (Mar. 17, 2020), https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/cet1-capital-ratios-at-europe-s-largest-banks-q4-57567429 [https://perma.cc/EF4C-S5NE]. On the ways in which banks responded to the post-crisis capital ratios, *see* Benjamin H.Cohen & Michela Scatigna, *Banks and capital requirements: Channels of adjustment*, 69 J. OF BANKING & FIN. S56 (2016).

85. *See* Howard Mustoe, *Are Britain's Banks Strong Enough for Coronavirus?*, BBC NEWS (May 20, 2020), https://www.bbc.com/news/business-52691369 [https://perma.cc/DU2U-ZU27]; Alissa Kleinnijenhuis et al., *Usable Bank Capital,* VOXEU (June 30, 2020), https://voxeu.org/article/usable-bank-capital#.XwA9ibxoIRc.twitter [https://perma.cc/787T-34B2]; Simon Sameuls, *Banks Need to Prepare Now for COVID-19 Losses Later,* FIN. TIMES (July 9, 2020, 5:00 AM), https://www.ft.com/content/918fe325-8a7f-4646-9031-6e7f2d61b3db (last visited Aug. 19, 2020).

86. Peer-to-peer lending platforms manage payment deferral requests and potential loan defaults on their own, *see* Patrick Collinson, *UK's Biggest Peer-To-Peer Lender Halves Interest Rates to Prepare for Defaults,* THE GUARDIAN (May 5, 2020), https://www.theguardian.com/money/2020/may/05/ratesetter-uk-biggest-peer-to-peer-lender-cuts-rates-to-prepare-for-loan-defaults-coronavirus [https://perma.cc/QF8H-DMEW].

87. FIN. CONDUCT AUTH., LOAN-BASED ('PEER-TO-PEER') AND INVESTMENT-BASED

both sides of the market, i.e. the lenders/investors in loans and borrowers. This is a hazard in 'regulatory commons' articulated by Buzbee[88] who cautions against regulatory gaps that may be ideologically anomalous but caused by the drawing of regulatory boundaries.[89] The treatment of borrowers is completely left to the self-regulation of peer-to-peer lending platforms, some of whom allow payment holidays and 'pass the pain' to their lenders/investors by freezing withdrawals or slashing returns.[90]

B. Increasing Credit Availability to Businesses

The PRA has instructed UK banks that all elements of liquidity and capital buffers "exist to be used as necessary to support the economy."[91] This relates to the 'rescue' element of the UK's policy for businesses to access credit during the COVID-19 crisis. This policy pronouncement arguably creates dissonance in relation to regulatory objectives in micro-prudential regulation designed to combat excessive lending and risk-taking[92] in the wake of the global financial crisis. However, the expansion of credit is fiscally supported.[93] Fiscal support for corporate borrowing, trade credit and commercial paper is also introduced in the US,[94] although it is left to state and federal prudential regulators to work out prudential regulatory adjustments.

UK businesses with turnover of less than £45 million can benefit from

CROWDFUNDING PLATFORMS: FEEDBACK TO CP18/20 AND FINAL RULES (2019), https://www.fca.org.uk/publication/policy/ps19-14.pdf [https://perma.cc/658J-XJN2].

88. William W. Buzbee, *Recognizing the Regulatory Commons*: *A Theory of Regulatory Gaps*, 89 IOWA L. REV. 1 (2003).

89. *See id.* For discussion on regulatory boundaries being challenged due to the structural changes that innovation brings to markets, *see* Charles A. E. Goodhart & Rosa M. Lastra, *Border Problems*, 13 J. INT. ECON. L. 705 (2010).

90. Marc Shoffman, *The Quandary Facing P2P Lenders and Borrower Payment Holidays*, PEER2PEER FIN. NEWS (Mar. 25, 2020), https://www.p2pfinancenews.co.uk/2020/03/25/the-quandary-facing-p2p-lenders-and-borrower-payment-holidays/ [https://perma.cc/9QVX-NG9Q].

91. Prudential Regulation Authority, *Q&A on the Usability of Liquidity and Capital Buffers*, BANK OF ENG. (July 6, 2020), https://www.bankofengland.co.uk/prudential-regulation/publication/2020/buffer-usability-qanda (last visited Aug. 29, 2020).

92. FIN. SERVS. AUTH., THE TURNER REVIEW: A REGULATORY RESPONSE TO THE GLOBAL BANKING CRISIS 39-42 (2009), http://www.actuaries.org/CTTEES_TFRISKCRISIS/Documents/turner_review.pdf [https://perma.cc/2P9S-2HKJ]; HOWARD DAVIES, THE FINANCIAL CRISIS: WHO IS TO BLAME? (2010).

93. *See infra* notes 95, 97.

94. CARES Act §§ 1102, 1105, 3102. For small businesses, *id.* §§ 1102, 1105. For sectors affected severely, *id.* § 3102 (total cap of $208bn for loan assistance).

the Coronavirus Business Interruption Loan Scheme.[95] Under this scheme, accredited lenders may provide loans and overdraft facilities of up to £5 million, guaranteed at 80% by the government, to be repaid over up to six years.[96] Smaller UK businesses can borrow from the Bounce Back Loan Scheme that provides loans of up to £50000, guaranteed at 100% by the government to be repaid over up to six years with no payments in the first twelve months.[97] Lenders are expected to assess businesses' viability.[98] Eligible borrowers should not be suffering from existing financial difficulty.[99]

Regulatory suspensions to incentivize bank lending, besides the CCyb adjustment, include the use of all regulatory buffers, the liquidity ratio and a generous treatment of leverage ratio constraints.[100] First, regulatory capital buffers such as the capital conservation, systemic risk, PRA buffer and buffers applying to systemically important banks are imposed on banks as risk-constraining measures in post-crisis reforms.[101] Banks may draw down any discretionary buffer[102] they have on top of regulatory ones, and after its exhaustion draw down their regulatory buffers.[103] The PRA and FPC have nevertheless maintained the notional levels of mandatory regulatory buffers (except CCyb), for institutional continuity in capital regulation.[104]

Second, banks are encouraged to allow businesses with credit lines and undrawn credit to draw upon such lines, even if this means banks' liquidity ratios may fall below the mandatory 100% they are supposed to maintain.[105]

95. *Apply for the Coronavirus Business Interruption Loan Scheme*, U.K. DEP'T FOR BUS., ENERGY & INDUS. STRATEGY (May 1, 2020), https://www.gov.uk/guidance/apply-for-the-coronavirus-business-interruption-loan-scheme [https://perma.cc/R776-ZQTK].

96. *Id.*

97. *Apply for a Coronavirus Bounce Back Loan*, U.K. DEP'T FOR BUS., ENERGY & INDUS. STRATEGY (May 4, 2020), https://www.gov.uk/guidance/apply-for-a-coronavirus-bounce-back-loan [https://perma.cc/699N-W79E].

98. *See supra* notes 95, 97.

99. *Id.*

100. *See supra* note 65.

101. CHIU & WILSON, *supra* note 25, at ch. 8.

102. Prudential Regulation Authority, *supra* note 65.

103. *See* BANK OF ENG., THE FINANCIAL POLICY COMMITTEE'S FRAMEWORK FOR THE SYSTEMIC RISK BUFFER (2016); BANK OF ENG., THE PRA'S APPROACH TO THE IMPLEMENTATION OF THE SYSTEMIC RISK BUFFER (2018) (amended the Financial Policy Committee's framework from 2016).

104. Prudential Regulation Authority, *PRA Decision on Systemic Risk Buffer Rates,* BANK OF ENG. (Apr. 9, 2020), https://www.bankofengland.co.uk/prudential-regulation/publication/2020/pra-decision-on-srb-rates [https://perma.cc/5U28-Z29K].

105. Prudential Regulation Authority, *supra* note 65.

The liquidity coverage ratio is intended to be maintained at all times at 100% so that banks can meet their cash outflows for a period of 30 days to prevent a liquidity-driven crisis.[106] This unexpected elasticity, however, raises concerns about the balancing of short-term crisis management objectives against prudential objectives. It may be argued though that banks' risk of depleting their liquidity is mitigated by the Bank of England's new Coronavirus Corporate Financing Facility,[107] designed to help businesses tide over liquidity squeezes through their bank.

At the EU level, a new legislative initiative allows banks not to count certain loans as subject to the prudential measure of the leverage ratio.[108] The leverage ratio limits all leverage created by banks to be supported by at least 3% of CET1 capital.[109] This backstops bank lending and compliments other micro-prudential regulation. The new EU Regulation,[110] called the 'CRR Quick Fix' package, introduced temporary flexibility in calculating banks' lending to avoid unnecessary constraint by the leverage ratio.[111] Certain exposures such as guaranteed loans by national governments can be excluded from the ratio.[112] The PRA allows loans made under the Bounce Back Scheme to not be counted in the leverage ratio.[113]

In order to precisely steer banks' behaviour towards increased support

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106. BASEL COMMITTEE ON BANKING SUPERVISION, BASEL III: THE LIQUIDITY COVERAGE RATIO AND LIQUIDITY RISK MONITORING TOOLS (2013), https://www.bis.org/publ/bcbs238.pdf [https://perma.cc/3WQ5-4JUM], enacted in EU and UK legislation.

107. *Covid Corporate Financing Facility (CCFF): Information for Those Seeking to Participate in the Scheme*, BANK OF ENG. (Oct. 26, 2020), https://www.bankofengland.co.uk/news/2020/march/the-covid-corporate-financing-facility [https://perma.cc/P8EZ-K2JC].

108. *See infra* note 110.

109. Council Regulation (EU) 575/2013, art. 429, 430, 2013 O.J. (L 176); on the leverage ratio, *see* Article 78(1) of the Regulation (EU) 2019/876 of the European Parliament and of the Council of 20 May 2019 amending Regulation (EU) No 575/2013; as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements, *see* Regulation (EU) No 648/2012. CET1 capital relates to shareholders' equity, regarded as best quality loss absorbing capital.

110. Council Regulation (EU) 2020/873, 2020 O.J. (L 204) 4.

111. EUR. BANKING AUTH., FINAL REPORT–GUIDELINES ON SUPERVISORY REPORTING AND DISCLOSURE REQUIREMENTS IN COMPLIANCE WITH THE CRR 'QUICK FIX' IN RESPONSE TO THE COVID-19 PANDEMIC (2020), https://bit.ly/3mEIbW8 [https://perma.cc/H6VM-UW34].

112. Regulation (EU) No 873/2020, *supra* note 110 at recital 8.

113. Prudential Regulation Authority, *Statement on Credit Risk Mitigation Eligibility and Leverage Ratio Treatment of Loans Under the Bounce Back Loan Scheme*, BANK OF ENG. (May 4, 2020), https://www.bankofengland.co.uk/prudential-regulation/publication/2020/pra-statement-on-crm-and-leverage-ratio-loans-under-bbls [https://perma.cc/4X62-R4EG].

for the real economy instead of perverse incentives such as rewarding shareholders, the PRA and ECB have discouraged banks from paying dividends or engaging in share buy-backs, as well as paying any cash bonus to certain material categories of staff.[114] This is a different type of 'suspension' as it is a form of intervention that disrupts market participants' expectations, such as those of institutional shareholders. Regulators' power over dividend restrictions is warranted under existing regulation[115] to promote the resilience of banks and financial stability. This use of discretionary power, outside of the original rationale, may, however, raise long-term problems relating to banks' cost of capital and ability to attract and retain talented staff.

The relaxation of micro-prudential requirements to incentivize lending is complemented by the suspension of externally administered stress testing. The Bank of England (BoE) carries out annual cyclical and biennial exploratory stress tests so that supervisors can understand banks' capital-resilience and potential for continuity in stressful scenarios.[116] The BoE has postponed the 2020 stress test,[117] to reduce pressure on banks and focus them on the relief and rescue agenda.[118] Although the BoE has discretion to determine the timing of stress tests, the drawback of such suspension is that

114. Prudential Regulation Authority, *PRA Statement on Deposit Takers' Approach to Dividend Payments, Share Buybacks and Cash Bonuses in Response to COVID-19,* BANK OF ENG. (Mar. 31, 2020), https://www.bankofengland.co.uk/prudential-regulation/publication/2020/pra-statement-on-deposit-takers-approach-to-dividend-payments-share-buybacks-and-cash-bonuses [https://perma.cc/E8U9-84PF]; Press Release, Eur. Cent. Bank, ECB Extends Recommendation Not to Pay Dividends Until January 2021 and Clarifies Timeline to Restore Buffers (July 28, 2020), https://www.bankingsupervision.europa.eu/press/pr/date/2020/html/ssm.pr200728_1~42a74a0b86.en.html [https://perma.cc/G5TC-8TQQ].

115. Council Directive 2013/36, art. 141, 2013 O.J. (L 176) (EU).

116. Donald Kohn, External Member of the Fin Policy Comm., Bank of Eng., Speech at European Central Bank, Macroprudential Stress Testing Conference: Stress Tests: A Policymaker's Perspective (Feb. 5, 2020), https://www.bankofengland.co.uk/speech/2020/donald-kohn-speech-at-2020-ecb-conference-on-macroprudential-stress-testing [https://perma.cc/V5LM-HGAH].

117. *Bank of England Announces Supervisory and Prudential Policy Measures to Address the Challenges of COVID-19*, BANK OF ENG. (Mar. 20, 2020), https://www.bankofengland.co.uk/news/2020/march/boe-announces-supervisory-and-prudential-policy-measures-to-address-the-challenges-of-covid-19 [https://perma.cc/W3EV-FD2B].

118. Delphine Strauss & Stephen Morris, *BoE Cancels Stress Tests to Ease Pressure on Lenders*, FIN. TIMES (Mar. 20, 2020, 10:29 AM), https://www.ft.com/content/7433d55c-6a89-11ea-800d-da70cff6e4d3 (last visited Aug. 29, 2020).

information opacity[119] may be exacerbated at this current time of crisis.[120] Uncertainty over the timeframe for the next stress test makes it hard for banks to plan in advance[121] and delayed stress tests also mean delayed supervisory guidance on banks' micro-prudential positions.

1. Unintended Adverse Consequences for Bank Resilience, Regulatory Objectives and Social Justice

Regulators need to consider the longer-term adverse consequences of increased lending, such as the accumulation of nonperforming exposures on banks' balance sheets.[122] This consequence is beneficial neither for banks nor borrowers as banks' regulatory compliance may be jeopardised and their future capacities to support the real economy diminished. Further, balance sheet pressures can also entail enforcement against borrowers, leading to social frictions between finance and society.[123]

In the UK, and arguably in the US, banks' credit risks are likely exacerbated by fiscal support for government-backed loans. Fiscal guarantees may fuel moral hazard as the urgent demand for loans makes underwriting a pressed process exacerbated by information asymmetry.[124]

119. Jonathan Ford, *Coronavirus exposes illusion of UK bank capital strength*, FIN. TIMES (5 Apr. 2020), https://www.ft.com/content/31e9e474-1398-430e-92fa-ef4e43c4e0ac.

120. Kathryn Judge, *Stress Tests During Times of War*, EURO. CORP. GOVERNANCE INST.: Working Paper No. 529, 2020), https://ssrn.com/abstract=3633310 [https://perma.cc/B97W-7CBM]; Dean Buckner & Kevin Dowd, *Can UK Banks Pass the COVID-19 Stress Test?* 10 (2020), https://ssrn.com/abstract=3614865 [https://perma.cc/5CL2-EZM9].

121. Robert Weber, *A Theory for Deliberation-Oriented Stress Testing Regulation*, 98 MINN. L. REV. 2236, 2248–50 (2014).

122. Henk Jan Reinders, Dirk Schoenmaker & Mathijs van Dijk, *Is COVID-19 a Threat to Financial Stability in Europe?* 2–3 (2020), https://ssrn.com/abstract=3633932 [https://perma.cc/SNM4-CJ3D].

123. This problem is recognized in the UK by the Treasury who is concerned about banks taking enforcement action against many small business borrowers, leading to a 'PR disaster', *see* Daniel Thomas, Stephen Morris, & George Parker, *UK Treasury and Banks in Talks on Coming Wave of Bad Covid Debt*, FIN. TIMES (July 26, 2020), https://www.ft.com/content/aa102028-710e-43e5-a199-0198f5f16ec2.

124. Peter Lee, *CBILS Faulty: Sunak's Flagship UK Lending Scheme Looks Unfit for Purpose*, EUROMONEY (Apr. 24, 2020), https://www.euromoney.com/article/b1lbgfwrx72nn3/cbils-faulty-sunaks-flagship-uk-lending-scheme-looks-unfit-for-purpose [https://perma.cc/P6TX-6KM5]; Collen Masunda, Shalini Sankaranarayanan, Pratibha Chhabra, Fabrizio Fraboni, & Luz Maria Salamina, *COVID 19 Emergency Policy Responses. Why Credit Reporting Matters in the Stabilization and Recovery Phases?*, WORLD BANK (May 2020), https://openknowledge.worldbank.org/handle/10986/33814 [https://perma.cc/QRP5-HL95].

Banks may minimize diligence standards as they do not have the incentive to price conservatively,[125] relying on the eventuality of fiscal bailout. Commentators already expect at least 40% of Bounce Back loans to default in due course.[126]

The level of loans made in the wake of the COVID-19 crisis that can be expected to be non-performing would likely rise,[127] entailing adverse consequences for bank resilience,[128] even if banks' current capital positions are relatively strong. Regulators are already concerned,[129] but refrain from impeding the policy goals of 'rescue and relief'. We urge contemporaneous engagement with these hazards instead of blithe assumptions that the regulatory framework would simply resume after the cessation of regulatory suspensions.[130] How far can the expected challenges to bank resilience be

125. Patrizia Baudino, *Public Guarantees for Bank Lending in Response to the COVID-19 Pandemic*, BIS FIN. STABILITY INS. BRIEFS (Apr. 2020), https://www.bis.org/fsi/fsibriefs5.pdf [https://perma.cc/8LQ2-ZM5P]; Pierre Schammo, *Who Knows What Tomorrow Brings? Of Uncertainty in Times of a Pandemic*, OXFORD BUS. L. BLOG (Apr. 28, 2020), https://www.law.ox.ac.uk/business-law-blog/blog/2020/04/who-knows-what-tomorrow-brings-uncertainty-times-pandemic [https://perma.cc/WQ9V-SJWS].

126. Stephen Morris et al., *UK Banks Warn 40%-50% of 'Bounce Back' Borrowers Will Default*, FIN. TIMES (May 31, 2020, 9:30 PM), https://www.ft.com/content/8a551c37-2de8-446b-a8b8-d4a61d33ef73 (last visited Aug. 19, 2020).

127. *See* Ivan Huljak et al., *Do Non-Performing Loans Matter for Bank Lending and the Business Cycle in Euro Area Countries?* 2–3 (Eur. Cent. Bank, Working Paper No. 2411, 2020), https://www.ecb.europa.eu/pub/pdf/scpwps/ecb.wp2411~839bc74726.en.pdf [https://perma.cc/RF4M-MWLY]; *COVID-19: The Regulatory and Supervisory Implications for the Banking Sector*, JOINT IMF-WORLD BANK STAFF POSITION NOTE (May 21, 2020), https://www.imf.org/en/Publications/Miscellaneous-Publication-Other/Issues/2020/05/20/COVID-19-The-Regulatory-and-Supervisory-Implications-for-the-Banking-Sector-49452 [https://perma.cc/5JF3-H5YC]; Laura Noonan & Robert Armstrong, *Three US Banks Set Aside Record $28bn for Loan Losses*, FIN. TIMES (July 14, 2020, 5:37 AM), https://www.ft.com/content/f1bbaf65-7cb7-4855-ba7f-d9bda5f4b053 (last visited Aug. 19, 2020); Stephen Morris & Owen Walker, *European Banks Braced for €800bn of Loan Losses if Pandemic Worsens*, FIN. TIMES (July 21, 2020, 5:00 AM), https://www.ft.com/content/1c4faf6c-975c-4566-8e0e-c9cbd613db42 (last visited Aug. 19, 2020).

128. ANIL ARIET AL., EUR. CENT. BANK, COVID-19 AND NON-PERFORMING LOANS: LESSONS FROM PAST CRISES 6-7 (May 27, 2020), https://www.ecb.europa.eu/pub/economic-research/resbull/2020/html/ecb.rb200527~3fe177d27d.en.pdf [https://perma.cc/8H8X-EWG2]; ELENA CARLETTI ET AL., CTR. FOR ECON. POL'Y RSCH., THE BANK BUSINESS MODEL IN THE POST-COVID-19 WORLD 19–20 (2020), https://cepr.org/content/bank-business-model-post-covid19-world [https://perma.cc/KD3K-GEYA].

129. *Basel Committee Meets; Discusses Impact of COVID-19; Reiterates Guidance on Buffers: Press Release*, (June 17, 2020), https://www.bis.org/press/p200617.htm [https://perma.cc/7EQ7-SGZ7] (reiterating the importance of maintaining the existing regulatory regime).

130. PRUDENTIAL REGUL. AUTH., PILLAR 2A: RECONCILING CAPITAL REQUIREMENTS AND MACROPRUDENTIAL BUFFERS (2020), https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/policy-

met by the fiscal backstop for government-guaranteed loans?[131] Further, would a fiscal backstop not create a vicious circle problem for banks, as banks are also funders for sovereigns?

Increased credit is also a snare for borrowers. The Bounce Back Scheme relieves businesses of payments for the first twelve months, but it is uncertain if this would be sufficient for a business to recover.[132] The government guarantee can introduce perverse incentives for banks to accelerate treating recovering Bounce Back borrowers as in default so as to call upon the guarantee, exacerbating the pressure placed on the fiscal backstop. Huertas[133] argues that current loan support measures must be coupled with regulatory thinking about reasonable conduct in treating borrowers in due course.

It may be argued that the hazards of banks in supporting expanded credit are overstated as companies have the option of raising equity, a more stable form of finance, to tide over the crisis. Equity-raising also benefits from regulatory suspension discussed in Section IV. However, investors are risk averse during the COVID-19 crisis and can be highly selective or make equity financing costly, favouring companies that are already financially strong, punishing those that have signals of weakness but are not unviable.[134] Empirical research finds that companies are turning more to debt than equity issuances,[135] and companies' stock market prices are penalized by investors' perceptions such as whether they are affected by trade with China or have healthy leverage and cash levels.[136]

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statement/2020/ps1520.pdf?la=en&hash=8FEBCB779D8FE8FB6328AB57AF79AA47B4914614 [https://perma.cc/8JNW-EG68] (discussing a 12-month estimated suspension of the CCyb, while the ECB refers to suspension until end 2021, n. 86).

131. Szu Ping Chan, *Coronavirus: UK Faces 'Explosive' Debt Levels*, BBC NEWS (July 14, 2020), https://www.bbc.com/news/business-53402176 [https://perma.cc/QF84-A9KC].

132. Uncertainties in the timeframe for business recovery have been opined in Larry Elliot, *UK Economy: A Full Recovery from the Covid Slump Will Be Slow*, THE GUARDIAN (Aug. 12, 2020), https://www.theguardian.com/business/2020/aug/12/uk-economy-a-full-recovery-from-the-covid-slump-will-be-slow [https://perma.cc/FM3B-DJRM].

133. *See* Huertas, *supra* note 36.

134. *See* Sam Kerr, *Investors Demand Companies Justify COVID-19 Equity Raises*, GLOB. CAP. (Apr. 6 2020), https://www.globalcapital.com/article/b1l2knxz0czqhq/investors-demand-companies-justify-COVID-19-equity-raises [https://perma.cc/7T9S-5FZA].

135. Michael Halling, Jin Yu & Josef Zechner, *How Did Covid-19 Affect Firms' Access to Public Capital Markets?* (Sweedish House of Fin. Rsch., Working Paper No. 20-15, 2020), https://ssrn.com/abstract=3596114 [https://perma.cc/T7K7-R4E5].

136. Stefano Ramelli & Alexander F. Wagner, *Feverish Stock Price Reactions to COVID-19*, REV. OF CORP. FIN. STUD. (forthcoming 2020) (June 2020),

Legal elasticity in facilitating bank lending is an important policy in 'relief and rescue' aims. But such elasticity creates a number of unintended and adverse consequences that policymakers should consider on an *ex ante* basis rather than wait for problems to be manifest *ex post.*[137] Regulators should engage in a fully-theorized understanding of the structural nature of legal elasticity, as follows:

(a) Regulators should consider how they can engage and assist banks in the dynamic landscape of assessing asset quality and banks' resilience and the impact of these upon banks' conduct of customers.[138] The supervision of prudential and conduct of business aspects can benefit from integrated conversations between the FCA and PRA,[139] but regulatory coordination may be more challenging in jurisdictions with disparate regulators, such as the US.

(b) Regulators may need to consider safe harbours from capital or liquidity breaches by banks in due course as suspended regulatory requirements resume.

(c) Regulators also have to engage with how to strike a balance between economic welfare/justice and bank resilience, such as considering writing-off for non-performing loans that penalize neither banks nor borrowers in circumstances caused by the onset of the COVID-19 crisis. For example, the US offers loan forgiveness for small businesses for wages incurred by workforce earning under $33,333 in a year.[140] The UK's furlough scheme arguably goes further, since government support for 80% of wages is structured as grants not loans. There are policy option mixes involving public and private sector support,[141] debt versus equity,[142] for regrouping corporations as economic engines, to achieve the balance between rescue of the

https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3550274 [https://perma.cc/36PU-9NQD].

137. Nicholas Dorn, *Legal 'Elasticity' and 'Sidestepping' in European Crisis Management of Financial Markets*, 21 EUR. L. J. 802 (2015).

138. Editorial Board, *EU Banks Should Heed Lessons of 2008 Crisis*, FIN. TIMES OPINION: FT VIEW (July 22, 2020), https://www.ft.com/companies/financials (last visited Aug. 20, 2020).

139. The PRA's and FCA's co-ordination is discussed in Sect V, *infra*, under "Proposal Two".

140. CARES Act § 1105.

141. Chris Giles, *UK Financiers' Flawed Call for Grants Not Loans*, FIN. TIMES (July 23, 2020), https://www.ft.com/content/06281720-80dc-479a-97e5-ca319be74830 (last visited Aug. 20, 2020).

142. Alex Brazier, Exec. Dir. for Fin. Stability Strategy and Risk, Bank of Eng., Speech: Protecting Economic Muscle: Finance and the COVID Crisis (July 23, 2020).

real economy, bank resilience[143] and fiscal implications.

III. REGULATORY ELASTICITY IN CAPITAL MARKETS REGULATION: CORPORATE FUND-RAISING

As freezes in economic activity during the COVID-19 lockdown threaten corporate revenues, business operational continuity, and even survival,[144] regulators have addressed equity fund-raising by companies on an emergency basis.[145] Equity provides a stable pool of capital for companies,[146] and can reinforce a company's financial resilience. Such fund-raising could be pre-emptive as businesses try to safeguard against the depletion of their cash reserves during the lockdown. The building up of companies' capital positions would strengthen their ability to retain employees and maintain investment. Debt on the other hand may be more accessible but can exacerbate financial fragility.[147] However, companies seeking to raise funds could also be in a precarious state, especially if they have high levels of debt and expenses.

The FCA issued a Policy Statement[148] to facilitate corporate fund-raising exceptionally, to last only for the duration of the pandemic. This Policy introduces regulatory suspensions and adjustments to three key aspects of fund-raising: the treatment of pre-emption rights, the general meeting procedures ordinarily needed for shareholder approval of significant transactions in the Listing Rules, and the mandatory disclosure

143. Mathias Drehmann, Marc Farag, Nikola Tarashev, & Kostas Tsatsaronis, *Buffering COVID-19 Losses – The Role of Prudential Policy*, BIS BULLETIN NO. 9 (Apr. 24, 2020), https://www.bis.org/publ/bisbull09.htm [https://perma.cc/83SY-NT52].

144. Luca Enriques, *Pandemic-Resistant Corporate Law: How to Help Companies Cope with Existential Threats and Extreme Uncertainty During the COVID-19 Crisis*, (Eur. Co. & Fin. L. Rev., Working Paper No. 530, 2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3641505 [https://perma.cc/9QAQ-ETS2].

145. *See infra* note 148.

146. *See* Hse-Yu Chiu, *Can UK Small Businesses Obtain Growth Capital in the Public Equity Markets? – An Overview of the Shortcomings in UK and European Securities Regulation and Considerations for Reform*, 28 DEL. J. CORP. L. 933 (2003).

147. Chris Giles, *Corporate Debt Levels Risk Amplifying Economic Fragility, Says IMF*, FIN. TIMES (Apr. 10, 2019), https://www.ft.com/content/9be23506-5b64-11e9-9dde-7aedca0a081a (last visited Aug. 20, 2020).

148. *Statement of Policy: Listed Companies and Recapitalisation Issuances During the Coronavirus Crisis*, FIN. CONDUCT AUTH. (Apr. 8, 2020), https://www.fca.org.uk/news/statements/listed-companies-recapitalisation-issuances-coronavirus [https://perma.cc/7CE8-JXC4].

document required for the fund-raising.[149]

A. Relaxation of Pre-emption Rights

Shareholders in the UK have a right of first refusal to the company's new offer of shares in proportion to their existing holdings[150] unless pre-emption is exempt.[151] The right of pre-emption seeks to mitigate managerial agency problems as managers may offer new shares cheaply and easily to third parties if left to their own incentives.[152] Shareholders would be adversely impacted in terms of value dilution and the reduction in voting power.[153] In the US, pre-emption rights are the exception and not the rule, particularly for publicly traded companies, as existing shareholders have a choice to purchase shares in the open market if they wish to maintain the level of their shareholdings.[154] Market mechanisms in the US are seen as sufficient to provide shareholder protection needs.[155] Despite its similarity with the US in terms of deep and liquid capital markets, the UK has a different balance of flexibility-control in relation to safeguarding the rights of shareholders.[156] There is however the possibility that articles of association can provide for a waiver of pre-emption rights in advance, for a period of up to five years, so that directors can be pre-authorized to an agreed degree of flexibility.[157] The limit is usually set at 5% of the issued share capital for any given year and not more than 7.5% of the share capital over a 3-year period.[158] This best practice is recommended by the Pre-emption Group (PEG), which comprises a range of institutional investors.[159]

149. *Id.*
150. Companies Act 2006, c. 3 § 561 (UK).
151. *Id.* §§ 564-69.
152. Eilís Ferran & Look Chan Ho, *Principles of Corporate Finance Law* 125–46 (2nd ed. 2014).
153. *Id.*
154. *Id.*
155. Arthur R. Pinto, *An Overview of United States Corporate Governance in Publicly Traded Corporations*, 58 Supp. l American J. of Compar. L. 257, 266–68 (2010).
156. Consistent with EU Second Company Law Directive; Jennifer G. Hill, *The Trajectory of American Corporate Governance: Shareholder Empowerment and Private Ordering Combat*, 2019 U. ILL. L. REV. 507 (2018).
157. Companies Act 2006 §§ 570–71.
158. *Disapplying Pre-emption Rights: A Statement of Principles*, PRE-EMPTION GROUP (July 2008), https://www.ivis.co.uk/media/6059/Statement-of-Principles-July-2008.pdf, ¶ 8.
159. *Pre-Emption Group*, FIN. REPORTING COUNCIL (Mar. 12, 2015), https://sway.office.com/HHPgz98MJB2jfEqM?loc=swsp.

The PEG made an extraordinary recommendation to investors that pre-emption rights could be waived for issuances up to 20% of issued share capital during the pandemic.[160] The extended suspension of pre-emption rights is not exactly a regulatory suspension, as it is recommended market practice by the PEG. Its status is more like soft law, with the FCA's endorsement not a form a legalization but a reinforcing signal of legitimacy and a nudge directed to investors.[161]

Although pre-emption rights are an aspect of mandatory 'shareholder protection' in UK company law, their exact implementation is subject to tailoring between companies and their shareholders in relation to pre-authorizations, disapplications and constitutional provisions. This is often regarded as the 'enabling' aspect of company law ideologically supported for its efficiency effects regarding the allocation of governance rights between voluntarily bargaining parties.[162] In the US, the enabling effects of company law are realized in terms of the doctrine of pre-emption rights itself being up for voluntary adoption.[163] One can argue that the UK's pre-emption rights regime is mandatory and not enabling law. However, there are different shades of enabling law, in terms of the extent of discretion given for private agreements between companies and their shareholders.[164] As the UK allows negotiated exclusion or disapplication of pre-emption rights between shareholders and companies,[165] pre-emption rights can be

160. *Pre-Emption Group expectations for issuances in the current circumstances*, FIN. REPORTING COUNCIL (Apr. 1, 2020), https://www.frc.org.uk/getattachment/9d158c89-f0d3-4afe-b360-8fafa22d2b6a/200401-PEG-STATEMENT.pdf [https://perma.cc/8K2N-J63P]; *Pre-Emption Group extends additional flexibility for equity placings to 30th November 2020*, FIN. REPORTING COUNCI (Sept. 4, 2020), https://www.frc.org.uk/news/september-2020-(1)/pre-emption-group-extends-additional-flexibility-f [https://perma.cc/5QYG-5F5F].

161. *See* Oren Bar-Gill & Omri Ben-Shahar, *Rethinking Nudge: An Information-Costs Theory of Default Rules*, U. CHI. L. REV. (forthcoming Apr. 2020), https://ssrn.com/abstract=3582129 [https://perma.cc/7Q54-ZS8M].

162. Roberta Romano, *Answering the Wrong Question: The Tenuous Case for Mandatory Corporate Laws*, 89 COLUM. L. REV. 1599 (1989); Henry N. Butler & Larry E. Ribstein, *Opting out of Fiduciary Duties: A Response to the Anti-Contractarians*, 65 WASH. L. REV. 1 (1990); Jonathan R. Macey, *Corporate Law and Corporate Governance a Contractual Perspective*, 18 J. CORP. L. 185 (1993); Anita Indira Anand, *An Analysis of Enabling vs. Mandatory Corporate Governance Structures Post-Sarbanes-Oxley*, 31 DEL. J. CORP. L 229 (2006).

163. Iain MacNeil, *Company Law Rules: An Assessment from the Perspective of Incomplete Contract Theory*, 1 J. OF CORP. L. STUDIES 107, 131–33 (2001).

164. Eric W. Orts, *The Complexity and Legitimacy of Corporate Law*, 50 WASH. & LEE L. REV. 1565 (1993); Jens Dammann, *The Mandatory Law Puzzle: Redefining American Exceptionalism in Corporate Law*, 65 HASTINGS L.J. 441 (2014).

165. Companies Act 2006 §§ 567–73.

regarded as a default rule but embedding flexibility.[166] However, in a crisis situation, it is uncertain if shareholders are able to agree on coherent actions, and negotiation costs can be high in the face of uncertainty and different private preferences. In this manner, the role of soft law such as best practices recommended by the PEG provides a benchmark for convergence and efficiency in private decision-making.[167] The need for harmonized optimal terms in company law, despite shareholders' theoretical freedoms to bargain with companies, has been theorized by Easterbrook and Fischel.[168]

Although the PEG has shown flexibility in waiving pre-emption rights, it is arguable that suspensions do not go far enough. Commentators have raised the prospect of shortening offer periods as lessons from the emergency fund-raising exercise by banks in the 2007–09 global financial crisis point to disadvantages of a long offer period.[169] Ferran opines that long offer periods allow short-sellers to depress the issuer's share price, adversely impacting uptake of shares.[170]

The FCA has nevertheless introduced unexpected regulatory suspensions complementing the soft law measure above. On the whole, although legal elasticity is deployed beyond what is inherently flexible, it can be argued that these measures build in significant market deference and are not overly interventionist. The bundling of inherent flexibility with unexpected suspensions may have led to a strong marketization character for the *other* regulatory suspensions, thinning out its public interest aspects. Part C in particular discusses this.

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166. *See* Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87 (1989); Ian Ayres, *Making a Difference: The Contractual Contributions of Easterbrook and Fischel*, 59 U. CHI. L. REV. 1391 (1992).

167. *See* Marc T. Moore, *Whispering Sweet Nothings: The Limitations of Informal Conformance in UK Corporate Governance*, 9 J. CORP. L. STUD. 95 (2009) (regarding the Corporate Governance Code, another soft law institution).

168. FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW (1996).

169. *See* Ferran, *infra* note 170; Iain MacNeil & Irene-Marie Esser, *The Pandemic Response in the UK in the Context of Corporate and Financial Law – within and without Law* at 9–10 (June 29, 2020), https://ssrn.com/abstract=3636292 [https://perma.cc/T9UM-FZQS].

170. Eilís Ferran, *Limits of Private Sector Solutions for Banks: Recent UK Rights Issues* (Eur. Corp. Governance Inst., Working Paper No. 115, 2008), http://ssrn.com/abstract=1290717 [https://perma.cc/B35P-7HCN].

B. Dispensation of General Meetings

Next, the FCA Policy[171] allows companies to financially re-organize themselves in a less cumbersome manner, by engaging in certain substantial transactions specified in the Listing Rules,[172] relating to significant disposals of assets. Companies can now apply for a dispensation for general meetings, which the FCA grants on a case by case basis.[173] Issuers would have to provide evidence that shareholders would have voted in favour of such a resolution if a general meeting had taken place.[174]

The procedural law of general meetings ensures that all shareholders receive the same information at the same time and are able to participate collectively in decision-making processes.[175] In reality, such procedural fairness has been somewhat undermined as institutional shareholders have begun to be more engaged with their investee companies informally, as part of 'stewardship' (since the Stewardship Code of 2010, amended 2020,[176] and the advent of similar provisions in the European Shareholders' Rights Directive 2017).[177] Policymakers' approve of and encourage institutional investors' monitoring roles.[178] Moreover, with the rise of American style[179] hedge fund shareholder activism,[180] the level of voice observed in the

171. FIN. CONDUCT AUTH., *supra* note 148.
172. FCA Handbook Listing Rules 10.5.1 (UK).
173. FCA, 'Technical Supplement – modification of general meeting requirements under the Listing Rules' (8 April 2020), https://www.fca.org.uk/publication/primary-market/modification-general-meeting-technical-supplement.pdf.
174. *Id.*
175. R.C. Nolan, *The Continuing Evolution of Shareholder Governance*, 65 CAMBRIDGE L.J. 92, 118–19 (2006).
176. FIN. REPORTING COUNCIL, THE UK'S STEWARDSHIP CODE (2020), https://www.frc.org.uk/investors/uk-stewardship-code [https://perma.cc/23BL-ZJUS]. The UK's stewardship code is voluntary and administered by the Financial Reporting Council that oversees the quality of corporate reporting and professional roles of auditors. Iris H. Chiu, *Institutional Shareholders as Stewards: Towards a New Conception of Corporate Governance?*, 6 BROOKLYN J. CORP. FIN. & COM. L. 387 (2012).
177. Directive 2007/36, on the Exercise of Certain Rights of Shareholders in Listed Companies Directive (EU) 2017/828 Amending Directive 2007/36, 2020.
178. *See* Iris H-Y Chiu, *Turning Institutional Investors into "Stewards"– Exploring the Meaning and Objectives in "Stewardship"*, 66 CURRENT LEGAL PROBS. 443 (2013) (UK).
179. Stuart L. Gillan & Laura T. Starks, *The Evolution of Shareholder Activism in the United States*, *in* INSTITUTIONAL INVESTOR ACTIVISM: HEDGE FUNDS AND PRIVATE EQUITY, ECONOMICS AND REGULATION 63–65 (William W. Bratton & Joseph McCahery eds., 2016).
180. John Armour & Brian Cheffins, *The Past, Present and Future of Shareholder Activism by Hedge Funds*, 37 J. CORP. LAW 51 (2012) (U.K.).

institutional shareholder community has risen, both because institutions have worked with hedge funds in joint campaigns[181] and because the corporate sector has attracted negative attention since the global financial crisis and home-grown scandals.[182]

The discretionary dispensation of general meeting procedures for substantial transactions may, in our view, not be regarded as prejudicial to shareholders. We argue that this is because: first, its 'bundling' with the relatively more enabling company law discussed above allows shareholders to see the regulatory suspension as an extension of what shareholders could have agreed to, and as less of a top-down imposition. Second, companies are still compelled to engage with shareholders, much in the 'stewardship' ethos of informal engagement 'outside of general meetings' to secure sufficient pre-approval.[183] Finally, regulatory discretion in dispensation can be regarded as a gatekeeping device, providing comfort for shareholders that their voice is not necessarily marginalised in corporate decision-making regarding the substantial transactions.

Nevertheless, to allow dispensation of general meetings conditioned upon companies securing written consent from a sufficient number of shareholders would mean that companies are likely to engage in selective

181. Dionysia Katelouzou, *Worldwide Hedge Fund Activism: Dimensions and Legal Determinants*, 17 U. PA. J. BUS. L. 789 (2015).

182. Home-grown scandals include: fraudulent financial reporting surrounding the collapse of Carillion, HOUSE OF COMMONS, BUS., ENERGY & INDUS. STRATEGY & WORK & PENSIONS COMMITTEES OF SESSION 2017–19, CARILLION (2018), https://publications.parliament.uk/pa/cm201719/cmselect/cmworpen/769/769.pdf [https://perma.cc/7Q8B-MTJB] (U.K.); scandal at Patisserie Valerie, *see Patisserie Valerie Says Accounting Scandal Worse Than Thought*, BBC NEWS (Jan. 16, 2019), https://www.bbc.com/news/business-46897543 [https://perma.cc/J6LY-8G9P]; social irresponsibility scandals at Sports Direct, HOUSE OF COMMONS, BUS., INNOVATION AND SKILLS COMMITTEE OF SESSION 2016–17, EMPLOYMENT PRACTICES AT SPORTS DIRECT (2016), https://bit.ly/35EndQ0 [https://perma.cc/X5DV-NZNP] (U.K.); concerns regarding UK companies' exploitation of global supply chains culminating in Modern Slavery Act 2015, *see* Molly Millar, *Five Years On, Is The UK's Landmark Anti-Slavery Law Fit For Purpose?*, REUTERS (Oct. 17, 2019), https://www.reuters.com/article/us-britain-slavery-expertviews-trfn/five-years-on-is-the-uks-landmark-anti-slavery-law-fit-for-purpose-idUSKBN1WX02J [https://perma.cc/ZJ92-UMUN].

183. Shareholder engagement between companies and institutional shareholders is expected under Arts 3g, 3h, Directive (EU) 2017/828 of the European Parliament and of the Council of 17 May 2017 amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement and UK Stewardship Code 2020, *The UK Stewardship Code 2020*, FIN. REPORTING COUNCIL, https://www.frc.org.uk/getattachment/5aae591d-d9d3-4cf4-814a-d14e156a1d87/Stewardship-Code_Dec-19-Final-Corrected.pdf [https://perma.cc/3WJF-8C6J].

engagement, with perhaps 'friendly' but significant shareholders in order to reach the required majority. In this manner, the underlying principle of fairness amongst treatment of shareholders in the collective decision-making of general meetings is compromised. Further, retail investors are likely to be marginalized as companies may not contact them to ask for their support.[184] Although stewardship practices already entail differences in the quality of company-investor relationships amongst different investors, allowing companies to selectively 'court' shareholders seems to go a step further and exacerbate the already uneven playing field. Further, even if companies accurately estimate the level of majority support, this is not equivalent to a general meeting where the percentage of shareholders dissenting is recorded. The level of dissent is important for signalling the controversiality of company proposals.

The FCA should consider the incentives on the part of affected constituents as a result of regulatory suspension and the trade-offs made amongst different interest groups affected by the suspensions. This is especially true in the stewardship landscape that emphasizes the role of institutional investors over the retail investor. Should shareholder engagement be regarded as part of the enabling character of company law, that facilitates shareholders to tailor-make their monitoring arrangements with companies and or as part of mandatory law that standardizes common expectations of protection and reflects collective values?[185] For the broader purposes of conceptualization in corporate law scholarship, bundling of regulatory suspensions in capital markets regulation with inherently flexible company law aspects raises more questions about the institutional relationship between the perceived 'more enabling' nature of corporate governance and the mandatory aspects. What boundaries are there, if any, between the ideological or jurisdictional separation[186] of corporate law from securities regulation?[187]

On the one hand, the bundling exercise may make porous the

184. Merryn S. Webb, *Bypass Retail Investors at Your Peril*, FIN. TIMES (Apr. 24, 2020), https://www.ft.com/content/b9255dab-385d-4182-8c44-200948bfaae2 (last visited Aug. 20, 2020).

185. Michal Barzuza, *Inefficient Tailoring: The Private Ordering Paradox in Corporate Law*, 8 HARV. BUS. L. REV. 131 (2018).

186. James J. Park, *Reassessing the Distinction Between Corporate and Securities Law*, 64 UCLA L. REV. 116 (2017).

187. Robert B. Ahdieh, *From 'Federalization' to 'Mixed Governance' in Corporate Law: A Defense of Sarbanes-Oxley*, 53 BUFF. L. REV. 721 (2005); Allen Ferrell, *The Case for Mandatory Disclosure in Securities Regulation Around the World*, 2 BROOKLYN J. CORP. FIN. & COM. L. 81 (2007).

boundaries of enabling corporate law and mandatory securities regulation and allow regulators greater freedom to foray into the former.[188] One the other hand, the bundling exercise may also result in the shareholder-centric ideology underpinning enabling aspects of corporate law being extended to the whole package of legal elasticity, therefore thinning out notions of public interest.[189] The longer term impact on the nature of shareholder relations and corporate governance should not be ignored even if there appears to be pressure for quick policy adjustments.[190]

C. Relaxation of Working Capital Disclosure

The cost of preparing disclosure documents for investors[191] and how disclosure may affect investors' behavioural biases in times of great uncertainty may be twin obstacles for corporate fund-raising. In such times, investors may greatly discount a company's share price as they are susceptible to risk aversion. The FCA, with the PEG's support, urged companies to utilize the exemption from the EU Prospectus Regulation 2017 with regard to issuances of securities up to 20% of total traded securities so these would not need to be accompanied by a prospectus.[192] Ferran,[193] drawing on lessons from the last emergency fund-raising by banks during the global financial crisis, recommended that suspension of mandatory disclosure in whole could be warranted if issuers are not new to the market. Not having to prepare a disclosure document would save issuers time and cost. However, mandatory disclosure is a cherished tenet in investor protection[194] and suspending this may be counter-productive if

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188. For critique *see* Roberta Romano, *The Sarbanes-Oxley Act and the Making of Quack Corporate Governance*, 114 YALE L.J. 1521 (2005).*; but see* Robert B. Ahdieh, *From "Federalization" to "Mixed Goverance" in Corporate Law: A Defense of Sarbanes-Oxley*, 53 BUFF. L. REV. 721 (2005).

189. Melvin A. Eisenberg, *The Structure of Corporation Law*, 89 COLUM. L. REV. 1461 (1989); Jeffrey N. Gordon, *The Mandatory Structure of Corporate Law*, 89 COLUM. L. REV. 1549 (1989); Robert B. Thompson, *The Law's Limit on Contracts in a Corporation*, 15 J. CORP. L. 377 (1990); William W Bratton, *Welfare, Dialectic, and Mediation in Corporate Law*, 2 BERKELEY BUS. L.J. 59 (2005).

190. Luca Enriques, *Regulators' Response to the Current Crisis and the Upcoming Reregulation of Financial Markets: One Reluctant Regulator's View*, 30 U. PA. INT'L L.J. 1147 (2009).

191. Elizabeth Howell, *An Analysis of the Prospectus Regime: The EU Reforms and the 'Brexit' Factor*, 15 EUR. CO. & FIN. L. REV. 69 (2018).

192. Art 1(5)(a), EU Prospectus Regulation 2017.

193. Ferran, *supra* note 170.

194. Rafael La Porta, Florencio Lopez-De-Silanes & Andrei Shleifer, *What Works in Securities Laws*, 61 J. FIN. 1 (2006).

companies' cost of capital increases due to investor risk aversion.[195] Hence, the FCA has not chosen to be more radical but rather to adjust mandatory disclosure in a manner that arguably puts issuers in the most favourable light possible.

Companies' annual reporting obligations still stand although filing can be delayed.[196] Investors would likely rely on issuers' disclosure on whether they have working capital for the next 12 months as a going concern, such disclosure to be audited by the company's auditors.[197] The FCA has exceptionally decided to tweak this requirement by allowing companies to provide an unqualified 'clean' working capital declaration as if the company had not been affected by the crisis, and to append disclosure about effects of the crisis in a separate document not requiring formal audit, but only a comfort letter from an auditor in support.[198] This only applies if a company's adverse financial position has been caused by the pandemic and has not entailed from other weaknesses.[199] The FCA requires that the additional 'Coronavirus Working Capital Statement' contain models and assumptions relating to the impact of the pandemic on the company.[200] This tweak is arguably a form of framing that achieves a balance between investors' information rights and issuers' fund-raising interests.

The Coronavirus Working Capital Statement[201] is arguably a form of framing of information that mitigates investors' behavioural biases in the face of negative disclosures. Kahnemann and Tversky's prospect theory[202]

195. *See* Brian J. Bushee & Christian Leuz, *Economic Consequences of SEC Disclosure Regulation: Evidence from the OTC Bulletin Board*, 39 J. ACCT. & ECON. 233 (2005); John L. Campbell et al., *The Information Content of Mandatory Risk Factor Disclosures in Corporate Filings*, 19 REV. OF ACCT. STUD. 396 (2014).

196. *Statement of Policy: Delaying Annual Company Accounts During the Coronavirus Crisis,* FIN. CONDUCT AUTH. (Mar. 26, 2020), https://www.fca.org.uk/news/statements/delaying-annual-company-accounts-coronavirus [https://perma.cc/N33H-XQKZ].

197. The working capital disclosure obligations for companies raising equity capital are set out by the UK Listing authority, *see UKLA Technical Note: Working Capital Statements — Basis of preparation*, FIN. CONDUCT AUTH. (Dec. 2012), https://www.fca.org.uk/publication/ukla/tn-320-1.pdf [https://perma.cc/5UGN-EAU8].

198. *Technical Supplement – working capital statements in prospectuses and circulars during the coronavirus epidemic*, FIN. CONDUCT AUTH. 3 (8 April 2020), https://www.fca.org.uk/publication/primary-market/working-capital-technical-supplement.pdf [https://perma.cc/9SE9-B6KL].

199. *Id.*

200. *Id.*

201. *Id.*

202. Daniel Kahnemann & Amos Tversky, *Prospect Theory: An Analysis of Decision Under Risk,* 47 ECONOMETRICA 263 (1979).

shows how the framing of information affects choice, and in particular, O'Clock and Devine[203] show how negatively-framed information by companies affects auditors' opinions (in the same way) and that the opposite produces a salutary effect upon auditors' perceptions. The disaggregation of the 'clean' working capital declaration would help to avoid auditors' biases against negatively-framed information.[204] The confinement of coronavirus-related impact to its own separate statement frames such information as being more contingent, and highlights the exogenous nature of the impact. This may encourage such information to be assessed in more forgiving light and not to preponderantly 'infect' the positive framing within a 'clean' working capital declaration.

A crucial question is whether such framing disrupts the balance of institutional values in securities regulation, i.e. the promotion of rational (as far as possible, despite behavioural biases[205]) investor market discipline for issuers. The rational investor brings about efficient pricing in capital markets,[206] and allocates capital according to such price signals.[207] It may however be argued that such framing serves as a behavioural antidote to counter sub-optimal investors' behavioural biases, such as excessive risk aversion.

Nevertheless, a more important question is what the FCA seeks to achieve in the regulatory suspensions introduced. If the net effect to facilitate easier equity fund-raising by companies only entails rational, and arguably ruthless market evaluations as well as selective and costly financing for these companies, the marketization effects of the regulatory suspensions could undermine a pro-social rhetoric in relation to saving companies or jobs. Should we allow the crisis to sift out the most robust companies, albeit bringing about a transitionary period of instability? Left to market forces, commentators[208] find that investors gravitate towards

203. Priscilla O'Clock & Kevin Devine, *An Investigation of Framing and Firm Size on the Auditor's Going Concern Decision*, 25 ACCT. & BUS. RSCH. 197 (1995).

204. Denise Dickins et al., *The Terminology of Going Concern Standards: How Subtle Differences in Wording Can Have a Big Impact*, CPA J. 35 (2016), https://www.cpajournal.com/2016/01/13/terminology-going-concern-standards/ [https://perma.cc/7EHU-BZJB].

205. ROBERT J. SHILLER, IRRATIONAL EXUBERANCE (3d ed. 2015).

206. Eugene F. Fama, *Efficient Capital Markets: A Review of Theory and Empirical Work*, 25 J. FINANCE 383 (1970).

207. *Id.*

208. Rüdiger Fahlenbrach, Kevin Rageth & René M. Stultz, *How Valuable is Financial Flexibility*

funding companies with less financial fragility during the COVID-19 crisis.[209] This may defeat the broader policy goals of saving companies and jobs, as capital markets can be excessively unforgiving towards companies with some weaknesses. There is a deeper question of whether market discipline should be the optimal channel for selecting corporate survivors as many jobs and near-term economic pain for households are at stake.

The FCA's intervention[210] in framing reflects a hint of public interest in relation to preventing massive destabilization of the corporate economy and capital markets.[211] As the UK Listing Authority, the FCA has an interest in preserving the robustness of London's capital markets.[212] However, are pro-social goals relatively unarticulated and dominated by the private and marketized character of corporate law which the FCA has chosen to rely on? The regulator has refrained from more pronounced interventionist stances, such as stock market closures proposed by Andhov in order to prevent short-termist value destruction by shareholders or short-sellers.[213] Schammo[214] queries if regulatory choices should be more explicitly 'precautionary' in the public interest.

Although we are sceptical that precautionary tools such as stock market closures are necessarily optimal in achieving a balance between pro-social

When Revenue Stops? Evidence from the COVID-19 Crisis 1-10 (Nat'l Bureau of Econ. Rsch., Working Paper No. 27106, 2020), https://www.nber.org/papers/w27106 [https://perma.cc/3T4E-6EMV].

209. Didier Saint-Georges, *Post-Coronavirus Growth Should Be More Robust But Less Optimal*, FIN. TIMES (Apr. 27, 2020), https://www.ft.com/content/e3c4b133-9aaf-4a32-bc59-03fa5438585a (last visited Aug. 20, 2020).

210. The FCA is acting in its capacity as Listing Authority in its treatment of disclosure requirements for companies seeking to raise equity during the pandemic, *see Primary markets*, FIN. CONDUCT AUTH. (2020), https://www.fca.org.uk/markets/primary-markets [https://perma.cc/X7ZN-B9KC]. We are of the view that the FCA's treatment of disclosure documents required under FINANCIAL CONDUCT AUTHORITY, *supra* note 197, is a form of interpretive framing that seeks to assist companies in their equity-raising exercise.

211. *See* Martin Wolf, *Coronavirus Crisis Lays Bare the Risks of Financial Leverage, Again*, FIN. TIMES (Apr. 28, 2020), https://www.ft.com/content/098dcd60-8880-11ea-a01c-a28a3e3fbd33 (last visited Aug. 20, 2020).

212. *See* Chris Brummer, *Corporate Law Preemption in an Age of Global Capital Markets*, 81 S. CAL. L. REV. 1067 (2008).

213. Alexandra Andhov, *COVID-19 Market Protection: Close Down Stock Exchanges*, FINREG BLOG (Mar. 25, 2020), https://sites.duke.edu/thefinregblog/2020/03/25/COVID-19-market-protection-close-down-stock-exchanges/ [https://perma.cc/NR7B-A6GY]. For an opposing view, *see* Luca Enriques & Marco Pagano, Emergency Measures for Equity Trading: The Case Against Short-Selling Bans and Stock Exchange Shutdowns (May 2020) (unpublished manuscript) (available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3598151) [https://perma.cc/R9DR-FV7L].

214. Schammo, *supra* note 125, at 3.

goals in saving the real economy and investor protection in capital markets, the FCA should consider the substantive effects of regulatory suspensions, and whether more radical options are needed[215] such as:

¶a) using public sector vehicles or public-private partnerships to support capital injection into companies alongside private sector fund-raising,[216] in a manner that does not breach state aid rules;[217]

¶b) tying down investments made in support of companies during the COVID-19 crisis to duties, measures or restrictions in support of long-termism on the part of investors to help strengthen or rebuild companies, to avoid short-termist behaviour. A form of fiduciary duties imposed on hedge fund activists[218] or controlling shareholders;[219] may be warranted;

¶c) requiring companies to make adequate disclosures and continuing transparency regarding the use of funds,[220] especially where investors may have an interest to ensure that companies pursue sustainable behaviour going forward; and[221]

¶d) instituting a form of prudential regulation[222] for the non-financial

215. JOHN KAY, UK DEPARTMENT FOR BUSINESS INNOVATION AND SKILLS, THE KAY REVIEW OF UK EQUITY MARKETS AND LONG-TERM DECISION-MAKING (2012), https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/253454/bis-12-917-kay-review-of-equity-markets-final-report.pdf [https://perma.cc/C8AE-PLTR].

216. Daniel Thomas, *Investor Plans £15bn Support for UK Companies Toiling with Crisis Loans*, FIN. TIMES (June 1, 2020), https://www.ft.com/content/e38f23da-4147-4bd3-b613-c7e6f1096cc6 [https://perma.cc/P6BY-GHBB].

217. Communication from the Commission Third Amendment to the Temporary Framework for State Aid Measures to Support the Economy in the Current COVID-19 Outbreak 2020 O.J. (C 218) 3.

218. Iman Anabtawi & Lynn A Stout, *Fiduciary Duties for Activist Shareholders*, 60 STAN. L. REV. 1255 (2008).

219. ERNEST LIM, A CASE FOR SHAREHOLDERS' FIDUCIARY DUTIES IN COMMON LAW ASIA (2019).

220. For example, investors expressed concerns that corporate bond issuances are unclear as to purposes of proceeds, and this can apply to equity issuances too, *see* Camilla Hodgson, *Rise in COVID-19 Bond Issuance Fans Fears over 'Social Washing'*, FIN. TIMES (June 30, 2020), https://www.ft.com/content/d35d1abc-0a4e-4e09-a776-154a469ef8de (last visited Aug. 20, 2020).

221. Sustainable investing is set to surge in the wake of the coronavirus pandemic. Pippa Stevens, *Sustainable Investing is Set to Surge in the Wake of the Coronavirus Pandemic*, CNBC (June 7, 2020, 4:02 PM), https://www.cnbc.com/2020/06/07/sustainable-investing-is-set-to-surge-in-the-wake-of-the-coronavirus-pandemic.html [https://perma.cc/J29K-LPZH]; *Dutch Businesses Endorse Sustainable COVID-19 Recovery*, ING (June 19, 2020), https://www.ing.com/Newsroom/News/Dutch-businesses-endorse-sustainable-COVID-19-recovery.htm [https://perma.cc/4DPV-YWX2].

222. Izabella Kaminska, *Why the Real Economy Needs a Prudential Authority Too*, FIN. TIMES (Apr. 1, 2020, 12:59 AM), https://ftalphaville.ft.com/2020/04/01/1585730516000/Why-the-real-

corporate sector in order to improve their long-term resilience.

We have explored critically the regulatory objective dilemmas,[223] challenges, unintended consequences, and possible adverse effects flowing from regulatory suspensions in credit and capital markets regulations designed overall to achieve 'relief and rescue' of households and the corporate economy. Even if regulators do not intend to bring permanent adjustments about pro-actively or prematurely, they should engage with deeper and broader considerations in the deployment of legal elasticity and impact on institutional dissonance. The deployment of legal elasticity can also be regarded as part and parcel of the need for regulators to engage in a broad notion of 'responsiveness',[224] so that dynamism can be brought to substantive policy solutions as well as regulatory processes.

IV. DEPLOYING LEGAL ELASTICITY BY FINANCIAL REGULATORS: THE WAY FORWARD

We propose three aspects of a management process for legal elasticity, as empowering measures for regulators rather than to prescribe what substantive solutions may be preferred for combatting the COVID-19 crisis. Different substantive solutions may work to different extents in different jurisdictions, but where legal elasticity is deployed, regulators face similar challenges. The three aspects of regulatory management deal with:

(a) recognizing the potential for institutional dissonance and responsively managing these effects;
(b) actively engaging in multipartite frameworks for crisis management; and
(c) pre-crisis preparedness on the part of regulators.

economy-needs-a-prudential-authority-too/ (last visited Aug. 20, 2020).

223. ARMIN J. KAMMEL, *Government Versus Markets – A Change in Financial Regulation*, *in* THE CHANGING LANDSCAPE OF GLOBAL FINANCIAL GOVERNANCE AND THE ROLE OF SOFT LAW 1–27 (2015).

224. *See supra* Section II.

A. Managing Institutional Dissonance

The reluctance of financial regulators to manage institutional dissonance more explicitly may stem from fears of proactively bringing about institutional instability. However, the cosmetic approach of bundling regulatory suspensions that are inherently flexible with those apparently not does not of itself reinforce institutional stability. Fundamental questions regarding how institutional tenets and values 'encoded' in law or regulations have been rendered imbalanced arise, in relation to moral hazard,[225] or financial institution resilience.[226] Questions abound as to whether longer-term or permanent effects arise from institutional dissonance and pave the way for policy change in due course.[227] As Baldwin et al. argue, regulatory stability is not itself a tenet that should be necessarily maintained, [228] but it is important to understand how it should be disturbed.[229]

Pistor's legal theory of finance provides the theoretical basis for conceiving of legal elasticity as structural in nature and inextricably connected with institutional disruption, even if that is a matter of degree.[230] However, one may take a more limited reading of the theory. Pistor posits that there is a hierarchy of actors in the financial system, depending on their size and economic power from large systemic banks down to retail investors and borrowers.[231] Legal elasticity is crucially supported by powerful structures, as was the case in the global financial crisis when these needed bail-outs.[232] Elasticity tends to be more accentuated at the top of the system to the benefit of sovereigns and large banks, while those at the bottom are

225. KAMMEL, *supra* note 223, ARISTIDES N. HATZIS *A Law and Economics Framework for Financial Regulation*, *in* THE CHANGING LANDSCAPE OF GLOBAL FINANCIAL GOVERNANCE AND THE ROLE OF SOFT LAW 28 (2015).
226. RESTORING FINANCIAL STABILITY: HOW TO REPAIR A FAILED SYSTEM (Viral V. Achary & Matthew Richardson eds., 2009).
227. EDWARD M. IACOBUCCI, *Reflections on Financial Crises, Regulation, and Sunsetting*, *in* SYSTEMIC RISK, INSTITUTIONAL DESIGN, AND THE REGULATION OF FINANCIAL MARKETS (Anita Anand ed., 2016).
228. ROBERT BALDWIN ET AL., REGULATORY STABILITY AND THE CHALLENGES OF RE-REGULATING (Martin Cave ed., 2013) https://www.cerre.eu/publications/regulatory-stability-and-challenges-re-regulating [https://perma.cc/Y35Z-RQFB].
229. *Id*.
230. *See* Pistor, *supra* note 11.
231. *See* Pistor, *supra* note 11.
232. This is borne out in Pistor, *supra* note 11.

left to face the full rigour of the law.[233] The COVID-19 pandemic is, however, exogenous to the financial system in the sense that financial firms are not responsible for its occurrence. Hence, it is unlikely that powerful structures would support legal elasticity towards radical institutional change. Elasticity is posited as temporary for welfarist goals.

However, the objective effects observed are that elasticity does bring to fore questions regarding regulatory objective trade-offs, and normative questions regarding what finance's role is and should be. Is it *right* at the end of the COVID-19 crisis for banks simply to return to an 'enforcement' mode against borrowers? Is this issue only a matter of conduct of business?[234] Would consumer protection require more radical distributive treatment such as debt forgiveness? With prolonged economic uncertainty, these questions cannot be answered satisfactorily with simple resumption of regulatory regimes. Power structures alone may not sustain institutional stability, as bottom-up social demands can exert new pressures due to the longer-term effects of institutional dissonance. One of us has argued that social movements have contributed to a gradual institutional change in corporate regulation.[235] Lothian and Arup have also called for greater socialization of financial regulation objectives in the wake of the global financial crisis.[236] Such a radical re-orientation is not yet seen in the UK, being dominated by an economic paradigm[237] in financial regulation. Post-crisis reforms have only edged closer to macro-level economic perspectives such as financial stability.[238] However, there is a consistent social cry for financial regulation reform such as in consumer welfare.[239] The

233. This is borne out in Pistor, *supra* note 11.

234. Such as 'treating customers fairly' under the FCA's Principles for Conduct of Business. PRIN FCA HANDBOOK, FIN. CONDUCT AUTH. ch. 2 (2020), https://www.handbook.fca.org.uk/handbook/PRIN/2.pdf [https://perma.cc/ST47-BTVL].

235. Iris H-Y Chiu, *An Institutional Theory of Corporate Regulation*, 71 CURRENT LEGAL PROBS. 279 (2018).

236. TAMARA LOTHIAN, LAW AND THE WEALTH OF NATIONS: FINANCE, PROSPERITY, AND DEMOCRACY (2017) on re-orienting the service of finance to the real productive economy instead of a free-market approach; Christopher Arup, *The Global Financial Crisis: Learning from Regulatory and Governance Studies*, 32 L. & POL. 363 (2010).

237. ZANNA ISCENKO ET AL., ECONOMICS FOR EFFECTIVE REGULATION (2016), https://www.fca.org.uk/publications/occasional-papers/occasional-paper-no-13-economics-effective-regulation [https://perma.cc/MMR3-A4DR].

238. MADS ANDENAS & IRIS H-Y CHIU, THE FOUNDATIONS AND FUTURE OF FINANCIAL REGULATION 16–72 (2014).

239. Such as the US Consumer Financial Protection Bureau. The UK FCA was compelled to consider reform to customer protection, *see* Press Release, Financial Conduct Authority, Financial

undercurrents of dissatisfaction with the myopic paradigms of financial regulation may again be raised in the opportunities provided by institutional dissonance.

Financial regulators should deploy legal elasticity with an understanding of its structural nature in accordance with the fully theorized account of Pistor's theory. It should be recognized that some extent of institutional dissonance *will* result, and regulators should give consideration to monitoring the levels of and managing such dissonance. Keeping an open mind allows regulators more fully to appreciate the risks and opportunities in deploying legal elasticity and allows regulators to operate more fully in the intersection between financial regulation and wider public policy goals.

1. Proposal One: Financial regulators should expect institutional dissonance and focus on how to monitor and manage it in terms of public discourse and policy review. Regulators should factor such effects into their decision-making matrix.

We suggest that financial regulators can benefit from an approach of rational, but holistic regulatory decision-making.[240] Such a rational approach can be even more justified in the midst of crisis management where behavioural biases, such as risk aversion and short-termism may dominate perception.

Regulatory decision-making can be grounded in cost-benefit analysis in its broadest terms.[241] This approach allows regulators to anticipate and assess the broadest possible effects of legal elasticity. This approach goes beyond looking to monetary values of benefits and drawbacks in the marketized sense, and seeks to encompass 'hard to value', controversial and subjective evaluations in a holistic way. The evaluative compass is anchored upon the human perspective, including the difficulties in putting a value on social values and preferences.[242] The broad pursuit of such cost-benefit

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Conduct Authority (FCA) Publishes Feedback Statement on Duty of Care (Apr. 23, 2019), https://www.fca.org.uk/news/press-releases/financial-conduct-authority-publishes-feedback-statement-duty-of-care [https://perma.cc/9EL3-TZEC].

240. CASS R. SUNSTEIN, VALUING LIFE: HUMANIZING THE REGULATORY STATE 47–64 (2014).

241. Cass R. Sunstein & Robert W. Hahn, *A New Executive Order for Improving Federal Regulation? Deeper and Wider Cost-Benefit Analysis* (John M. Olin L. & Econ., Working Paper No. 150, 2002), https://chicagounbound.uchicago.edu/law_and_economics/10/ [https://perma.cc/VS2Q-7W88].

242. Cass R. Sunstein, *The Limits of Quantification*, 102 CAL. L. REV. 1369 (2014).

analysis is challenging, as it requires regulators to have a broad scope of information before them[243] and to make dynamic and responsive judgments.

Commentators have criticized regulatory implementation of cost-benefit approaches in regular times as being flawed as they have become narrowly defined,[244] avoiding issues that are difficult to quantify,[245] and highly proceduralized.[246] However, as Wiener[247] argues, cost-benefit analysis need not be practised in narrow, formalistic and meaningless terms.

We encourage regulators to consider broadly and holistically near and longer-term effects and implications when deploying legal elasticity. Opportunities for law reform should not be ruled out. Where regulatory suspensions have mobilized a suite of laws and regulations not inherently thought to be flexible, regulators can consider if more flexibility needs to be built into regulatory systems.[248] The evaluative approach also provides a more robust basis for regulatory accountability.[249]

This leads us to the second proposal, intricately linked to Proposal One. Financial regulators have communicated at great length to their regulated entities to carry out regulatory suspensions and to adhere to the institutional framework, especially in micro-prudential regulation and corporate

243. Jonathan B. Wiener, *Better Regulation in Europe* (Duke Law Sch., Working Paper No. 65, 2006), http://www.osservatorioair.it/wp-content/uploads/2009/08/wiener2006.pdf [https://perma.cc/WGM2-25JN].

244. Mark Harrison, *Assessing the Impact of Regulatory Impact Assessments*, 16 AGENDA 41 (2009), http://ssrn.com/abstract=1906482 [https://perma.cc/XEP9-JP6N] (discussing Regulatory Impact Assessments as being poor in quality and usually not detailed, comprehensive, or fully accountable as to the rationales for introducing regulation.)

245. Julie Froud & Anthony Ogus, '*Rational' Social Regulation and Compliance Cost Assessment*, 74 PUB. ADMIN. 221 (1996) (on the requirement of rationality for exercises of cost-benefit analyses in the UK resulting in analyses that may not fully explain why benefits or costs are quantified in certain manners, especially if social values are at stake which make benefits or costs difficult to quantify. In this manner, we argue that rough quantifications in cost-benefit analyses may not fully capture debatable social values and perceptions that would affect perceptions of cost or benefit.).

246. Christopher Carrigan & Stuart Shapiro, *What's Wrong with the Back of the Envelope? A Call for Simple (And Timely) Benefit–Cost Analysis*, 11 REGUL. & GOVERNANCE 203–12 (2016) (on bureaucrats treating cost-benefit analyses as a formality and chore, and perceiving such analyses as necessary only to justify an already-decided policy).

247. Wiener, *supra* note 243.

248. Heikki Marjosola, *Regulating Financial Markets Under Uncertainty: The EU Approach*, 39 EUR. L. REV. 338 (2014).

249. Cass R. Sunstein, *The Cost-Benefit State* (Coase-Sandor Inst. for L. & Econ., Working Paper No. 39, 1996) (arguing that cost-benefit analyses are a way for state agencies to justify policies and regulations in a manner consistent with economic efficiency, not wasting public resources and not influenced by interest group lobbying. This is consistent with democratic accountability on the part of state agencies.).

transparency in capital markets regulation. Such communications give the impression that, because financial regulators firmly believe in their assumption of institutional stability, the management of institutional dissonance is merely an implementational matter for the regulated entities. In this manner, institutional dissonance can become externalized or 'delegated' to their regulated entities. This leads to hazards in terms of unexpected behaviour on the part of regulated entities and social justice consequences. We argue that regulatory leadership is necessary for managing such 'delegated implementation'.

B. Delegated Implementation by Regulated Entities in Managing Institutional Dissonance

Balancing the policy of relief and rescue, and adherence with existing regulations[250] is challenging. How should banks exercise discretion to either draw down capital and liquidity buffers, when they are uncertain where the bottom-line is, or to make less loan loss provisions, without being certain how much to provision for? The exercise of discretion by banks can become a burden, not a freedom.

At a broader level, this is an archetypical problem of modern regulatory approaches such as meta-regulation[251] where regulators' broad principles and open-ended frameworks are by necessity realized through implementation by firms. Firms cannot be overly prescribed as regulators cannot micro-manage regulatory compliance. However, the breadth of discretion in implementation can lead to firms' cosmetic compliance[252] if firms are not committed to the underlying policy. Firms can also be left to a form of self-regulation if regulators fail to supervise meaningfully.[253] In

250. Letter from Sam Woods, Deputy Governor and CEO of the Prudential Regulation Authority, to Chief Executive Officers of UK Banks, COVID-19: IFRS 9 and Capital Requirements – Further Guidance on Initial and Further Payment Deferrals (June 4, 2020), https://www.bankofengland.co.uk/prudential-regulation/letter/2020/COVID-19-ifrs-9-capital-requirements-further-guidance [https://perma.cc/W33Z-B4LN] (setting out that the PRA is not changing any of its regulatory rules, but firms are to apply them in a manner sensitive to the needs of deferred borrowers in delayed payments for existing loans).

251. CHRISTINE PARKER, THE OPEN CORPORATION: EFFECTIVE SELF-REGULATION & DEMOCRACY (2002); Colin Scott, *Regulating Everything: From Mega- To Meta-Regulation*, 60 ADMIN. 57 (2012).

252. Kimberly Krawiec, *Cosmetic Compliance and the Failure of Negotiated Governance*, 81 WASH. U. L. Q. 487 (2003).

253. *See* Cristie Ford, *New Governance, Compliance, and Principles-Based Securities Regulation*,

the deployment of legal elasticity in credit and capital markets regulation, regulators have tended towards a *greater degree* of leaving to regulated entities and markets to implement legal elasticity. The more regulators assume that institutional stability is not affected by temporary legal elasticity, the more likely a 'delegated' approach will ensue, in the meta-regulatory outworking of legal elasticity. Regulated entities, in managing the uncertainties of institutional dissonance, can engage in undesirable behavioural responses.

First, regulated entities can become excessively risk averse, mindful of the possible boomerang effect of compliance once elasticity recedes. This can explain why the Coronavirus Business Interruption Loan Scheme discussed in Section III did not result in much lending. Second, delegated implementation by the regulated sector can give rise to perverse behaviour to exploit opportunities.[254] It was reported in the UK that private-equity owned companies that were already debt-laden sought to increase debt by turning to government-backed loans. This caused public outcry as private equity backers are seen as exploitative and unwilling to capitalize companies in a manner that may help them become more resilient in the future.[255] These companies would also be competing with others for loan finance, and could unduly deprive other companies from accessing such finance. Third, delegated implementation can also entail behavioural sub-optimality on the part of regulators. Regulators place blame on the regulated sector[256] if social sentiment is unfavourable to their actions.[257]

Legal elasticity often results in reallocations of burden and benefit. The

45 AM. BUS. L. J. 1 (2008) (discussing principles-based regulation in the UK and British Columbia as a form of 'new governance' or 'meta-regulation' where firms are left with detailed implementation of broadly framed regulations ('principles'). Although the need for firms to understand and implement can compel them to internalize compliance as firm culture, there can also be hazards in firms falling short of implementation and not detected by the regulator. In this manner, 'meta-regulation' or new governance approaches need to be supervised and monitored by the regulator.)

254. Kaye Wiggins et al., *Coronavirus: Private Equity's Bailout Moment*, FIN. TIMES (Apr. 23, 2020), https://www.ft.com/content/f7cc82d7-70b9-40c3-b4a0-815ebc5d99d5 (last visited Aug. 20, 2020).

255. Michael Kirkham, *Should the World Worry about America's Corporate-Debt Mountain?*, THE ECONOMIST (Mar. 14, 2019), https://www.economist.com/briefing/2019/03/14/should-the-world-worry-about-americas-corporate-debt-mountain (last visited Aug. 20, 2020).

256. Bridget M. Hutter & Sally Lloyd-Bostock, *Risk Regulation and High-Profile Disasters: Regulatory Crisis as a Distinct Phenomenon*, *in* REGULATORY CRISIS: NEGOTIATING THE CONSEQUENCES OF RISK, DISASTERS AND CRISES 1–32 (2017).

257. *See* Elke U. Weber, *Understanding Public Risk Perception and Responses to Changes in Perceived Risk*, *in* POLICY SHOCK: RECALIBRATING RISK AND REGULATION AFTER OIL SPILLS,

dangers of delegated implementation for distributive consequences are: (a) welfare outcomes may be attributed to regulated entities' actions, putting them in a difficult position in balancing their private decision-making, the needs for regulatory compliance and the part they play in the public policy of 'relief and rescue'; and (b) the roles of regulators and policymakers may become ambiguous even though welfare outcomes that result are essentially matters of public interest.

Distributive judgments implicate private capacities[258] as well as public institutional structures, in relation to the nature of the Lockean social contract in politics. The rise of the risk society[259] and welfare state in Western developed countries,[260] poses the question whether consumers should be favoured in terms of protection, relief and welfare, and under what circumstances should the operation of market forces be regarded as optimal.[261] Even in an institutional context, there can be redistributive consequences. The adjustments to mandatory disclosure for securities offerings in emergency fund-raising by corporations discussed in Section IV have redistributive consequences in terms of reducing cost for companies, but potentially increasing opacity cost for investors.

Financial regulators should engage continuously with the regulated sector carrying out the delegated implementation of legal elasticity. Further, supervisory steering is needed in light of behavioural developments that may be unexpected. Policy steering would be needed for broader implications of welfare outcomes that are mixed matters of private and public interest. Legal elasticity has to be managed *relationally*, with those

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NUCLEAR ACCIDENTS AND FINANCIAL CRISES (Edward J. Balleisen et al. eds., 2017); Thomas A. Birkland & Megan K. Warnement, *Focusing Events, Risk, and Regulation*, *in* POLICY SHOCK: RECALIBRATING RISK AND REGULATION AFTER OIL SPILLS, NUCLEAR ACCIDENTS AND FINANCIAL CRISES (Edward J. Balleisen et al. eds., 2017).

258. Sebastián Fleitas, Price Fishback, & Kenneth Snowden, *Forbearance by Contract: How Building and Loans Mitigated the Mortgage Crisis of the 1930s* (Nat'l Bureau Econ. Rsch., Working Paper No. 21786, 2015), https://www.nber.org/system/files/working_papers/w21786/w21786.pdf [https://perma.cc/SFJ3-FHH2] (explaining how private lenders exercised forbearance in the historical study of the US mortgage crisis of the 1930s. This was due to borrowers themselves being members of building societies and voting in favour of forbearance. Forbearance provided the needed time for many borrowers to repay their loans. This resulted in an avoidance of many bankruptcies and a net increase in welfare.).

259. ULRICH BECK, RISK SOCIETY: TOWARDS A NEW MODERNITY (1992).

260. RICHARD ROSE & REI SHIRATORI, THE WELFARE STATE: EAST AND WEST (1987); CLAUS OFFE, MODERNITY AND THE STATE: EAST, WEST (1996).

261. Fleitas et al., *supra* note 258.

tasked to implement it, as well as those likely to be affected by or interested in the outcomes of implementing legal elasticity.

1. Proposal Two: Consistent with a pro-active approach to monitoring and managing institutional dissonance entailing from legal elasticity, regulators should engage in relational frameworks, proactively with their regulated entities, also extending to other agencies and stakeholders.

The relational management aspects of legal elasticity include:

(a) The relationships amongst financial regulators, relevant agencies and policymakers;[262]

(b) The relationships between regulated entities and regulators; and

(c) The relational dimension between regulators, policymakers, stakeholders or society more broadly, as crisis management benefits from multi-stakeholder participation and drawing together of resources,[263] social mobilisation and solidarity.

One of the lessons from the global financial crisis for financial regulators was the need to coordinate amongst each other. In the UK, crisis management must be coordinated between the Treasury, BoE, and PRA in respect of financial stability and public interest needs.[264] As the reform was inspired by the last crisis relating to financial instability, the FCA was excluded due to a lack of perception of business conduct as being contributory to these objectives.[265] However, the global financial crisis was quickly followed by business conduct scandals in the banking industry.[266]

262. *See* Charles Baubion, *OECD Risk Management: Strategic Crisis Management* (Org. for Econ. Co-operation & Dev., Working Paper No. 23, 2013), https://www.oecd-ilibrary.org/docserver/5k41rbd1lzr7-en.pdf?expires=1604031030&id=id&accname=guest&checksum=7EB1224E43DD96F83319398C2F189A91 [https://perma.cc/EC8W-Y3WR].

263. Black, *supra* note 33, at 114–15.

264. Financial Services Act 2012 §§ 64-65 (U.K.).

265. Niamh Moloney, *The Legacy Effects of the Financial Crisis on Regulatory Design in the EU*, *in* THE REGULATORY AFTERMATH OF THE GLOBAL FINANCIAL CRISIS 111–202 (Eilís Ferran, Jennifer Hill, Niamh Moloney & John C. Coffee eds., 2012).

266. The LIBOR manipulation scandal and mis-selling scandals such as the UK London and Capital Finance unregulated product mis-selling scandal, *see Timeline: Libor-fixing scandal*, BBC NEWS (Feb. 6, 2013), https://www.bbc.co.uk/news/business-18671255 [https://perma.cc/PZM9-JTFJ]; Francesca Washtell, *Thirteen businessmen including a former energy minister being sued for £178m to recover cash lost by victims in London Capital & Finance scandal*, THIS IS MONEY UK (Sept. 4, 2020,

In practice, the PRA and FCA closely coordinate policies and actions, such as in the management of the COVID-19 crisis.

Although the regulated-regulator relationship is fraught with lobbying, informal 'capture or sympathy'[267] or excessive trust (especially before the global financial crisis),[268] it remains imperative that regulators maintain informational and supervisory proximity to the regulated. Omarova argued, in the wake of the global financial crisis, that a system of tripartite financial regulation should be introduced where 'bankers' and 'bureaucrats' would enrol 'guardians' who are stakeholders representing public interest to co-govern in financial regulation.[269] Such a multipartite form of networked governance has always been envisaged in regulatory theory.[270] Perhaps there is fear that diverse demands from multiple stakeholders may confuse the policy agenda. However, excluding voice or dialogue at a time of crisis-management does not necessarily lead to more effective policy decisions. In Section IV, the FCA and the PEG legitimized the waiver of pre-emption rights for capital-raising by companies, showing the importance of catalysing influence on the part of non-public sector stakeholders. However, there may be an issue regarding how stakeholders are selectively engaged by regulators for the purposes of crisis management. An example of a more open multistakeholder dialogue during the COVID-19 crisis is the UK Business, Energy and Industrial Strategy Committee's (BEIS) channel for feedback from the business sector in relation to the impact of the virus and the needs of various parties.[271] While such a channel is open to the public, this does not prevent the Committee from engaging selectively with

4:57 PM), https://www.thisismoney.co.uk/money/markets/article-8698829/Now-13-face-court-London-Capital-Finance-scandal.html [https://perma.cc/EE8N-KLZP].

267. Edward Baxter, *Capture in Financial Regulation: Can We Channel It Toward the Common Good?*, 21 Cornell J.L. & PUB. POL'Y 175 (2011).

268. LORD A. TURNER, FIN. SERVS. AUTH., THE TURNER REVIEW: A REGULATORY RESPONSE TO THE GLOBAL BANKING CRISIS 39–49 (2009), http://www.actuaries.org/CTTEES_TFRISKCRISIS/Documents/turner_review.pdf [https://perma.cc/FQ93-YYWH].

269. Saule T. Omarova. *Bankers, Bureaucrats, and Guardians: Toward Tripartism in Financial Services Regulation*, 37 J. CORP. L. 621 (2012).

270. Black, *supra* note 33; Julia Black, *Mapping the Contours of Contemporary Financial Services Regulation*, 2 J. CORP. L. STUD. 253 (2002).

271. Business, Energy and Industrial Strategy Committee, *The Impact of Coronavirus on Businesses and Workers: Inquiry*, UK PARLIAMENT, https://committees.parliament.uk/work/178/the-impact-of-coronavirus-on-businesses-and-workers/ [https://perma.cc/K5JL-MEZS].

respondents in further dialogue.

C. Preparation for Crisis Management and Legal Elasticity

Finally, if legal elasticity is to become an integral part of crisis management for financial regulators, regulators need to engage with it in an *ex ante* and sustained manner. Regulators should have a pre-crisis framework for thinking about the scope of and possibilities relating to legal elasticity.

1. Proposal Three: Financial regulators should have a pre-crisis framework for crisis management, including deploying legal elasticity, as this goes some way towards the ex post management of institutional dissonance.

Regulators should have a dedicated outfit for pre-crisis preparation, and wisdom may be borrowed from scenario planning literature in business management. Oliver and Parrett[272] argue that the more dynamic and unpredictable a business environment may be, the more a business needs to engage in scenario planning. Scenario planning allows business leaders to take stock of information and possibilities in a holistic manner, and consider the existing suite of tools in imagining responses.

In a similar vein, pre-crisis preparation on the part of regulators can incorporate useful elements from scenario planning. Regulators already have access to significant amounts of market and regulated information,[273] a development since the global financial crisis.[274] Such information should also be regularly shared amongst networked regulators and policymakers discussed in Proposal Two.[275]

Next, regulators should model deploying crisis management tools and

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272. John J. Oliver & Emma Parrett, *Managing Future Uncertainty: Reevaluating the Role of Scenario Planning*, 61 BUS. HORIZONS 339 (2018).

273. Iris H-Y Chiu, *Transparency Regulation in Financial Markets- Moving into the Surveillance Age?*, 2 EUR. J. RISK REG. 305 (2011).

274. Stijn Claessens & Laura Kodres, *The Regulatory Responses to the Global Financial Crisis: Some Uncomfortable Questions*, *in* POLICY SHOCK: RECALIBRATING RISK AND REGULATION AFTER OIL SPILLS, NUCLEAR ACCIDENTS AND FINANCIAL CRISES 435 (Edward J. Balleisen et al. eds., 2017).

275. THOMAS H STANTON, WHY SOME FIRMS THRIVE WHILE OTHERS FAIL: GOVERNANCE AND MANAGEMENT LESSONS FROM THE CRISIS 43–66 (2012); for information exchange and dialogue between policy-makers and regulators, refer to discussion under Proposal Two.

legal elasticity. Maymin argues that regulators need to be aware that the timing and duration of their interventions can promote regularization of dysfunctional markets but can also distort markets. [276] Regulators should enhance their preparedness in considering scenarios where legal elasticity may be needed. Crawford argues that although regulators cannot prepare for the exact types and extents of crises that occur, training intuitive judgment by a 'wargaming' approach is beneficial. [277] This is similar to stress-testing that regulators carry out for systemically important banks and financial institutions.[278]

CONCLUSION

The COVID-19 crisis has severely impacted economic activities globally, precipitating wide-ranging policy responses. A crucial piece of the mosaic in the policy response comes from financial regulation, as financial regulators adjust regulatory rules in order to allow the financial sector to meet the policy goals of 'rescue and relief.' By studying the UK's policies and experience, we argue that regulatory suspensions introduced by financial regulators obscure hazards to regulators, regulated financial entities, as well as households and corporations, and may fall short of the welfarist goals desired. This is because such regulatory suspensions affect institutional stability to different extents. We situate the deployment of regulatory suspensions within the theoretical framework for legal elasticity developed in Pistor's legal theory of finance, and argue that the very legal nature of elasticity is structural in nature. Regulators need to confront the structural nature of legal elasticity to avoid greater hazards to legal certainty, institutional stability, and ultimately policy outcomes.

We make a series of recommendations to improve financial regulators' decision-making processes. First, we propose that regulators should anticipate that institutional dissonance follows from deploying regulatory

276. Philip Maymin, *Regulation Simulation*, 2 EUR. J. FIN. & BANKING RES. 1 (2009).

277. John Crawford, *Wargaming Financial Crises: The Problem of (In)Experience and Regulator Expertise*, 34 REV. BANKING & FIN. L. 115 (2014–15).

278. Basel Committee on Banking Supervision, *Principles for Sound Stress Testing Practices and Supervision,* BANK INT'L SETTLEMENTS (May 2009), http://www.bis.org/publ/bcbs155.pdf [https://perma.cc/2JHG-2LQB]; Mario Quagliariello, *Macroeconomic Stress-testing: Definitions and Main Components*, *in* STRESS-TESTING THE BANKING SYSTEM: METHODOLOGIES AND APPLICATIONS (Mario Quagliariello ed., 2009).

suspensions and should proactively seek to evaluate all relevant aspects pertaining to institutional stability and change. Second, regulators should engage constructively in relational paradigms with relevant public sector agencies, regulated entities, and broader stakeholders in order to monitor and supervise the outworking of legal elasticity. Third, regulators should put in place *ex ante* frameworks for preparing for crisis management and the potential use of legal elasticity.