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Editors' Note

Welcome to the Fall 2020 edition of the *Stanford International Policy Review* (Volume 5, Issue 2). This issue features work addressing the theme of Inflection Points, offering insightful policy analysis of our turbulent and changing geopolitical landscape. The theme was inspired by the COVID-19 pandemic, the Black Lives Matter movement and other global justice movements, and declining trust in political institutions. During the editorial cycle, the United States weathered a historic presidential election and an unprecedented attack on the U.S. Capitol. These events, alongside a host of international developments, further underscore the urgent need for policymakers to begin identifying and reflecting on the challenges and opportunities of shaping the way forward.

Against this backdrop, SIPR's authors present an array of policy suggestions and reflections, among them analyses on the unmet promises for transitional justice in Mexico during the Andrés Manuel López Obrador administration and the impacts of the end of "One Country, Two Systems" on Hong Kong's property law and the autonomy of its people. SIPR continues to balance academic and practitioner perspectives, serving as a bridge between the two communities. In particular, we are thrilled to feature commentary from William Perry Research Fellow at Stanford's Center for International Security and Cooperation and former U.S. ambassador to Ukraine Steven Pifer on prospects for the U.S.-Ukraine relationship under the new Biden administration. Finally, to reach a broader range of audiences, the SIPR editorial board is also pleased to announce the launch of the SIPR Forum, the digital companion to the Stanford International Policy Review, which publishes cutting-edge analyses of timely and relevant issues in international affairs in the form of short articles and opinion pieces.

The editorial board hopes you will enjoy the contributions and critically engage with the policy questions they grapple with. In closing, we would like to thank our advisory board, the Master's in International Policy program, and the Office of the Vice Provost for Graduate Education for their continued support.

Kelsi Caywood and Adriana Stephan
Editors-in-Chief, SIPR
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Relief and Rescue
Financial Regulatory Suspensions in the United Kingdom

By Iris H-Y Chiu, Andreas Kokkinis, and Andrea Miglionico

I. Introduction

This introduction provides an overview of the context in which financial regulators in the United Kingdom responded to extraordinary financial needs from the outset of the COVID-19 pandemic. We provide a brief introduction to policies of "relief" and "rescue" supported by financial regulatory suspensions and a roadmap to the rest of the article.

The outbreak of the COVID-19 pandemic severely impacted economic activity as governments imposed lockdowns in many countries.[1] In the UK, fears of widespread contagion and risk to public health caused the government to announce a lockdown of society and the economy.[2] Business activity has been adversely affected in many sectors[3] and in April 2020, economic output fell by at least 20 percent compared to the same period in the previous year.[4]

The financial implications of the economic lockdown were immediate as the corporate sector is heavily financialized.[5] The freezing of business activity in many sectors has implications for corporations' cash flow, servicing of debt, potential insolvency and, hence, their market valuation and credit rating assessments. Besides public finance packages for emergency help, such as furloughing,[6] policymakers have turned to private sector finance to alleviate the financial stresses and hardships caused to households and corporations. In other words, private sector finance is being relied on, to a significant extent, but not exclusively, 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 are exacerbated in the weak economic conditions during the pandemic. "Rescue" refers to facilitating the access of corporations to finance to keep them afloat in relation to expenses, losses, and shoring up for the future.

These policies are similar 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 obligations applicable to their regulated entities. Regulatory suspensions may, at first blush, be regarded as temporary, and we may expect regulatory resumption once the crisis of the pandemic fades. However, we argue that more permanent institutional change may occur, based on the theoretical positioning of regulatory suspensions within the legal theory of finance.[11]

Regulatory suspension can be seen as one of the ways the "elasticity" of law is realized in order to cater to wider political, social and economic needs.[12] Legal elasticity is posited in Pistor's legal theory of finance,[13] showing when suspensions of laws and regulations may occur under extraordinary circumstances such as financial crises. We situate the regulatory suspensions introduced by UK financial regulators during the COVID-19 crisis within the theorization of legal elasticity. Reis and Vasconcelos[14] argue that such elasticity is institutionally supported based on the expected macro-economic behaviour of agents in markets, and empirical evidence also offers support for the *ex post* efficiency and welfare effects of certain suspensions, in private law agreements such as debt moratoria.[15] Carruthers[16] characterizes contractual suspensions as "financial decommodification" that is necessary when markets are temporarily dysfunctional.

In Pistor's legal theory of finance, law is central for constructing finance; hence, legal elasticity is resorted to when existing law is no longer able to meet overarching policy goals such as financial stability.[17] This theorization, drawn largely from observations during the global financial crisis of 2007-09,[18] depicts law in an instrumental sense and bound up with power structures that influence legal change, but also treats law in a structural sense.[19] Hence, legal elasticity may not avoid structural effects, such as institutional dissonance and change. In this manner, regulatory suspensions in the UK should be perceived as 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. This will help mitigate the unintended and adverse consequences that regulatory suspensions may entail, which could ultimately undermine the public policy goals of relief and rescue. Further, the impression that regulatory suspensions in financial law and regulation are only short-lived is difficult to sustain, with extensions having already been made to them.[20] Our study, although focused on the UK, offers lessons and insights for developed financial jurisdictions that embarked on financial regulatory suspensions.[21]

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. However, as Sections III and IV illustrate, the application of legal elasticity to credit laws and regulation, and capital markets regulation respectively, has resulted in a number of unanswered questions and unintended consequences, including hazards to regulators, banks, markets, and the intended beneficiaries themselves, i.e., households and corporations. We call for a fully theorized understanding of legal elasticity and caution that financial regulators' deployment of regulatory suspensions risks bringing about hazards resulting from the failure to situate such suspensions within the fully theorized framework for legal elasticity.

In Section V, we argue 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 proposals for the key aspects of these frameworks. This contribution assists in framing legal elasticity not only as a crisis management regulatory tool but also as a general regulatory tool pursuant to a modern and broad understanding of regulatory responsiveness.[22]

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 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, and legal elasticity in those areas may have to be theorized in a different manner. We do not discount the possibility that other regulatory "enterprises"[23] can benefit from this study, but we do not claim direct applicability within the confines of this article. Section VI concludes.

II. Legal Elasticity in Financial Regulation

Legal elasticity is argued to be a function of the legal theory of finance posited by Pistor.[24] The legal theory of finance frames finance in legal terms, as financial transactions and obligations are constructed as legal structures in order to work as intended. In particular, the theory constructs finance as being underpinned by the crucial qualities of certainty and enforceability that law supplies. However, in the global financial crisis, it was observed that the very qualities of certainty and strict enforceability of financial obligations and transactions in various markets would collectively lead to systemic risk, such as collective fire sales of financial assets.[25] As such, the solution is also found in law, i.e., to resort to legal elasticity in order to suspend and mitigate the adverse impacts driven by law, to meet the needs of crisis management.

In this theoretical framework, it can be argued that legal elasticity served an unwinding purpose, i.e., 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 regulation as such, even when it appears that the application of an existing law or regulatory instrument has run its course, as legal elasticity entails institutional change and paves the way for law reform.

The above conceptualization of legal elasticity in finance portends of impending institutional change from the previous law. Indeed, it can be argued that the post-crisis reforms to the banking and financial sector reflected this conceptualization of legal elasticity. Where banks had been unable to absorb their losses during the global financial crisis, legal elasticity was applied so that regulatory discipline was not meted out to them for being inadequately capitalized. Instead, many jurisdictions bailed out their banks by injecting state capital[26] and then proceeded to reform capital rules to tie banks to higher and more robust levels of capitalization for loss absorption.[27] In the UK, government intervention prevented the full force of insolvency law from applying to banks in crisis,[28] leading to subsequent development of a bespoke bank crisis management and resolution regime in many jurisdictions.[29]

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. 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.[30] Regulators constructed an increasingly prescriptive regime for prudence[31] and conduct[32] by banks and financial institutions—and therefore also specifically carved out particular measures of inherent flexibility that can be adjusted.[33] This juristic development suggests that legal elasticity in finance may have been theoretically enriched by the provision of *ex ante* 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 achieve legal elasticity 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.[34] In the post-crisis regulatory regime which appears comprehensive, *ex post* exercises of legal elasticity continue to be necessary, such as in relation to crisis management. 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 capable of taking effect in different degrees along a spectrum of institutional stability and disturbance, or would legal elasticity necessarily entail more structural considerations of institutional dissonance and change?

We suggest that, just as the application of legal elasticity during the global financial crisis paved the way for structural changes in financial regulation, the application of legal elasticity by UK financial regulators during the COVID-19 pandemic may also bring about the same trajectory. Further, the structural effects of legal elasticity may be along a spectrum of intensity of institutional impact. Such a spectrum 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,[35] and regulators have no appetite for major institutional changes. Further, the COVID-19 crisis can be regarded as a crisis exogenous to the financial sector, and crisis management is therefore not perceived as entailing existential consequences for either the substance of laws/regulations or regulators. Many jurisdictions are also keen to emphasize that lockdowns adversely affecting economic activities are temporary,[36] although no one has a sense of certainty as to how temporary these are.

We argue that 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 is fundamental to effective financial regulatory policy in supporting the broader relief and rescue agenda, and 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 and by regulators more generally. More general application of legal elasticity as a regulatory tool can be theoretically anchored in responsive regulation.[37] Although Ayres' and Braithwaite's work on "responsive regulation" was most famous for its enforcement pyramid and the creative options regulators have for engaging regulated entities in securing compliance, it more broadly redefined the nature and directions for modern regulation.[38] It provides a vision of regulatory dynamism not only for substantive purposes[39] but also for purposes relating to regulatory participation,[40] processes,[41] and implementation,[42] breathing new theoretical life into procedural aspects of regulatory genesis and outworking. Legal elasticity, if regarded as an extension of the responsive regulatory paradigm, can provide a fuller and richer basis for regulators to engage with dynamic regulatory goals, tools, and processes. We argue in Section V that the theoretically informed understanding of legal elasticity in terms of its structural nature can help regulators make decisions in regulatory suspensions in a more robust manner.

III. Regulatory Suspensions in Credit Laws And Regulation: Advancing "Relief And Rescue" in the UK

During the COVID-19 crisis in the UK, a key policy concern has been how credit arrangements would affect households and corporations that are in debt and/or need financing by debt in order to meet financial needs during the challenging period. Regulatory suspensions were made by the PRA and FCA,[43] and specific legislation for business debt was passed.[44]

First, regulatory suspensions are made to allow borrowers, both households and corporations battered by lockdowns, to enjoy temporary relief from the pressures of debt while regrouping themselves during the crisis. Second, the suspensions facilitate access to finance and credit to business borrowers during a period where banks may be risk-averse to lend more. This would help businesses avoid inflicting knock-on effects upon their suppliers and needing to introduce massive redundancies.[45] As the FCA has a consumer protection mandate,[46] measures on personal finance were rapidly introduced from the early stages of the pandemic.

In order to achieve the two effects above, certain suspensions from financial regulation had to be implemented. These are discussed in Parts A and B in this section. We first consider how regulators looked first to financial regulatory measures that are inherently flexible. This provided a starting point for regulatory suspensions.

The macro-prudential regulator in the UK, the Bank of England's Financial Policy Committee (FPC), has oversight for the systemic health of the financial system,[47] and to this end is able to exercise an inherently flexible power to adjust a prudential regulatory measure known as the countercyclical buffer (CCyb). The exercise of this power is supported by the PRA which oversees banks' prudential compliance with all capital requirements, including the CCyb. The CCyb was introduced in the wake of the global financial crisis as a measure to allow the macroprudential regulator to impose capital cost on banks to dampen pro-cyclical creation of debt.[48] If the macroprudential regulator, who is responsible for surveying financial market trends,[49] takes the view that asset prices are rising excessively and markets may be overconfident about leverage and asset prices, the introduction of the CCyb would make it more costly for banks to extend credit. This measure plays a part in moderating financial institutions' behaviour and markets' tendencies towards a cycle of Minskian instability.[50] 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 there was a risk that banks could be overly optimistic and engage in excessively liberal lending. This was abruptly adjusted to 0% during the COVID-19 crisis,[8] freeing up for banks an estimated capital cost of £190bn.[51]

The regulatory elasticity in the CCyb reflects inherent flexibility in the prudential regulation of banks to adjust banks' incentives according to regulatory capital cost. Masur and Posner (2017)[52] argue that such regulation is designed to address the need for financial regulators to shape the incentives of financial actors that are inherently biased towards procyclicality, in order to moderate potential market excesses that are not self-correcting. In downturns, as has been 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 sub-optimal market behaviour. This downward adjustment is aimed at incentivizing banks to engage in more lending since capital cost for credit is significantly reduced with the removal of the CCyb's constraint.

Freeing up the cost of capital originally imposed by the CCyb does not, however, automatically result in more lending either. During the COVID-19 crisis, borrowers' creditworthiness would be difficult to discern due to the uncertainties of their circumstances, such as future income and employment of individuals, or volatility of business revenues for corporations, as affected by wider economic conditions. Banks may be behaviourally inclined to refrain from lending more. Behavioural tendencies such as risk aversion and impediments to efficient markets such as acute information asymmetry may result in capital hoarding instead.

Hence the PRA and FCA introduced a raft of measures in addition to the inherently flexible measure of the CCyb to steer more precise actions on the part of banks. This means suspending other regulations not inherently thought to be flexible to send stronger incentive-based messages to banks. We examine the bundling of inherently flexible and unexpected legal elasticity, targeted at the immediate needs of loan forbearance as well as borrowing. We argue that such legal elasticity inevitably gives rise to more fundamental issues and institutional dissonance, and it would be difficult to merely regard such elasticity as temporary and that reversion to "normal" would take place in due course. We argue that the deployment of legal elasticity necessarily entails considerations of what could become the "new normal" on the part of policymakers. This is not to discourage policymakers from deploying legal elasticity, but they should be prepared to address consequential effects of regulatory suspensions in a manner that would result in broader institutional robustness and social justice[53] in due course.

A. Regulatory Package Aimed at Relief for Borrowers

First, regulatory suspension is made in relation to consumer credit taken out by household borrowers. The FCA introduced periods of deferred payment, known as loan payment holidays, for consumer credit products it regulates. As the FCA does not have regulatory perimeter over business lending, an Act of Parliament was passed to give temporary relief for business borrowers.[54]

For households, the FCA has introduced rights for mortgage, credit card, motor finance consumers, and unsecured personal borrowers to defer their payment obligations by making a request to their respective lenders. Lenders are not to conduct diligence investigations into the affordability of such requests and should grant them as a matter of course.[55] This measure does not affect the accrual of interest on the loan and firms are not required to investigate the individual circumstances of each customer who makes a request for such a payment holiday or extension. The balance achieved in this measure is that customers are not imposed with burdens to prove that they can afford a payment holiday, given that their personal economic circumstances may be in flux anyway. At the same time, banks are not asked to forego their expected earnings on these assets in due course. In cases where a customer is already in default at the commencement of the guidance, the guidance prevents firms from commencing or continuing repossession proceedings and any possession order already made must not be enforced. Higher risk short-term credit borrowers have also been granted deferred payment.[56] However, with the second lockdown, the FCA has extended the timeframe for customers who have yet to make deferral requests to do so, but limiting the number of periods for deferred payments for those who have already made such requests.[57] Overall, no customer would be able to defer debt payments for more than two periods of deferral, which is six months in total.

As business lending is not regulated by the FCA, a fast-tracked piece of legislation has been passed to allow companies with debt obligations to apply for a moratorium. Directors can make such an application if they are of the view that the company is unable to pay its debts. They however need to appoint an insolvency practitioner as "monitor" to verify that rescue for the company is possible.[58] A successful application for moratorium allows the company to enjoy relief from its debt obligations, except specified obligations such as rent and employees' wages, for an initial 20 days with a possible extension for another 20 days.[59] During the period of the moratorium, no insolvency proceedings can commence against the company. It is envisaged that this period will be used for the company to seek arrangements with its creditors or explore avenues of raising finance.

Temporary relief from debt has immediate implications for creditors such as banks. Should banks treat the outstanding obligations as being in default or as prospects for increased default risk at least? This has knock-on effects on banks' balance sheet strength, and they would need to conserve capital, or worse, raise capital themselves, to shore up against credit risks. In this manner, payment holidays would be contrary to banks' ability to lend or help their borrowers. A suite of bank regulation suspensions has therefore been introduced by the PRA, working in tandem with the FCA.

The PRA clarifies[60] that banks should not treat deferred payments as being in default. Even if deferred payments are not able to resume promptly, whether they should be treated as impaired assets or not should not be mechanistic, but subject to the understanding of individual financial situations. This clarification meets two purposes. One is to protect borrowers from relentless enforcement. The other is to protect banks from the sudden blow to their balance sheets, and the need to ensure that they have sufficient capital to absorb losses. To achieve the latter, the PRA allows ambiguity in whether deferred borrowers are in default, and this ambiguity extends to ambivalence in treating deferred borrowers who have not yet defaulted as poor credit risks.

After the global financial crisis of 2007-09, it was thought important to inculcate prudential behaviour in banks by subjecting them to conservative measurements of their borrowers' creditworthiness in order to have sufficient loss-absorbing capital in place. The accounting standard IFRS 9 requires banks to account for debt instruments at fair value.[61] Changes in fair value have to be reported in the profit and loss account, e.g., a reduction in fair value is registered as a loss. Banks are thus required to make loan loss provisions and ensure that they have sufficient capital to absorb these potential losses. This is an example of a forward-looking approach for prudential treatment and supervisory reporting adopted in the aftermath of the global financial crisis[62] aimed at correcting the behaviour of delayed loss recognition by banks before the crisis.

Payment holidays exacerbate information asymmetry for banks in relation to borrowers' creditworthiness, and banks may indeed make increased loan loss provisions against outstanding debt,[63] paddling back against the capital liberation that has been offered. The application of IFRS 9 during the pandemic crisis would inevitably lead to a significant increase in expected credit loss provisions and hence a contraction of the ability of banks to grow their balance sheet by lending. Hence, the PRA had to moderate banks' above tendencies by clarifying[64] that deferred payments under the COVID-19-induced payment holidays should not necessarily be treated as expected credit losses that warrant capital provision against them. Banks should use reasonable and balanced information and assumptions to assess their borrowers. Borrowers for example may be assessed on the basis of whether loans may be past due for 90 days instead of the narrower test of 30 days.[65] Although the PRA does not wish to undermine the prudent regulatory regime that has been reformed since the global financial crisis, its strict application would certainly cause banks to hoard capital rather than lend to borrowers in such an extraordinary time.

Nevertheless, even as the PRA recognizes the balancing difficulties between the rigor of prudential regulatory standards and the liberation policies aimed at banks due to demands in the COVID-19 crisis, the PRA has in effect "delegated" to banks the implementation of such a balance at the micro level of evaluating their borrowers. Such "delegated" implementation does not put banks in an easy position as they need to deal with the dissonance of changing regulatory objectives and are yet not certain to what extent the boundaries of the existing regulatory regime can be pushed.[66]

The PRA is not in a unique position, as the European Banking Authority faces the same policy challenge of encouraging banks to support the real economy's needs[67] while upholding the prudential regulatory frameworks that have only just been completed in the decade after the global financial crisis of 2007-08.[68] The European Central Bank which has direct microprudential supervisory authority over key euro area banks[69] also allows banks to take a longer-term view of loan adversity so that banks may refrain from excessive loan-loss provisioning.[70] Although the elasticity parameters are relatively clarified by banking regulators, the need to maintain overall institutional coherence has caused bank regulators to be unwilling to articulate excessively on possible impairments to credit risk and bank balance sheets. This is understandable as bank regulators do not wish to become stumbling blocks to the policy purposes of relief and rescue. However, regulated entities are ultimately left with the balancing act of achieving the goals of legal elasticity while maintaining institutional coherence.

Unintended Adverse Consequences for Markets, Institutional Stability, and Social and Distributive Justice

Although legal elasticity in suspending financial regulations supports the relief packages for borrowers and appears to meet social welfare needs in the near term, the longer-term implications of such elasticity are not articulated by regulators and arguably internalized by banks. Banks remain uncertain about how impaired their balance sheets may be, and when the full strictness of prudential regulation would resume. Yet asking banks to internalize the balance poses a difficult challenge—should banks take the opportunity to treat borrowers generously, especially favoured clients? How should banks manage the resumption of regulatory expectations in due course? Banks are arguably faced with contradictory regulatory expectations: on the one hand to apply maximum flexibility to accommodate the immediate financial needs and limitations of their customers while on the other to maintain prudential standards and safeguard the quality of their assets. Hence, it is likely that banks' behaviour in enforcement and borrower treatment could be socially adverse when banks are able to resume efficient market-based behaviour.

In credit arrangements, contractual terms regarding default, which operate as efficient market mechanisms to protect lenders, are forcibly suspended for the wider public interest objective of alleviating household suffering. If left to efficient market mechanisms, the operation of private law could lead to the systemically destabilizing effect of mass household defaults and even bankruptcies during this period. The FCA's power to suspend contractual operation is based on its general conduct of business principles, especially on Principle 6 that requires firms to pay due regard to the interests of their customers and treat them fairly, while contractual operation for business debt is suspended under the Corporate Insolvency and Governance Act 2020 discussed above.

However, payment holidays are not the same as permanent debt relief. Borrowers benefiting from this may postpone their troubles, but may be storing up an amount of arrears and debt that may become even more unmanageable in the future.[71] Banks and other lenders may try to pre-emptively discourage retail customers from taking advantage of payment holidays too. The FCA has not provided clear enough guidance to lenders on how to deal with requests for payment holidays, leaving to borrowers the burden of negotiating the exact terms of their debt for the period after the suspension of repayments. The conduct of debt enforcement down the road is also a matter of concern, especially from the point of view of social justice,[72] as lenders would be anxious to mitigate the impairments to their balance sheets. Further, the FCA's Chairman[73] and commentators have warned that regulators' ambiguous positions risk pushing customers into unsustainable levels of debt. As household debt in the UK is already at very high levels, the implementation of regulatory suspensions to facilitate financial relief and rescue may exacerbate the problem of high household leverage and the fragility of household finances in the long-term.[74] Huertas[75] speaks of both relief during the pandemic and the need for normalization so that predictability and efficiency can work in markets after the pandemic is over. The question at stake is: 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 in due course, bearing in mind that business borrowers may be responsible for stakeholders and job creation?

Next, efficiency disruptions introduced by regulatory suspension 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. Underwriters of mortgages seek to bundle up mortgages into securitized assets usually after three months of such mortgages being written. Payment holidays affect the information quality of such mortgages as no reliable stream of income can be reported for securitized assets sales, and this can in turn freeze up mortgage markets, adversely affecting households that need mortgages or refinancing.[76]

Regulators also need to consider the distributive effects of the measures above. There may be a temporary distributive effect from lenders to borrowers entailing from relief granted during the crisis. This is privately borne by banks and their shareholders. This type of redistribution via interfering with private contracts may be blunt as 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.[77] The years of microprudential regulatory reform have made banks more resilient,[78] and such a redistributive effect may well be within banks' current capacities.[79] However, it remains uncertain how far banks can push their newly-built resilience and at what point they may be jeopardized.[80] Such concerns would shape banks' behaviour in their pursuit of unviable borrowers when relief ceases. Yet the private enforcement paradigm against borrowers would likely be socially scrutinized, and long-term implications emerge in terms of how much permanent redistribution would or should take place as a result of writing off bad debts. These dilemmas and challenges arise as longer-term consequences due to the deployment of legal elasticity, and there are no easy answers in the short-term.

Finally, regulatory suspensions also bring about immediate effects of institutional dissonance if their application leaves gaps and creates differences between markets. Regulatory suspensions in relation to payment holidays for consumers and business borrowers do not apply to peer-to-peer lending arrangements. This is because "peer" lenders are not regulated entities and only the platform that facilitates peer-to-peer lending is regulated[81] with respect to their duties in conduct of business vis-à-vis their customers on both sides of the market, i.e., the supply side for credit (who are treated as investors in loans) and demand side (the borrowers). This may be regarded as a hazard in "regulatory commons" articulated by Buzbee[82] who cautions against regulatory gaps that may be ideologically anomalous but that are caused by the drawing of regulatory boundaries.[83] The treatment of borrowers has been completely left to the self-regulation of peer-to-peer lending platforms, some of whom allow payment holidays and "pass the pain" to their lender/investors by freezing withdrawals or slashing returns.[84]

B. Regulatory Package Aimed at Increasing Credit Availability to Businesses

The PRA has clearly instructed UK banks that all elements of liquidity and capital buffers "exist to be used as necessary to support the economy."[85] This relates to the second element of the UK's rescue and relief policy goals for households and corporations—access to credit during the COVID-19 crisis. Arguably, this general pronouncement reflects the introduction of objectives in microprudential regulation that are different from the objectives in post-crisis regulatory reforms from 2010. The diagnosis of excessive lending and risk-taking[86] by banks in the wake of the global financial crisis 2007-08 led to microprudential regulatory regimes that incentivized deleveraging in the UK and EU.[87] A call to expansion in credit provision is likely to cause banks some sense of dissonance in terms of assessing what their behavior ought to be. The expansion of credit is a policy not unique to the UK, as fiscal support for corporate borrowing, trade credit, and commercial paper is also enacted in the United States,[88] although it is left to state and federal prudential regulators to work out the prudential regulatory adjustments that are needed to cohere with such measures.

Legal elasticity in microprudential regulation has been deployed in the UK to shape lenders' incentives to lend. Besides the downward adjustment of the inherently flexible CCyb discussed above, several other unexpected prudential measures have been relaxed. The PRA guidance clarifies that banks can draw down all their capital buffers starting with any discretionary capital buffer. Regulatory capital buffers such as the capital conservation, systemic risk, PRA buffer and buffers applying to systemically important banks are required to be maintained as risk-constraining measures since the post-crisis reforms.[89] Banks may also build up a discretionary additional buffer on top of regulatory buffers in order to be prudent. They are now encouraged to draw down such discretionary buffer[90] to maximise their capacity to lend. After exhausting any discretionary buffer, banks are able to draw down their regulatory buffers as well, starting from the PRA buffer which is individual to each bank and not publicly disclosed, followed by any remaining CCyb, the capital conservation buffer and the systemic risk buffers that only applies to banks with more than £25bn in deposits.[91] The PRA and FPC have nevertheless maintained the notional levels of mandatory regulatory buffers (except CCyb), such as firms' systemic risk buffer rates so as to maintain confidence in banks' resilience.[92]

Further, a suite of microprudential regulatory measures in liquidity and leverage thresholds have been relaxed, many of these not thought to be inherently flexible as they relate to the risk moderation objective in shaping banks' lending behaviour. 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 percent they are supposed to maintain.[93] The liquidity coverage ratio is intended to be maintained at all times at 100 percent which effectively means that a firm can meet its cash outflows for a period of thirty days so as to prevent a liquidity-driven systemic crisis.[94] This relaxation is an example of unexpected elasticity which raises concerns about the balancing of short-term crisis management objectives against prudential regulatory objectives. It is unclear to what extent banks can draw down their liquidity ratio, as this can cause liquidity hazards for them. However, the Bank of England has provided a new Coronavirus Corporate Financing Facility[95] which is designed to help businesses tide over liquidity squeezes through their bank. This could help prevent banks from being dragged into liquidity hazards by corporate customers.

Next, at the EU level, there is a new legislative initiative to allow banks not to count certain loans as subject to the prudential measure of the leverage ratio, in order to augment banks' capacities to lend in a less constrained manner by existing regulation. The leverage ratio limits all leverage created by banks to be supported by at least 3 percent of CET1 capital.[96] This is a measure that backstops bank lending and complements other microprudential regulatory measures. The new EU Regulation,[97] called the "CRR Quick Fix" package, introduced temporary flexibility in calculating institutions' total exposure measure in order to reduce the risk of amplifying leverage in a time of economic contraction and constrained business.[98] In particular, certain exposures such as guaranteed loans by national governments can be excluded from banks' balance sheets. This is justified by the need to maintain the level of lending to households and businesses.[99] This measure applies to the UK in view of the transitional status of the UK before exiting the EU at the end of 2020.[100]

In order to precisely steer banks' behaviour towards increased support for the real economy instead of perverse incentives such as rewarding shareholders, the PRA has also provided strongly phrased guidance to UK banks to suspend any capital distributions to shareholders including the payment of dividends and share buy-backs as well as the payment of any cash bonus to certain material categories of staff.[101] This can be regarded as a different type of "suspension" as it is a form of intervention that disrupts market participants' expectations, such as on the part of institutional shareholders. Regulators' power over dividend restrictions is warranted under existing regulation[102] in order 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.

Finally, the relaxation of microprudential requirements to incentivize lending, and hence turn banks' potentially risk-averse preferences to supporting the real economy, is complemented by the suspension of externally administered stress testing. Stress tests are a useful exercise for supervisors to understand whether banks have enough capital to continue to intermediate and lend in disrupted scenarios.[103] The Bank of England (BoE) normally runs the following stress tests: an annual cyclical scenario and a biennial exploratory scenario. The tests are forward looking and facilitate cross-bank comparisons, as well as monitoring for signs of systemic risk. The BoE has postponed the 2020 stress test.[104] This decision is intended to keep credit flowing to households and businesses and reduce pressure on banks induced by the stress test.[105]

Although the suspension is based on an inherently elastic structure as the PRA has full discretion on the timing and frequency of regulatory stress testing, the drawback of such suspension is that information opacity may be exacerbated in relation to banks' strength at times of crisis. Further, the uncertainty over the timeframe for the next stress test exercise makes it hard for banks to plan in advance and develop their lending and broader asset quality strategies in line with regulatory expectations. Such uncertainty can neutralize the intended effects of the regulatory package to increase credit availability to business if banks act in a cautious manner in anticipation of imminent stress testing. Regulatory suspensions of stress testing do not help address the unknowns that exacerbate fragility in the post-COVID period. At the same time, delayed stress tests also mean delayed supervisory guidance on banks' capital and resilience positions. Suspending stress testing exacerbates instability and increases information gaps[106] in the banking sector, particularly in times of stress where market participants need more information to plan for crisis management processes.[107] Regulators may be responding only to the near-term needs to release bank lending, and although they remain keen to protect the prudential regulatory framework, there is inevitably some extent of undercutting and compromise, the effects of which can be longer-term and create uncertainties for both regulators' objectives and regulated entities' behaviour.[108]

The regulatory suspensions discussed above may incentivize banks to expand their lending, but the pressure to lend in a less discriminate manner may increase. This could lead to longer-term adverse consequences such as the accumulation of non-performing exposures on banks' balance sheets.[109] This consequence is neither beneficial for banks nor borrowers as banks' regulatory compliance may be jeopardised and their future capacities to support the real economy could be diminished. Further, balance sheet pressures can also entail necessary enforcement against borrowers, leading to more social frictions between finance and society in due course.

In order that the legal elasticity discussed above achieves real effects, the UK has further introduced fiscal support to boost lending. On the one hand, this overcomes banks' incentives not to respond to the legal elasticity introduced. However, such measures positively distort banks' incentives in the near term, and may produce results of a short-term focus with longer term adverse impact on both bank resilience and social justice.

The UK government has announced fiscal support for two loan schemes, so that fiscal underwriting can incentivize bank lending. UK businesses with turnover of less than £45 million can benefit from the Coronavirus Business Interruption Loan Scheme, which is administered by the government-owned British Business Bank and enables accredited lenders to provide loans and overdraft facilities of up to £5 million, guaranteed at 80 percent by the government, to be repaid over up to six years.[110] UK small and medium-sized businesses will also benefit from the Bounce Back Loan Scheme that provides loan facilities of up to £50000, guaranteed at 100 percent by the government to be repaid over up to six years with no payments in the first twelve months.[111] Lenders are expected to assess whether businesses should access such government-guaranteed finance, the principle being that loans should only be available to otherwise healthy businesses that need to trade through the short to medium-term revenue loss caused by the lockdown. To support the lending programme, the PRA has announced that loans made under the Bounce Back Scheme, which is 100 percent guaranteed, would not be counted in the leverage ratio.[112]

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

Credit, or leverage, is often a double-edged sword. It may allow present problems to be solved, but often at the price of deferred constrictions and augmentation of financial risk for the future.[113]

In the UK, and arguably in the United States, banks' credit risks are likely exacerbated by underlying fiscal support for government-backed loans. Fiscal guarantees are likely to fuel moral hazard as the urgent demand for such loans makes underwriting a pressed process exacerbated by information asymmetry.[114] The government guarantee is likely to incentivize minimal underwriting diligence standards as banks do not have the incentive to price conservatively. It is uncertain if the UK government's policy choice to greatly expand commercial channels of financial support for businesses, such as through banks, is necessarily optimal, as the public interest needs underlying policy choice greatly interferes with the delicate relationship between microprudential regulation and commercial decision-making.[115] This creates 'legalized' moral hazard as banks are incentivized to ignore resilience implications of the increased loan underwriting by relying on the eventuality of fiscal bailout. Commentators already expect at least 40 percent of Bounce Back loans to default in due course.[116]

The level of loans made in the wake of the COVID-19 crisis that can be expected to be non-performing would likely increase.[117] This could have adverse consequences for bank resilience[118] even if regulators have taken the view that banks' capital positions are now relatively strong. Regulators are already concerned[119] about increased debt levels during the pandemic. There is no indication yet of any major shift in financial regulation in the long term at the end of regulatory suspensions. The PRA, for example, seems to assume that the regulatory framework would simply resume after a likely twelve-month period of the suspension of the CCyb, and maintains that other unadjusted capital requirements remain the same.[120] However, would legal elasticity result in more permanent issues for banks to deal with, and would the existing regulatory framework be sufficient? How far can the expected challenges to bank resilience be met by the fiscal backstop for government guaranteed loans?[121] Further, would a fiscal backstop not create a vicious circle problem for banks, as banks are also funders for sovereigns? If banks suffer from impaired balance sheets from excessive credit creation during the COVID-19 crisis, to what extent would governments' own fiscal backstops be credible, since governments rely on private sector funding (including banks) themselves?

Further, it is uncertain that the temporary boost of lending to businesses would not become a snare for borrowers in the future. The Bounce Back Scheme relieves businesses of payments for the first twelve months, but it is uncertain if the period would be sufficient for a business to recover. The government guarantee can also introduce perverse incentives for banks to accelerate treating recovering Bounce Back borrowers as in default so as to call upon the guarantee and to remove these borrowers from banks' balance sheets, exacerbating the pressure placed on the fiscal backstop. Huertas[122] rightly argues that current loan support measures must be coupled with regulatory thinking about conduct in treating borrowers in due course, as careful discernment of unviable borrowers and their fair treatment remains a paramount concern even as the crisis recedes.

It may be argued that the hazards of compelling banks to support expanded credit in such emergency times may be overstated as companies have the option of raising equity which is a more stable form of finance to tide over the crisis. Equity-raising also benefits from regulatory suspension which is discussed below. However, investors in the markets are rightly risk averse during the COVID-19 crisis, and can be highly selective or make equity financing costly, favoring those companies that are already financially strong, punishing those that have signals of weakness.[123] Indeed, empirical research finds that companies are turning more to debt than equity issuances,[124] and companies' stock market prices are highly penalized by risk-averse investors' perceptions such as whether they are affected by trade with China or have healthy leverage and cash levels.[125]

Legal elasticity in facilitating banks' incentives to lend is arguably 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.* As Dorn[126] argued, "elasticity in application of finance laws opens up such law to a process of deterioration, undermining legal certainty, loosening market discipline and inviting crisis." Although the measures of keeping open access to credit and creating a fiscal backstop for business loans could be necessary in principle, regulators could engage in more holistic policy thinking, especially supported by a fully-theorized understanding of the structural nature of legal elasticity. Possible options for policy thinking include the following:

(a) There is room to consider how banks and regulators can be more engaged in the dynamic landscape of asset quality and banks' resilience and the impact of these upon banks' conduct of borrowers and customers.[127] The supervision of prudential and conduct of business aspects can benefit from integrated conversations between relevant regulators. In the UK, the FCA and PRA have a history of coordination,[128] but this may be more challenging in jurisdictions with disparate regulators, such as the United States.

(b) Regulators may need to consider safe harbors from capital or liquidity breaches by banks in due course for periods of time as banks take stock of their balance sheets and as suspended regulatory requirements resume. There should be some transitionary provision for regulatory forbearance while working in supervisory engagement with banks.

(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 neither penalize banks nor borrowers in circumstances caused by the onset of the COVID-19 crisis. There are policy option mixes involving public and private sector support,[129] debt versus equity,[130] for regrouping corporations as economic engines, in order to achieve the balance between rescue of the real economy, bank resilience,[131] and fiscal implications.

IV. Regulatory Elasticity in Capital Markets Regulation: Advancing Corporate Fundraising and Economic Recovery

As freezes in economic activity during the COVID-19 lockdown threaten corporate revenues, business operational continuity and even survival,[132] it is important to address equity fundraising by companies on an emergency basis. The channel of equity fundraising is important as equity provides a stable and long-term pool of capital for companies,[133] and can reinforce a company's financial resilience. Debt, on the other hand, may be more accessible but can exacerbate financial fragility.[134]

The FCA, regulator for publicly traded companies and the Listing Authority in the UK, introduced a slew of emergency measures, suspending and adjusting listing and securities offering regulations that would have applied in normal times, in order to facilitate less cumbersome fundraising by corporations. Such fundraising could be preemptive in nature 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 post-crisis. However, companies seeking to raise funds could also be in a precarious state, especially if they have inflexible contractually committed outflows such as debt servicing and rent, making their securities particularly risky for investors.

The FCA issued a Statement of Policy on April 8, 2020[135] to facilitate corporate fundraising exceptionally, intended to last only for the duration of the pandemic. This policy introduces regulatory suspensions and adjustments to three key aspects of fundraising: the treatment of preemption rights, the general meeting procedures ordinarily needed for shareholder approval of significant transactions in the Listing Rules, and the mandatory disclosure document required for the fundraising.

In relation to the treatment of preemption 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[136] unless preemption is exempt.[137] The right of preemption seeks to mitigate managerial agency problems as managers may seek to offer new shares cheaply and easily to third parties if left to their own incentives. Shareholders would be adversely impacted in terms of value dilution and the reduction in voting power.[138] Although this position was harmonized with the EU's Second Company Law Directive, reflecting the European stance for protecting shareholders against managerial exploitation, it is also regarded in the UK as a "core" right of shareholders.[139] Preemption rights may be regarded as a mandatory corporate law rule that is placed along the more "rigid" end of corporate law,[140] reducing the flexibility of managers to raise funds easily in a perhaps changing and dynamic environment. In the United States, preemption 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. In other words, market mechanisms in the United States are seen as sufficient to provide shareholder protection so that corporate governance rules such as preemption rights need not be legalized. Although there is an increased burden for shareholders to determine if they would use such market mechanisms, the corresponding flexibility for managers reduces cost to the company. The UK, despite similarity with the United States in terms of deep and liquid capital markets, has however opted for a different balance of flexibility-control in relation to safeguarding the rights of shareholders,[141] particularly in publicly-traded companies, not just leaving them to market mechanisms or ex-post remedies.[142] There is, however, the possibility that the articles of association can provide for a waiver of preemption rights in advance, for a period of up to five years, so that directors can be pre-authorized to an agreed degree of flexibility.[143] The general meeting can also provide ad hoc waivers by special resolution up to certain limits. 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. This best practice is recommended by the Preemption Group (PEG) which comprises a range of influential institutional investors.

The PEG made an extraordinary recommendation to investors that preemption rights could normally be waived for issuances up to 20 percent of issued share capital during the pandemic. This recommendation is explicitly endorsed by other trade bodies such as the Association for Financial Markets in Europe (AFME) and by the FCA. The FCA is not the direct authority to adjust company law provisions. However, this is not an adjustment to company law as such but rather an adjustment to the ordinary market practice of institutional investors within the framework of the exercise of their voting power as determined by company law. Although the PEG has shown flexibility during this challenging time for companies, fundraising still takes time to complete. Commentators have raised the prospect of shortening offer periods as lessons from the emergency fundraising exercise by banks in the 2007-08 global financial crisis point to disadvantages of a long offer period. Ferran[144] argued that the twenty-one day offer period that applied during that time, which has since been reduced to fourteen days under the Listing Rules, was too long and allowed short sellers to depress the share price of the issuer, adversely impacting uptake of the shares. The FCA also endorsed the PEG's stance on soft preemption offers, which allows companies to make private placements, therefore not attracting the compliance burden required in relation to public offers. Companies are urged to work with investment banks responsible for the placings to engage with existing institutional shareholders, in order to respect the ethos underlying the preemption regime despite the newly introduced flexibility.

Next, company law requires directors who wish to allot new shares in the company to seek authorization in the general meeting[145] unless pre-authorization is obtained either in the articles or by a resolution in an earlier general meeting.[146] The PEG has recommended that such pre-authorization could normally be for up to one-third of a company's issued share capital. Pre-authorizations must be revisited every five years, hence an in-built mechanism for shareholder monitoring is provided in law to countervail adverse effects of managerial flexibility.[147] The relatively high level of pre-authorization recommended by the PEG reflects the inherent flexibility in company law to enable shareholders and boards to implement their preferred bargains instead of being tied to mandatory standards. This is likely to meet many companies' fundraising needs during the pandemic.

However, although inherent flexibility in company law can pave the way for less cumbersome rights issues made by companies, such companies still have to contend with mandatory disclosure obligations under securities regulation, which has been regarded as a fundamental pillar of investor protection,[148] unless issuers only conduct private placements up to 20 percent of the company's issued share capital and are thus exempt from mandatory disclosure obligations. However, even in the latter situation, institutional investors in private placements would still likely require companies to make adequate disclosure of their needs and prospects.

In this manner, the cost of preparing disclosure documents for investors[149] and how disclosure may affect investors' behavioural biases in times of great uncertainty and challenge may prove to be twin obstacles for corporate fundraising. In such times, investors may greatly discount a company's share price as they are susceptible to risk aversion and other cognitive biases. The FCA, with the PEG's support, urged companies to utilize the exemption from the 2017 EU Prospectus Regulation with regard to issuances of securities up to 20 percent of total traded securities. This means that such issuances would not need to be accompanied by a prospectus, saving companies time and cost in preparing one. Where the exemptions[150] under the Prospectus Regulation 2017 do not apply, issuers are urged to utilize simpler disclosure requirements based on shelf registration of a base prospectus for seasoned offerings.[151]

Further, as mandatory disclosure includes a requirement for issuers to disclose on an audited basis that they have working capital for the next twelve months as a solvent entity, the FCA considers it impracticable for the requirement to apply as companies are facing the uncertainties wrought by the COVID-19 crisis. The FCA has exceptionally decided to tweak the application of 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 that does not require formal audit, but only a comfort letter from an auditor in support. This only applies if a company's adverse financial position has been caused by the pandemic crisis and has not entailed from other weaknesses. The FCA requires the additional "Coronavirus Working Capital Statement" to contain models and assumptions relating to the impact of the pandemic on the company, including taking into account the uncertainty in length and duration of the crisis and impact on revenue. This tweak is arguably a form of framing that achieves a balance between investors' information rights and issuers' fundraising interests, which we analyse below.

Next, the FCA Policy[152] also allows companies to financially reorganize themselves in a less cumbersome manner, by engaging in certain substantial transactions specified in the Listing Rules,[153] relating to significant disposals of assets. Such disposals may be a way of restructuring companies during difficult times as liabilities and expenses can be shed. It may be imperative for companies to be able to finalize their deals quickly, and such efficacy can be affected by the need for companies to seek general meeting approval for these under Listing Rules. Companies can now apply for a dispensation for general meetings, avoiding the cumbersome procedures and time required for conducting general meetings. The dispensation of general meetings is granted on a case-by-case basis, and issuers would have to provide evidence that shareholders would have voted in favour of such a resolution if a general meeting had taken place. Such dispensation is arguably sensible as social distancing during the COVID-19 crisis would make it difficult for general meetings to be physically convened. However, companies could virtually convene such meetings. The FCA's policy in favour of allowing dispensations possibly caters more for timeliness needs on companies' part.

Companies applying for dispensation can provide evidence that they have secured written undertakings from sufficient shareholders to indicate their support for the resolution either ahead of the issuer publishing a circular for the market generally, or after such a circular has been published. The FCA emphasized the temporary and extraordinary nature of such dispensation. Further, the need to apply to the FCA for dispensation means that regulatory discretion can be perceived by investors as a form of gatekeeping at a time where investor protection based on normally expected procedures is suspended.

In parallel, the FCA[154] has also provided temporary relief for listed companies in relation to normal compliance obligations to maintain efficient capital markets, to publish their audited annual financial reports. The FCA package of measures includes: (1) delaying the filing of accounts by companies; (2) postponing auditor tenders and audit partner rotation; (3) reducing Financial Reporting Council (FRC) demands on companies and audit firms; and (4) extending reporting deadlines for public sector bodies.[155] Although these measures disrupt expectations in capital markets for timely and accurate information, companies may not be in a position to offer such reporting in highly uncertain times, and short-termist information may be distortive in itself. Policymakers emphasize that the quality of transparency should continue to be robust,[156] but it is uncertain how such quality can be readily assessed in extraordinary and highly dynamic times. Companies are caught in a difficult position, as taking advantage of reliefs and regulatory suspensions may give rise to disfavor with investors. Delayed general meetings[157] and uncertain quality in annual reports can adversely affect the fundraising hopes of companies too.

We provide critical reflections below on the achievements as well as the unintended and adverse consequences that may entail from the capital markets regulatory suspensions discussed. We argue that, just as regulatory suspensions that apply to banks in effect result in delegated implementation to banks, so too regulatory suspensions in capital markets regulations allow the market to price and select companies. The outworking of market forces is not necessarily consonant with social appetite for "saving" companies or jobs. Further, just as deeper regulatory engagement with longer-term and broader effects of regulatory suspensions seems missing in the regulatory suspensions applicable to the regulation of credit, we suggest that more radical regulatory engagement and policy thinking may be needed if injection of equity into companies is viewed as socially desirable.

A. Analysis on Treatment of Preemption Rights

The extended suspension of preemption rights up to 20 percent of issued share capital is not exactly a regulatory suspension, as it is recommended market practice by the PEG to investors on a case-by-case basis. Its status is more like soft law, with the FCA's endorsement not exactly a form of legalization but rather a reinforcing signal of legitimacy and a nudge directed to investors.[158]

Although preemption rights are regarded as 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 referred to as the "enabling" aspect of company law that is ideologically supported for its efficiency effects regarding the allocation of governance rights between voluntarily bargaining parties.[159] It may be argued that in the United States, the enabling effects of company law are realized in terms of the non-mandatory nature of the doctrine of preemption rights. The United Kingdom's preemption 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.[160] As the United Kingdom allows negotiated exclusion or disapplication of preemption rights between shareholders and their companies,[161] preemption rights may be regarded as a default rule but one that can be characterized as 'strong default' given that deviating from the rule requires special procedures and is subject to a time limitation of five years, which discourages too much flexibility.[162]

Inherent flexibility in enabling corporate law is empowering in nature, as it allows for company innovations to be offered and shareholders' preferences to be voiced, without being subsumed under a one-size-fits-all mandatory prescription. 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 amongst investors. In this manner, the role of soft law such as best practices recommended by the PEG is highly valuable and provides a benchmark for convergence and efficiency in private decision-making.[163]. The need for harmonized optimal terms in company law, despite shareholders' theoretical freedoms to bargain with companies, has been theorized by Easterbrook and Fischel.[164]

The FCA's package of regulatory suspensions, which includes unexpected suspensions of capital markets regulations, is arguably bundled with the inherent flexibility expressed in company law. Such bundling can allow the FCA to benefit from the aura of inherent flexibility and create a reduced impression of dissonance for investors. The FCA's role in endorsing the PEG's recommendation can potentially achieve the effect of reinforcing legitimacy in the face of perhaps divergent investor preferences, nudging towards convergence in accepting the soft law standard. However, is the bundling of regulatory suspensions in capital markets regulation with inherently flexible company law aspects inappropriate? The latter is "enabling" in nature and can be adjusted, but the former is mandatory in nature due to the public interest of investor protection, and can be seen as being compromised by being bundled in regulatory suspensions encompassing inherently flexible company law. What boundaries are there, if any, between the ideological or jurisdictional separation[165] of corporate law from securities regulation?[166]

On the one hand, the bundling exercise may make porous the boundaries of enabling corporate law and mandatory securities regulation and allow regulators greater freedom to foray into the former.[167] On 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.[168] Further, it is uncertain to what extent the FCA has engaged with the PEG and AFME ahead of their announcement, and whether the soft law recommendations reflect the multifaceted mix of private and public interest in the exercise of inherent flexibility. Moreover, any coordination between the FCA and investor trade bodies, although useful in a crisis, can also create opaque networks that may become impenetrable to other interested stakeholders.

We turn to consider the unexpected regulatory suspensions that are juxtaposed with the inherently flexible measure. The strategic bundling of inherent flexibility with unexpected suspensions mitigates the dissonance effect of the latter. However, such bundling also results in a strong marketization character for the *other* regulatory suspensions, thinning out its public interest aspects. Part C in particular discusses this.

B. Analysis on Dispensation of General Meetings

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. In reality, such procedural fairness under company law 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,[169] and the advent of similar provisions in the European Shareholders' Rights Directive 2017).[170] Policymakers' nudge to institutional investors to become more engaged is due to concerns that passive institutional shareholders who vote with management are not effectively performing their monitoring roles.[171] Moreover, with the rise of American-style hedge fund shareholder activism,[172] the level of voice and vociferousness observed in the institutional shareholder community has risen because institutions have worked with hedge funds in joint campaigns[173] and because the corporate sector has attracted negative attention for the last decade or so, since the global financial crisis and a number of home-grown scandals.[174]

The discretionary dispensation of general meeting procedures for substantial transactions may not be regarded as too prejudicial to shareholders. First, its "bundling" with the relatively more enabling regime company law discussed above allows shareholders to see the regulatory suspension in a more integrated and less unfavourable light. Second, it may be argued that the condition for discretionary dispensation is that the company must show evidence of sufficient shareholder consent; hence, companies are still compelled to engage with shareholders, much in the "stewardship" ethos of informal engagement "outside of general meetings." Such engagement can also ameliorate the risks taken by investors in allowing the waivers of preemption rights discussed above. Finally, regulatory discretion in dispensation may be regarded as a gatekeeping device, although it is uncertain what level of evidence the regulator is looking for in relation to shareholder consent. For instance, it could be queried if shareholder consent with conditions or with qualifications may be regarded as sufficient.

Nevertheless, to allow dispensation of general meetings conditioned upon companies securing sufficient written consent of shareholders would mean that companies are likely to engage in selective engagement, with perhaps "friendly" but significant shareholders in order to reach the needed 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.[175] Although it may be argued that stewardship practices already entail differences in the quality of company-investor relationships amongst different investors, allowing companies to selectively "court" shareholders for decision-making seems to go a step further and exacerbate the already uneven playing field. Furthermore, even if companies accurately estimate the level of majority support for these measures, such estimates are not equivalent to a general meeting where the percentage of shareholders dissenting is recorded. A relatively high level of dissent is important for signalling the controversiality of company proposals.

In this light, 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. These should be considered not only on a temporary basis but also in terms of how such trade-offs may exacerbate a longer-running issue, such as the relative marginalisation of the retail investor, in the stewardship landscape that emphasizes the role of institutional ones. 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?[176] 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,[177] and should give rise to longer-term thinking even after a crisis settles.

C. Analysis on Working Capital Disclosure

Where a prospectus or simplified prospectus is required for corporate fundraising, the FCA[178] has not suspended mandatory disclosure obligations. Ferran,[179] drawing on lessons from the last emergency fundraising by banks during the global financial crisis, recommended that suspension of mandatory disclosure could be warranted if issuers are not new to the market and if the suspension would save issuers time and cost. However, mandatory disclosure is a cherished tenet in investor protection[180] and suspending it may be counterproductive if companies' cost of capital increases due to investor risk aversion.[181] 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.

By allowing issuers without underlying financial problems to issue a separate coronavirus statement which does not affect the otherwise "clean" working capital declaration, the FCA arguably engages in a form of framing of information while not undercutting the long-held institutional expectations of comprehensive and full disclosure. Investors would still be receiving the COVID-19 impact-related financial information, but in a disaggregated manner. Kahnemann and Tversky's prospect theory[182] shows how the framing of information affects choice, and in particular, O'Clock and Devine[183] demonstrate how negatively-framed information by companies affects auditors' opinions. The disaggregation of the "clean" working capital declaration would help to avoid auditors' biases against negatively-framed information[184] and would likely be viewed positively by investors. 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 a more forgiving light and not to preponderantly "infect" the positive framing within a "clean" working capital declaration.

A crucial question is whether the framing approach disrupts the balance of institutional values in securities regulation, i.e., the promotion of rational investor market discipline for issuers (as far as possible, given behavioural insights showing lapses in rationality[185]). The rational investor brings about efficient pricing in capital markets[186] so capital is ultimately allocated to the most efficient companies, resulting in long-term wealth creation for all participants in the corporate economy. It may, however, be argued that such framing could serve as a behavioural antidote to counter investors' sub-optimal behavioural biases, such as excessive risk aversion.

Nevertheless, a more important question is what the FCA seeks to achieve with the regulatory suspensions introduced. The regulatory suspensions to facilitate easier equity fundraising by companies do not change how investors select and price their investments in companies. These investment decisions would still be made for rational purposes and not necessarily for pro-social purposes in relation to saving companies or jobs. When a crisis exposes the fragilities in the corporate economy, it may be argued that it is rationally optimal for a destructive wave to sift out all but the most robust companies, albeit bringing about a transitionary period of instability. Left to market forces, commentators[187] have found that investors gravitate towards funding companies with less financial fragility during the COVID-19 crisis,[188] such as companies with lower levels of debt and higher cash buffers, which make them financially flexible. 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 many households are at stake.

The FCA's intervention in framing reflects a hint of public interest in relation to preventing massive destabilization of the corporate economy and capital markets.[189] The FCA has an interest in preserving the robustness of London's capital markets[190] throughout the crisis. However, the FCA has refrained from articulating pro-sociality, such as in relation to preservation of jobs by corporations, or more pronounced interventionist stances, such as stock market closures proposed by Andhov[191] in order to prevent short-termist value destruction by shareholders or short-sellers who may profit from anticipation of bad news. Schammo[192] queries if regulatory choices should be more pronounced to be in the overall public interest, such as being more "precautionary."

Although we are sceptical that precautionary tools such as stock market closures are necessarily optimal in achieving a balance between pro-social goals in saving the real economy and investor protection in capital markets, there is a need for the FCA to consider the substantive effects of regulatory suspensions, and whether more radical options are needed if supporting a robust corporate economy is a matter of public interest.[193] These include:

(a) using government or public sector vehicles or public-private partnerships to support capital injection into private sector companies alongside private sector fundraising,[194] in a manner that does not breach state aid rules;[195]
(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, so that subsequent short-ter-

> mist pressures do not become counter-productive or destructive. A form of fiduciary duties to be imposed for the benefit of the company may be warranted, such as discussed in relation to hedge fund activists[196] or controlling shareholders;[197] providing for adequate investor protection in return for their long-termist support, companies should make particular and adequate disclosures and continuing transparency regarding the use of funds,[198] and in particular investors may have an interest to ensure that companies pursue sustainable behaviour going forward.[199] instituting a form of prudential regulation[200] for the non-financial corporate sector too to improve their long-term resilience, entailing more mandatory standards in capital structures.

We have explored critically the dilemmas, challenges, unintended consequences, and possible adverse effects arising from regulatory suspensions in credit and capital markets regulations designed overall to achieve relief and rescue of households and the corporate economy. Although the suspensions themselves embed controversial policies that inevitably attract discussions of potential weaknesses, and the policies may not be perfect, we caution that these suspensions may have been carried out with near-sighted assumptions, with insufficient consideration being given to longer-term effects that may entail from the structural nature of legal elasticity. Even if regulators do not need to bring permanent adjustments about proactively or prematurely, they should engage with deeper and broader considerations in the deployment of legal elasticity, so that the demand for fundamental shifts, if they occur, do not take regulators by surprise and cause even more disruption and dissonance in due course. 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,"[201] so that dynamism can be brought to substantive policy solutions as well as regulatory processes, designs and implementation.

V. Deploying Legal Elasticity by Financial Regulators—the Way Forward

Sections III and IV have teased out the dilemmas, unintended and longer-term consequences of the regulatory suspensions introduced to achieve the relief and rescue agenda in the UK. We show that even where legal elasticity is used against a context of relative institutional stability, i.e., there is no apparent appetite for major regulatory reform, it introduces more than transient challenges in relation to institutional dissonance. Questions regarding regulatory objective trade-offs[202] arise, as well as critical scrutiny of outcomes achieved and unintended or adverse effects. We argue that regulators deploying legal elasticity should be mindful of its structural nature and be prepared to engage with managing its deployment.

We propose three aspects of a management process for legal elasticity, choosing to offer these 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 for the purposes of achieving substantive outcomes, regulators may face similar challenges. The three aspects of regulatory management of legal elasticity deal with:

(a) recognizing the potential for institutional dissonance and responsively managing these effects against a context of policy goals;
(b) actively engaging in multipart frameworks for crisis management, including with regulated entities who may be tasked with delegated implementation of the balance of regulatory suspensions and existing regulatory objectives;
(c) pre-crisis preparedness on the part of regulators in order to mobilize crisis management tools including legal elasticity in a robust manner.

A. Managing Institutional Dissonance

Where households and corporations engage in more debt to meet their financial needs in the wake of the COVID-19 crisis, the long-term macroprudential regulatory objective of debt reduction is affected,[203] not to mention the microprudential regulatory objective of prudent lending. We have earlier argued that lending behaviour is bound to be affected by policy nudges towards the expansion of bank balance sheets and the existence of government guarantees. In relation to capital markets regulation, although the facilitation of easier approvals for share issues and dispensation with general meeting procedures for substantial transactions may appear as pragmatic solutions to immediate problems, there are forces that may make the temporality of such measures questionable. The advent of technology and corporate pressures can both exert influences towards shaping the nature of shareholder engagement and the exercise of rights in subtle ways.[204] Further, institutional dissonance brings about more than just policy implications. Legal elasticity may also affect market-based structures in unintended ways as discussed in Section III regarding the market for securitized home mortgages in the US.[205]

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 that are mandatory does not of itself reinforce institutional stability, being merely a rhetorical device. Fundamental questions regarding how institutional tenets and values "encoded" in law or regulation have been rendered imbalanced would still arise, in relation to moral hazard,[206] or financial institution resilience.[207] Questions abound as to whether longer-term or permanent effects may entail from institutional dissonance and pave the way for policy change in due course.[208] In this way, institutional dissonance, initially perceived to be temporary, may affect social contract bargains underlying the institutionalization of norms or tenets.

Regulators should be mindful of the structural nature of legal elasticity and its potential to introduce disruptions that would portend questions of a more fundamental nature, and ultimately affect regulatory stability.[209] As Baldwin et al. argue, regulatory stability is not itself a tenet that should be necessarily maintained, but it is important to understand how it should be disturbed.[210]

Pistor's legal theory of finance provides a 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. However, one may take a more limited reading of the theory. According to the theory, finance is a hierarchical structure with sovereigns at its heart, to the extent that they control their own currency (and borrow mostly in their currency) and can therefore act as true lenders of last resort. Private parties fit into this hierarchical structure depending on their size and economic power from large systemic banks down to retail investors and borrowers. Pistor posits that 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 left to face the full rigour of the law. This conceptualization resonates very closely with the events of the global financial crisis during which most distressed large financial institutions were rescued with the use of public money while individual investors and borrowers were left to face the dire financial consequences of the crisis.

As the COVID-19-induced economic crisis is exogenous to the financial system in the sense that financial firms are not responsible for its occurrence and could have done nothing to prevent it, the key financial institutions and the sovereign at the heart of the financial system would not be incentivized to support any fundamental institutional change to financial law and regulation. Hence, elasticity is likely to be seen only as a set of temporary measures that need to circumvent the rigidities of institutional stability during an economic shock. In this manner, legal elasticity and its impact can be contained by the framing and decisions taken by powerful structures in finance, allowing legal elasticity to exist as minimally disruptive. Further, as much of the elasticity employed during the pandemic has been used to the benefit of actors in the periphery of the financial system, such as mortgaged households or small businesses, it can be argued that such elasticity is of a different and less radical quality than that affecting the heart of the financial system during the global financial crisis. Pistor's key thesis is that the core of the financial system must always be protected. In the current circumstances, despite the severity of the pandemic and the ensuing economic recession, financial institutions are not (yet) in distress. This permits governments and regulators to take measures to alleviate the consequences of the crisis for households and businesses on the grounds of social welfare but also as a means to implement a macro-economic policy of supporting the economy during what is hoped to be a V-shaped recession. But, if the core of the financial system becomes threatened, then it is likely that elasticity will again be used primarily to the benefit of core actors such as systemically important financial institutions.

Based on the power structures perspective of legal elasticity, institutional change would likely be resisted although legal elasticity has been deployed during the COVID-19 crisis. This narrower reading of the theory also means that legal elasticity and institutional change are only connected if power structures at the core of the financial system elect to do so. 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 in relation to the borrowers who have been on payment holidays? Is this issue only a matter of conduct of business?[211] Would consumer protection require more radical distributive treatment such as some extent of debt forgiveness? With prolonged economic uncertainty, these questions will not be answered satisfactorily with a simple resumption of regulatory regimes and the termination of suspensions. We posit that power structures alone are not likely to sustain institutional stability, as bottom-up social appetite and demands can exert new pressures in the future due to the longer-term effects of institutional dissonance. One of the authors has argued that social movements have contributed to a gradual institutional change in corporate regulation for example.[212] Lothian[213] and Arup[214] have also, in the wake of the global financial crisis, called for greater socialization of the objectives of financial regulation. Such a radical reorientation is not yet seen in the UK, being dominated by an economic paradigm[215] in financial regulation. Post-crisis reforms have only edged closer to macro-level economic perspectives such as financial stability.[216] However, there is a consistent social cry for financial regulation reform such as in consumer welfare.[217] The undercurrents of dissatisfaction with the myopic paradigms of financial regulation may again be raised in the opportunities provided by institutional dissonance. We simply do not think regulators can avoid thinking about radical and fundamental issues regarding institutional objectives, norms, and tenets, although it is beyond the scope of this work to prescribe that particular regulatory policy changes be made.

Hence, we argue that financial regulators should deploy legal elasticity with an understanding of its structural nature in accordance with the fully theorized account of Pistor's theory. This allows financial regulators to engage in dynamic evaluations of outcomes and effects of regulatory suspensions. Financial regulators should not start with the assumption that legal elasticity applied to the exogenous nature of the COVID-19 crisis is necessarily temporary and that resumption of institutional stability will automatically take place. Rather, we propose that when regulators deploy regulatory elasticity, it should be recognized that some extent of institutional dissonance *will* result, and should give consideration to monitoring the levels of and managing such dissonance, including engaging in regulatory discourse and institutional review. Keeping such an open mind allows regulators more fully to appreciate the risks and opportunities in deploying legal elasticity and allow regulators to operate more fully in the intersection between financial regulation as a system and wider public policy goals.

Proposal One: Financial regulators should expect institutional dissonance and focus on how to monitor and manage it in terms of public discourse. Regulators should adopt an open-minded stance to the longer-term effects of legal elasticity, factoring such effects into their decision-making matrix.

The practical implication for financial regulators is that monitoring and managing institutional dissonance is not a foregone assumption but an active approach, one that should be dynamic and sensitive to the overall pressures and drivers for change, without necessarily bringing about premature actions. In relation to this, we suggest that financial regulators can benefit from an approach of rational but holistic regulatory decision-making proposed by Sunstein.[218] Indeed, 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.

Sunstein's approach in regulatory decision-making is grounded in cost-benefit analysis in its broadest terms.[219] This approach allows regulators to anticipate and constantly assess the outcomes and effects of legal elasticity. This approach goes beyond merely calculating the monetary values of benefits and drawbacks in the marketized sense, and seeks to encompass "hard to value," controversial and subjective evaluations. The aim is to arrive at a more holistic evaluative compass. The evaluative compass is anchored upon the human perspective, including the difficulties in putting a value on social values and preferences.[220] Sunstein[221] sets out in detail and acknowledges the difficulties in such evaluations, clarifying that the aim is not to arrive at narrowly agreed monetized values in order to justify regulatory policies. Rather, this approach should tease out the factors that make variables hard to value, allowing ranges of tentative values to be assigned not to demean the variables but to map them out relative to other priorities and values, so that regulators can see the range of issues before them more clearly. The broad pursuit of such cost-benefit analysis is challenging, as it requires regulators to have a broad scope of information before them[222] and to make responsive judgments.

Commentators have criticized regulatory implementation of cost-benefit approaches in regular times as being flawed. Cost-benefit analyses have become narrowly defined, in order to avoid hard questions,[223] and highly proceduralized in order to show that formalities are completed for advancing a particular law reform.[224] Treatment of variables that are difficult to value could also be vague and weak.[225] However, as Wiener[226] argues, evaluative approaches like cost-benefit analysis need not be practised in narrow, formalistic and meaningless terms.

To apply this approach to financial regulators' management of legal elasticity and institutional dissonance, we encourage regulators to consider broadly near and longer-term effects and implications, in an ongoing manner. The deployment of legal elasticity raises institutional dissonance risks but also provides a unique opportunity to grapple with forward-looking thinking. Opportunities for law reform should not be ruled out. For example, where regulatory suspensions have mobilized a suite of laws and regulations not inherently thought to be flexible, this can provide an opportunity for regulators to consider if more flexibility needs to be built into regulatory systems.[227] The evaluative approach also provides a more robust basis for regulatory accountability in the management of legal elasticity and crisis management. [228]

This leads us to the second proposal which is intricately linked to Proposal One. We observe that financial regulators have communicated at great lengths to their regulated entities to carry out regulatory suspensions as well as to adhere to much of the institutional framework, especially in micro-prudential regulation and corporate 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 implementation matter for the regulated entities. In this manner, institutional dissonance can become externalized or "delegated" to their regulated entities. We argue that this leads to hazards in terms of unexpected behaviour by regulated entities and social justice consequences. There can be a better balance between regulatory management of legal elasticity and delegation to the regulated sector. Hence, besides the necessity of regulatory leadership under Proposal One that relates to regulators' monitoring and management of legal elasticity and institutional dissonance, regulatory leadership is necessary for managing delegated implementation in uncertain times resulting from institutional dissonance.

B. Delegated Implementation by Regulated Entities to Manage the Balance of Institutional Dissonance

The PRA emphasized at length that existing regulations continue to be implemented in a 'consistent, robust and well-balanced manner' although clarification is made towards lenient treatment of deferred debt payments benefiting from payment holidays.[229] This balance is not easy to maintain as regulated entities are mindful of the part they play in the broader agenda for relief and rescue while perceiving their needs for compliance with regulatory standards. The latter is arguably challenging as regulated entities are used to a relatively prescribed numerical governance regime in microprudential regulation. How should banks exercise the discretion to be able to draw down capital and liquidity buffers, not being certain where the bottom line is, or to make less loan loss provisions in light of the PRA's encouragement to refrain from treating deferred debt as being in default, not being certain how much to provision for? The exercise of discretion by banks can become a burden and not a freedom.

At a broader level, this is also an archetypical problem of modern regulatory approaches such as meta-regulation[230] where regulators' broad principles and open-ended frameworks are by necessity realized through detailed implementation by firms. Firms cannot be overly prescribed as regulators cannot micro-manage regulatory compliance. However, the breadth of discretion in implementation can often lead to firms' discretion being exercised in favour of cosmetic compliance,[231] 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.[232] We observe that in both the deployment of legal elasticity in credit and capital markets regulation, policymakers and regulators have tended towards a *greater degree* of autonomy for regulated entities and markets to implement legal elasticity. This discretion can be particularly difficult if regulated entities need to manage institutional dissonance while managing legal elasticity.

We argue that the more regulators assume that institutional stability is not affected by temporary legal elasticity and fail to engage with the implications of institutional dissonance, the more likely a 'delegated' approach will ensue, in the meta-regulatory outworking of legal elasticity. Regulated entities are in effect asked to implement new measures that challenge their sense of certainty, while being required to comply with existing rules and principles. This can give rise to different types of behavioural responses.

One is that the regulated entities can become excessively risk averse, mindful of the possible boomerang effect of compliance once temporary elasticity recedes. This can explain why the Coronavirus Business Interruption Loan Scheme discussed in Section III did not result in much underwriting by banks, as they were mindful of the existing prudential expectations on regulators' part. Second, delegated implementation by the regulated sector of legal elasticity can give rise to market participants' incentives to exploit opportunities.[233] This perverse behaviour can result from the perceived "freedom" in discretionary implementation of legal elasticity. Private-equity owned companies that were already laden with debt 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. Debt can increase future fragility for corporations.[234] These companies would also be competing with others for such 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. For example, regulators can engage in "blame games"[235] if social sentiment is unfavourable to their actions, and their narrative framing of crisis management can take on a form of defensiveness based on the delegation of implementation to the regulated sector.[236] We raise these possibilities because there may be outcomes that can be controversial, despite the overall policy agenda of relief and rescue. In this context, if regulators were to take enforcement actions against regulated entities for failure of regulatory compliance in the ambiguous context of managing institutional dissonance, this would also likely be regarded as unjust.[237]

Legal elasticity often results in reallocations of burden and benefit, and these may be perceived as justified on the basis of who can better bear risk or loss, and who may be in relatively greater need of welfare redistribution. The dangers of delegated implementation of legal elasticity to regulated entities, although likely inevitable in a meta-regulatory framework, are that: (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 or uncertain even though welfare outcomes that result are essentially matters of public interest.

Who should make judgments about welfare redistributive consequences[238] especially since these judgments are unlikely to be uncontroversial given a landscape of competing needs for individuals, corporations and systems in general?[239] Such distributive judgments implicate private capacities[240] as well as public institutional structures, such as in relation to the nature of the Lockean social contract in politics. The rise of the risk society[241] and welfare state in Western developed countries[242] poses the question of 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.[243] Even in an institutional context, there can be redistributive consequences. For example, the adjustments to mandatory disclosure for securities offerings in emergency fundraising by corporations discussed in Section IV have redistributive consequences in terms of reducing cost for companies, but potentially increasing opacity for investors.

In this manner, we propose that financial regulators ought to engage continuously with the regulated sector that is carrying out the delegated implementation of legal elasticity. Financial regulators would benefit from being apprised on an ongoing basis of information and problems "on the ground." Further, supervisory steering is needed in light of behavioral 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. In this manner, we reinforce the argument made in Proposal One that legal elasticity has to be managed, this time *relationally*, with those tasked to implement it, as well as those likely to be affected by or interested in the outcomes of implementing legal elasticity.

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

We propose that the relational management aspect of legal elasticity would include the following dimensions for practical application:

(a) The relational dimension amongst financial regulators and relevant policymakers. Crisis management by the public sector is often not assumed to be unitary due to the delineations between government bodies, independent agencies, and how government and bureaucracy is structured.[244]

(b) The relational dimension between regulated entities and their relevant regulators. This relationship is often fraught with depictions of capture,[245] polarisation, and excessive delegation (resulting in self-regulation).[246]. Although the regulated-regulator relationship remains a work in progress in regulation theory studies, this article suggests that constructive engagement is inevitable although relational dynamics may not be perfect.

(c) The relational dimension between regulators, policymakers, and stakeholders or society more broadly, as crisis management benefits from multi-stakeholder participation and drawing together of resources,[247] social mobilization, and solidarity.

One of the lessons from the global financial crisis for financial regulators was the need to coordinate amongst each other and with relevant government agencies and Treasury departments. After the global financial crisis, it is explicitly provided in UK legislation that crisis management should be coordinated between the Treasury, Bank of England, and PRA with respect to financial stability and public interest needs.[248] As the reform was inspired by the immediate needs of the crisis that related to financial sector instability, the FCA was not included. The exclusion of the FCA can be attributed to a lack of the perception of business conduct as being contributory to these objectives.[249] However, the financial stability crisis of 2007-08 was quickly followed by business conduct scandals in the banking industry.[250] As such, in this dynamic environment, there should be room to consider a wider and more permanent crisis management group including the FCA. Indeed, the management of the COVID-19 crisis also required the PRA and FCA to work in a coordinated manner so that the FCA's regulatory suspensions in consumer credit could be coordinated with the PRA's approach to microprudential regulation.

Although the regulated-regulator relationship has been depicted in relation to lobbying, informal "capture or sympathy,"[251] or excessive trust (especially before the global financial crisis),[252] it remains imperative that regulators maintain informational and supervisory proximity to the regulated. Omarova[253] argued, in the wake of the global financial crisis, that a system of tripartite financial regulation should be introduced where "bankers" and "bureaucrats" would enroll "guardians" who are stakeholders representing public interest to co-govern in the realm of financial regulation. This would allow public interest issues to be brought to bear in financial regulation, and weaknesses in the relational paradigm between the regulator and regulated to be moderated. Such a multipartite form of networked governance is consistent with and has always been envisaged in regulatory theory.[254] Perhaps there may be fear that diverse demands from multiple stakeholders may confuse the policy agenda. However, excluding voices or dialogue at a time of crisis management does not necessarily lead to more efficient or effective policy decisions. In Section IV, we discuss the dialogue between the FCA and the PEG which paved the way for the FCA's endorsement of the waiver of preemption rights and other regulatory suspensions included in the same communication. The support of relevant non-public sector actors and stakeholders can be important, especially if they play a catalyzing part in the introduction of legal elasticity or if their support may mitigate dissent and resistance. 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 (BEIS) of the Parliament's channel for feedback[255] from the business sector in relation to impact and needs. Such a channel is open to the public although the Committee may engage in further dialogue with select respondents.

C. Preparation for Crisis Management and the Role of Legal Elasticity

Finally, we suggest that if legal elasticity is to become a staple part of crisis management tools for financial regulators, or broadly as part of responsive regulation, regulators need to engage with it in an ex ante and sustained manner rather than in an ad hoc manner.

We propose that regulators should have a pre-crisis framework for thinking about the scope of and possibilities relating to legal elasticity, as preparedness is a quality that can be usefully honed and would be beneficial even if the actual crisis that materializes and needs to be managed is different from the one imagined.

Proposal Three: Financial regulators should put in place a pre-crisis framework for preparing for crisis management, including deploying legal elasticity. Pre-crisis preparedness goes some way towards the ex post management of institutional dissonance, discussed in Proposals One and Two.

It is useful for regulators to have a dedicated outfit for pre-crisis preparation, and wisdom may be borrowed from scenario planning literature in business management. Oliver and Parrett 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 perceptions in a more holistic manner, and to take stock of the existing suite of tools available to the business in imagining responses. This allows business leaders to develop alternative strategic options for possible responses, as they observe how the environment changes around them.

In a similar vein, pre-crisis preparation on the part of regulators can incorporate useful elements from scenario planning practice. In terms of gathering information, regulators' access to information, particularly from the financial sector, has increased dramatically after the global financial crisis. This is because of regulators' acknowledgement of their shortfalls in trusting markets and not having comprehensive and even granular information to map out the trends and risks in financial markets domestically and internationally. Hence, micro-prudential, conduct, and macro-prudential regulators in the UK and EU have vastly increased reporting and information return requirements. The current information environment for regulators is not anaemic by any means and provides a good starting point for developing greater preparedness for crisis management. However, such information should be regularly shared amongst regulators and policymakers in relational paradigms discussed in Proposal Two.

Next, regulators should map out the scope of their inherently flexible regulatory tools as these are designed with responsiveness in mind, as well as the likely effects entailing from their deployment. Maymin argues that regulators need to be aware that the timing and duration of interventions can promote regularization of dysfunctional markets but can also distort markets, and much depends on regulators' choice in timing and duration of interventions. Regulators can enhance their preparedness in considering scenarios in which flexible regulatory tools may be used and to what extent. This can contribute to more skillful judgment at the point of deployment. Crawford argues that although regulators cannot prepare for the exact types and extent of crises that occur, training to develop those judgments is beneficial. Indeed, he proposes a 'wargaming' approach in which the regulators design worst-case scenarios in different ranges of probability, in order to test the limits of inherently flexible regulatory tools that can be deployed. This may even be similar to stress-testing that regulators carry out for systemically important banks and financial institutions and would not be unfamiliar as a methodology to regulators.

Regulators' "wargaming" or "stress-testing" of inherently flexible tools may reveal their limits and the need for other flexibilities in other laws or regulations not hitherto explicitly flexible. This provides regulators with the opportunity to consider more holistically the needs for legal elasticity and possible effects in institutional dissonance. Although ex ante mapping is unlikely to be complete or exactly match a crisis, regulatory preparedness can be more optimally honed for the management of legal elasticity and the demands depicted in Proposals One and Two.

VI. Conclusion

The COVID-19 crisis has severely impacted economic activities globally, generating wide-ranging policy responses. A crucial piece of the mosaic of policy responses comes from financial regulation, as financial regulators have adjusted regulatory rules in order to allow the financial sector to meet the policy goals of rescue and relief. We argue that although the twin policy goals of relief and rescue meet the immediate needs of many households and corporations caused by unexpected stressful conditions, the regulatory suspensions introduced by financial regulators obscure hazards to regulators, regulated financial entities, households, and corporations, and may fall short of the policy goals desired. This is because such regulatory suspensions may not be as temporary as they seem and their impact on institutional stability should not be assumed to be minimal. The article situates the deployment of regulatory suspensions within the theoretical framework for legal elasticity developed in Pistor's legal theory of finance. We argue that legal elasticity brings about longer-term and structural effects, and gives rise to questions regarding institutional change. Regulators and policymakers' reluctance to engage with the structural nature of legal elasticity is pursuant to their perspective that regulatory suspensions during the COVID-19 crisis are only temporary. However, we critically caution that such reluctance to engage in institutional questions raised by deploying legal elasticity risks greater hazards to legal certainty, institutional stability, and ultimately policy outcomes in due course.

We make a series of recommendations to improve financial regulators' decision-making processes relating to regulatory suspensions. These recommendations are built upon our overarching argument that regulatory suspensions need to be understood in the fullness of the theoretical framework for legal elasticity. We not only draw upon but also extend Pistor's legal theory of finance to that end. First, we propose that regulators should anticipate that institutional dissonance follows from deploying regulatory suspensions and should proactively seek to evaluate all relevant aspects and considerations pertaining equally 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 to be better prepared for engagement with this complex regulatory tool. These approaches facilitate more richly considered and holistic decision-making on the part of regulators and policymakers, even if it is not perfectly clear what substantive policies may work optimally in an economic crisis such as that induced by the COVID-19 pandemic.

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July 1, 2047: Doomsday for Hong Kong Property Law?

By Saraphin Dhanani

I. Introduction

On the morning of June 9, 2019, Hong Kongers flooded the streets to protest the pernicious erosion of their fundamental rights and freedoms by the People's Republic of China (PRC), including the right to a democratic form of government; the right to speak freely and to protest openly; and perhaps most importantly, the right to due process in a territory historically governed by the rule of law.[1] These rights, though typical of Western democracies, were not unfamiliar to the people of Hong Kong. They were stitched into the very fabric of the territory and codified in the Sino-British Joint Declaration[2]—the 1997 treaty signed by the United Kingdom and the PRC to mark the official end of the UK's 99-year leasehold of Hong Kong and its handover to the PRC.[3]

The Sino-British Joint Declaration set up a new framework of governance between Hong Kong and China, known as One Country, Two Systems. This framework allowed Hong Kong to continue to enjoy its distinct political and economic rights for fifty years until July 1, 2047 when the PRC would have full authority to integrate Hong Kong into the Mainland.[4] The details of this framework were codified in a document written by the PRC known as the Basic Law which became Hong Kong's de facto constitution. Under the Basic Law, the rights to press, speech, and assembly were explicit as well.[5]

But early last year, pro-democracy Hong Kongers who had so fervently taken to the streets to protest the erosion of their freedoms for nearly nine months were forced to retreat back into their homes. The rapid spread of COVID-19 quashed any public demonstrations for several months. Chinese leader Xi Jinping took advantage of a lull in the protests and introduced a national security bill, the "Law of the People's Republic