Client Alert | **Newsflash** | Financial Institutions Advisory

COVID-19 FAQ 6: Are there restrictions on capital distributions?

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This FAQ is intended to provide financial institutions with an overview of the restrictions in place on capital distributions in various jurisdictions.

As the impact of the COVID-19 crisis continues to develop for banks and insurers, regulators are reminding firms to pay attention to capital maintenance and ensure that sufficient reserves remain available. At a European supervisory level, the European Banking Authority ("EBA") has called for banks to temporarily suspend all discretionary dividend distributions and share buybacks aimed at remunerating shareholders. This call to action stems from the EBA's concern that capital should be used "*for ensuring continuous financing to the economy*" during the crisis.

Likewise, the European Insurance and Occupational Pensions Authority ("EIOPA") has issued the same request to (re)insurers, noting that it is *"essential to ensure the access to and continuity of insurance services, safeguarding the ability of the insurance sector to continue to perform its role as risk transfer mechanism from citizens and businesses and its capacity to mobilize savings and invest them in the real economy."* Both supervisors have also encouraged prudence and discretion when paying out variable remuneration to senior managers and risk-takers.

These requests were echoed with force at the UK level and across some EU Member States, with a number of major European and UK banks and insurers in effect required to confirm their intention to comply. However, some market participants have expressed concern with this approach, particularly given the knock-on effect to pension funds and individual investors with cornerstone investments in insurance firms.

No formal restrictions have been put in place in the US, and indeed, regulators have taken steps to ensure that automatic limitations on capital distributions triggered where a bank lends into its capital buffers (as they have been encouraged to do) will apply more gradually.

Are there restrictions on capital distributions?

Jurisdiction	Restrictions on capital distributions
United States	No formal restrictions on capital distributions have been put into place. Regulators have acknowledged that banking organizations could face future restrictions on capital distributions if they lend into their capital buffers, as they have been encouraged to do, in an effort to make credit available to households and businesses affected by COVID-19. To incentivize such lending, the agencies have redefined "eligible retained income" as used in their capital rules, and the Federal Reserve has made a corresponding change to its total loss-absorbing capacity (the "TLAC") rule. These rule changes maintain the automatic limitations on capital distributions under the capital and TLAC rules, but seek to make their application more gradual so that a banking organization is less likely to be subject to abrupt and restrictive distribution limitations following a period in which it lends into its buffers in response to the pandemic. Our alert discusses these changes.
European Union	In a recommendation, the ECB has asked banks not to pay dividends or buy back shares until at least October 2020. The Recommendation concerns dividends for 2019 and 2020. Similarly, EIOPA has also urged that (re)insurers temporarily suspend all discretionary dividend distributions and share buybacks aimed at remunerating shareholders. *See*: EBA statement and EIOPA statement
United Kingdom	Yes, by way of non-legislative supervisory request. Banks: Following a series of published letters to the UK's largest systematically important UK deposit-takers (HSBC, Nationwide, Santander, Standard Chartered Bank, Barclays, RBS, Lloyds Banking Group), the PRA publicly welcomed the decisions by the boards of these banks to suspend dividends and buybacks on ordinary shares until the end of 2020, and to cancel payments of any outstanding 2019 dividends. The PRA also expects banks not to pay any cash bonuses to senior staff, including all material risk takers, and otherwise to take an appropriate approach to administering variable remuneration. Insurers: The PRA has also written to UK insurers on the specific topic of profit distributions, reminding them to manage their financial resources prudently, and of a specific pre-existing supervisory expectation of the PRA to the effect that, when deciding on distributions, boards should satisfy themselves that each distribution is prudent and consistent with their risk appetite. *See*: PRA statements banks/insurers
France	According to clear direction from the ACPR, preservation of capital resources to support the economy and/or absorb losses should be given priority at this time over the distributions of dividends and share buybacks. Therefore, the ACPR invites credit institutions under its direct supervision, and financing companies, to ensure, at least until October 2020 that: • no dividends are paid and no irrevocable commitment to pay dividends is made for the years 2019 and 2020; and • no share buybacks to remunerate shareholders take place. The ACPR also invites insurance companies under its supervision, at least until October 2020, to ensure that no dividends are paid and to exercise moderation in the policies for awarding variable compensation.

Jurisdiction	Restrictions on capital distributions
	Credit institutions, insurance companies and financing companies that would not be in a position to defer the payment of dividends because they consider themselves legally obliged to do so, should immediately explain the reasons for this to the ACPR.
Germany	In line with the EBA guidance, the German Federal Financial Supervisory Authority ("BaFin") expects that financial institutions should refrain from buying back shares and carefully consider dividend payments, profits and bonuses. However, it does not currently consider a blanket distribution ban for insurance companies and pension funds. *See*: BaFin statement
Italy	The Bank of Italy has adopted the EBA's guidance that no cash payouts and buybacks are carried out until October 1, 2020 and applied it to non-systemic banks. Equally, the Italian insurance supervisory authority ("IVASS"), in line with the EIOPA guidance, stated that Italian insurance companies should follow prudent dividend and other distribution policies.
Spain	No restrictions other than those recommended at EU level. The Bank of Spain is aligned with, and has been a part of, EU recommendations but has no imposed specific legal restrictions in this respect.
Sweden	No legal restrictions have been imposed. However, the Swedish regulator has made statements to the effect that any relaxation of capital requirements for banks shall not be used to make capital distributions or share buybacks. The Swedish banks are generally following the ECB recommendation for banks not to declare dividends under the current circumstances. Additionally, participation in certain support schemes may potentially restrict capital distributions.
Belgium	No restrictions other than those recommended at the EU level.
UAE	No restrictions.

Our FIA team has developed the ***COVID-19 Regulatory and Legislative Dashboard*** *as a resource to help affected financial institutions, companies, governments and individuals navigate the local and cross-border complexities of the crisis and the policy response. Please refer to the Dashboard for our periodic updates and insights on the issues addressed in this FAQ.*

Find out more about the business response to the Coronavirus outbreak: ***Coronavirus: Managing business impact and legal risks***.

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