ASIA-PACIFIC FINANCIAL FORUM

2017 Progress Report to the APEC Finance Ministers

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Asia-Pacific Financial Forum

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EXECUTIVE SUMMARY

The ongoing debate on globalization underscores the need for structural reforms to go hand in hand with trade and investment liberalization for the latter's fruits to be more broadly and equitably shared. The widening social and geographical income gaps in many economies and the persistence of huge current account imbalances that have fueled trade frictions have contributed to the notable erosion of public support for globalization over the past few years. These challenges cannot be met by retreating to protectionism. They can be met by advancing efforts to adapt our legal, policy and regulatory frameworks to the economic realities of the 21st century, to enable entire societies, not just a few, to seize the opportunities of globalization.

In the wake of the Global Financial Crisis (GFC), the APEC Business Advisory Council (ABAC) called attention in its 2009 Report to the APEC Finance Ministers to the "great need to promote domestic demand [in Asian developing economies] and correct the huge global imbalances that have built up over the previous decades." To this end, in the same report, ABAC recommended "the launch of an APEC Financial Inclusion Initiative and the promotion of infrastructure development through a regional partnership among governments, business and international financial institutions", "the enhancement of social safety nets, including social insurance and pension systems… and the strengthening of credit reporting systems to facilitate the growth of consumer finance."

In the years that followed, APEC Finance Ministers echoed these recommendations in their Kyoto Report on Growth Strategy and Finance and the launch of the Asia-Pacific Forum on Financial Inclusion in 2010, the establishment of the Asia-Pacific Infrastructure Partnership (APIP) in 2011, the creation of the Asia-Pacific Financial Forum (APFF) in 2013 and the various activities under the Finance Ministers Process to advance greater access to finance, infrastructure investment and financial market development and integration. In 2015, the Ministers incorporated key recommendations from the private sector in their Cebu Action Plan (CAP) and encouraged APFF to actively engage in advancing several initiatives in the CAP's financial integration, financial resilience and infrastructure pillars.

This Progress Report provides an update on this work. Among the initiatives in the CAP are promoting an enabling financing environment for MSMEs, including trade, supply chain and alternative financing mechanisms; expanding financial inclusion and literacy; facilitating the cross-border offering of funds through the Asia Region Funds Passport; developing disaster risk financing and insurance across the region; developing local currency bond markets in APEC economies and a roadmap to promote financial infrastructure; and various initiatives to promote bankable infrastructure projects and long-term investment in them.

The APFF is currently undertaking work to progress these initiatives. These include work that has been started in previous years in the following areas:

- Collaboration in capacity building to assist interested economies in developing their financial infrastructure, in particular credit information, secured transactions and insolvency systems to facilitate and expand MSMEs' access to credit;

- Regional workshops to help relevant agencies, financial institutions and global supply chain participants identify barriers to trade and supply chain finance, innovative solutions to address these challenges and opportunities for collaboration;

- Regional public-private sector dialogues on advanced technology in finance (fintech), particularly in the areas of lending, payments and regulatory technology (regtech) to promote collaboration among regulators, industry participants and experts in developing balanced regulatory approaches;

- Workshops to assist relevant stakeholders in interested economies, including regulators and industry participants, in identifying and addressing legal, policy, regulatory and market issues to enable the effective use of repurchase agreements (repos) and over the counter (OTC) derivatives for the purpose of improving the depth and liquidity of bond markets;

- Collaboration with regulators and industry to assist in progressing and increasing membership in the Asia Region Funds Passport;

- Advice to regulators of interested economies in implementing the APFF self-assessment templates to improve availability and quality of information for capital market investors in three key areas: issuer disclosure, bond market data and investor rights in insolvency;

- Development of recommendations for expanding the role of the pension fund and insurance industries as long-term investors in infrastructure projects and capital markets;

- Discussions and conferences to address policy and practical barriers to the expansion of cross-border investment in infrastructure by Islamic financial institutions; and

- International conferences to discuss broader global and regional issues and their implications for financial market development and integration in the Asia-Pacific region.

This year, APFF commenced work on two initiatives mandated by the CAP:

- The drafting of a proposed roadmap for the development of the region's financial market infrastructure; and

- The drafting of a proposed roadmap for expanding the coverage of microinsurance in developing Asia-Pacific economies.

Finally, the APFF is currently planning ways to advance the CAP's mandate to establish and promote private disaster insurance schemes, develop regional risk sharing measures and develop a roadmap for expanding the private sector's role in disaster risk financing and insurance.

This report also highlights the growing interest of APEC member economies to engage with the private sector in a wide variety of areas and confirms the importance of the CAP to the region's economic development. This year, the APFF made progress in starting new collaborative activities with various economies, such as in capital market development (with China and Thailand) and credit information and secured transactions (with Vietnam). The commencement of work on the roadmaps for developing financial market infrastructure in the Asia-Pacific region and for expanding the coverage of microinsurance has further broadened the areas for public-private sector collaboration in advancing the goals of the CAP.

Progress also continues to be made in the ongoing work on credit information and secured transactions work in the Philippines and Thailand, advancing a pilot project on cross-border sharing of credit information in the Mekong region, the development of a platform for public-private sector dialogue on fintech, support for the Asia Region Funds Passport, creating a platform for enabling Islamic financial institutions to expand cross-border investment in infrastructure, expanding the role of pension funds and insurance firms in infrastructure, and promoting a more active private sector participation in disaster risk financing and insurance.

To help advance the implementation of the CAP in coming years, this report recommends the following to the APEC Finance Ministers:

1. **Encourage relevant officials and regulators to collaborate with APFF's capacity building activities in:**
   - **promoting deep and liquid bond, repo and derivatives markets;**
   - **modernizing credit information, valuation, secured transactions and insolvency systems;**
   - **developing pilot programs for cross-border supply chain financing; and**
   - **expanding long-term investors' roles in infrastructure development.**

2. **Support APFF's efforts to develop a regional platform for public-private dialogue on harnessing fintech to create inclusive, sound and efficient financial systems.**

3. **Encourage senior finance officials to work with APFF in 2018 to finalize the roadmaps envisioned in the CAP for:**
   - **developing the region's financial market infrastructure;**

- **expanding the coverage of microinsurance; and**
- **promoting greater private sector participation in disaster risk financing and insurance.**

4. **Encourage more economies to host discussions on the Asia Region Funds Passport (ARFP) where APFF can convene experts from regulatory, industry, multilateral and academic institutions.**

5. **Encourage relevant authorities to collaborate with APFF in finalizing in 2018 a work program for the Islamic Infrastructure Investment Platform (I3P) to help expand cross-border investment by Islamic financial institutions in infrastructure.**

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Introduction

The debate on globalization, long thought of as resolved, has reemerged to become the defining theme of recent political discourse. While this debate involves a complex set of issues, much of it has been fueled by discontent among parts of the electorate in developed economies that saw themselves as adversely affected by open trade policies and greater freedom for commercial enterprises to choose where they wish to do business and create jobs.

Globalization can be disruptive, insofar as it enables businesses and consumers to seize opportunities across multiple markets at different levels of development that offer varying comparative and competitive advantages. In our region, this has been reflected in the growth of cross-border investment and supply chains. It has also led to huge trade imbalances among economies and the migration of jobs, especially in many traditional manufacturing sectors, from developed to developing economies.

Predictably, trading arrangements and practices have been convenient targets of blame for these trade imbalances, and protectionist measures promoted as the logical response. However, the fact that some developed economies have performed better than others under the same globalized regime suggests that the quality of policy and regulatory ecosystems affecting the international competitiveness of businesses has as much, if not more, to do with the outcomes than trade policies.

While it may appear that developing economies have benefited disproportionately from globalization, there is also a growing realization that growth strategies focused mainly on exports and related investment are not sustainable over time. The damaging impact on emerging markets of the collapse of consumer demand in developed economies following the Global Financial Crisis prompted this rethinking, which eventually came to be reflected in the APEC Finance Ministers' decision to adopt the Kyoto Report on Growth Strategy and Finance in 2010.[1]

An important element of this rethinking is the move to shift toward a more balanced economic growth strategy that raises the role of domestic consumption in the economy relative to exports and investment, which will also help address trade imbalances. There is much to be done in this regard. The East Asia and Pacific region's

[1] "Against this backdrop, we discussed and adopted "The Kyoto Report on Growth Strategy and Finance" today, which we believe will contribute to the discussion of the APEC Leaders' Growth Strategy. In this Report, we highlight the importance of strong, sustainable and balanced growth in the future, as well as the importance of fostering sound fiscal management, particularly in light of the challenge posed to public finances by aging populations. We also draw attention to the importance of securing appropriate financing as a critical component of growth, competitiveness, employment and poverty reduction, particularly: enhancement of infrastructure finance, and improvement of access to financing for micro, small and medium enterprises and households." APEC Finance Ministers, *The Kyoto Report on Growth Strategy and Finance*, 2010.

household consumption currently amounts to 49 percent of its GDP, compared to North America's 67 percent. Combining the ratios of exports and gross capital formation to GDP, the figure for East Asia and Pacific is 63 percent, compared to 35 percent for North America.[2]

The factors behind the low level of household consumption in many Asian emerging markets are complex and manifold. Various studies in China, which is now striving to promote domestic consumption, indicate that among the key inhibitors of household consumption growth are the lack of pension and health insurance,[3] lack of access to consumer finance, financing constraints on the growth of the MSME sector and its ability to provide more employment opportunities,[4] and the lack of infrastructure and investment in rural areas.[5]

Finance plays an important role in addressing these issues, and it is noteworthy that the Cebu Action Plan (CAP) includes a number of initiatives that are geared towards this objective. These include promoting an enabling financing environment for MSMEs, including trade, supply chain and alternative financing mechanisms; expanding financial inclusion and literacy; facilitating the cross-border offering of funds through the Asia Region Funds Passport; developing disaster risk financing and insurance across the region; developing local currency bond markets in APEC economies and a roadmap to promote financial infrastructure; and various initiatives to promote bankable infrastructure projects and long-term investment in them.

The APFF is currently undertaking work to progress a number of initiatives under the CAP. These include work that has been started in previous years in the following areas:

- Collaboration in capacity building to assist interested economies in developing their financial infrastructure, in particular credit information, secured transactions and insolvency systems to facilitate and expand MSMEs' access to credit;
- Regional workshops to help relevant agencies, financial institutions and global

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2 World Bank, *World Development Indicators*.

3 See for example a recent study on consumption among migrant workers in China, which concludes that the lack of pension and health insurance is a major contributor to the low level of domestic consumption among these population groups, Xin Meng, Sen Xue and Jinjun Xue, "Consumption and Savings of Migrant Households 2008-14," in Ligang Song, Ross Garnaut, Cai Fang and Lauren Johnston (Eds), *China's New Sources of Economic Growth: Reform, Resources and Climate Change*, Volume 1 (Canberra: ANU Press 2016), pp. 159-196.

4 This is described in Zeng Gang and Li Guangzi, "Consumer Finance and its Significance," in Guogang Wang, Gang Zeng and Xuan Xiaoying (Eds), *Development of Consumer Demand in East Asia* (Palgrave MacMillan 2017). The authors also define consumer finance as including (a) payment, (b) risk management, (c) credits, and (d) savings.

5 A recent analysis of consumption patterns in China's urban and rural areas concluded that the government's efforts in recent years to improve rural infrastructure, including transportation, electricity and communications stimulated consumption in small towns and rural areas and significantly narrowed the urban-rural divide in consumption, especially of electrical appliances and durable home appliances, Li Chunling, "Urbanization and the Urban-Rural Consumption Divide," Zheng Yongnian, Zhao Litao, Sarah Y. Tong (Eds.), *China's Great Urbanization* (London and New York: Routledge 2017), p. 52.

supply chain participants identify barriers to trade and supply chain finance, innovative solutions to address these challenges and opportunities for collaboration;

- Regional public-private sector dialogues on advanced technology in finance (fintech), particularly in the areas of lending, payments and regulatory technology (regtech) to promote collaboration among regulators, industry participants and experts in developing balanced regulatory approaches;

- Workshops to assist relevant stakeholders in interested economies, including regulators and industry participants, in identifying and addressing legal, policy, regulatory and market issues to enable the effective use of repurchase agreements (repos) and over the counter (OTC) derivatives for the purpose of improving the depth and liquidity of bond markets;

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- Development of recommendations for expanding the role of the pension fund and insurance industries as long-term investors in infrastructure projects and capital markets;

- Discussions and conferences to address policy and practical barriers to the expansion of cross-border investment in infrastructure by Islamic financial institutions; and

- International conferences to discuss broader global and regional issues and their implications for financial market development and integration in the Asia-Pacific region.

This year, APFF commenced work on two initiatives mandated by the CAP:

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- The drafting of a proposed roadmap for expanding the coverage of microinsurance in developing Asia-Pacific economies.

Finally, the APFF is currently planning ways to advance the CAP's mandate to establish and promote private disaster insurance schemes, develop regional risk sharing measures and develop a roadmap for expanding the private sector's role in disaster risk financing and insurance.

This report is divided into five sections, under which the progress of these initiatives are described:

- Expanding MSMEs' Access to Finance
- Creating deep, liquid and integrated capital markets
- Expanding the region's long-term investor base
- Fostering financially resilient communities
- Dialogue and research on the future of financial regulation

EXPANDING MSMES' ACCESS TO FINANCE

Micro-, small and medium enterprises (MSMEs) are the most important contributors to employment and innovation in Asia-Pacific economies. Thus, enabling MSMEs to effectively participate in economic activities and global value chains, including domestic commercial activity and access to international markets and export opportunities, has always been an important objective for APEC. Accessing finance is a key challenge for most MSMEs, due in large part to inadequate legal and institutional infrastructure to support risk-based lending using transaction data and the use of a wider range of assets, especially movable assets, as collateral.

The Finance Ministers have identified these issues as priorities and incorporated them in the CAP, which called for the establishment of the Financial Infrastructure Development Network (FIDN) within the APFF as a platform for collaboration among the private sector, finance ministries, regulatory agencies and other stakeholders to support member economies in developing their credit information, secured transaction and insolvency systems. The FIDN was launched in 2015 and following this, various activities were held in the Philippines, China, Brunei Darussalam, Thailand and Vietnam.

In addition to financial infrastructure that enable lenders to expand credit to MSMEs using their movable assets as collateral, as well as transaction data of business owners, opportunities to finance business activities are also increasing as a result of new business models arising from the development of advanced technologies in finance (fintech). Recognizing these opportunities, the Finance Ministers through the CAP called for promoting the development of new financial instruments for MSMEs, addressing regulatory barriers to digital, mobile and innovative financing and developing policy frameworks for alternative finance.

Finally, the Finance Ministers also acknowledged the need to address challenges that hinder MSMEs from participating in international trade and global supply chains. MSME exporters have been disproportionately impacted by increased costs and risks from elevated penalties for non-compliance with rules, such as those related to customer due diligence, that financial institutions face in providing trade financing. The CAP included initiatives to develop regionally consistent rules to facilitate cross-border trade and supply chain finance. It also called for expanding the use of electronic supply chain management platforms; and facilitating digital, mobile and innovative working capital management techniques.

Credit information systems

Capacity building to develop domestic credit information systems

Since 2015, the FIDN has been undertaking activities to bring together experts from the private sector, international organizations and development institutions to provide advice to policy makers and regulators in several economies on reforms to create or improve their credit information ecosystems. In 2017, through the Asia-

Pacific Credit Coalition (APCC) and the Policy and Economic Research Council (PERC), FIDN continued to serve as a resource to Philippine stakeholders currently developing the credit information system. At the soft launch of the Credit Information Corporation (CIC)'s data sharing platform in Manila on April 24, APCC and PERC recognized the progress made by CIC in acquiring data in their repository that will increase access to finance for MSMEs and individuals across the economy.

In addition to work in the Philippines, the FIDN has been in dialogue with industry executives and government officials in Australia. In 2012, both Australia and New Zealand reformed their domestic privacy laws to permit lenders and other non-financial creditors to report both timely and late payment data to private credit bureaus—positions advocated by the APFF. While the credit information system has progressed steadily in New Zealand, Australia remains a negative-only credit reporting regime.

In March 2017, the Australian Productivity Commission issued an interim report calling for industry to accelerate the reporting of full-file data to private credit bureaus (a target of 40 percent coverage by mid-2017 was set) or else face a mandate to do so. The Final Report of the Productivity Commission, issued in May, extended the deadline for the coverage target to December 31.[6] Given these developments, FIDN is now considering to be active in Australia both on full-file credit reporting and cross-border credit information sharing in 2018 as Papua New Guinea (PNG) assumes the chairmanship of APEC. Cross-border credit data flows between Australia and other Pacific Island nations, including PNG, is of growing interest.

Privacy regime development and credit information

FIDN stakeholders, including ABAC, the International Finance Corporation of the World Bank Group (IFC/WBG) and the People's Bank of China (PBOC) jointly organized a conference on Personal Data Protection and Credit Reporting on 20-21 April in Beijing. The event focused on the increasingly important topic of data privacy under the new environment that financial institutions are collecting, processing and increasingly using more data.

The senior leadership members of PBOC gave keynote addresses and announced a revised direction for the development of the credit reporting market in China. About 150 policy-makers, regulators and industry executives attended the conference including speakers and participants from several APEC economies (Korea, Hong Kong, Thailand, New Zealand, USA). The conference attracted extensive news coverage.

In recent years, numerous data and analytics players have emerged in China with many claiming to be doing credit reporting or credit reference. Among others, the two-day discussions helped to clarify the difference between credit bureaus and data

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6 Australian Government. Productivity Commission, *Data Availability and Use* [Productivity Commission Inquiry Report No. 82, 31 March 2017], http://www.pc.gov.au/inquiries/completed/data-access/report/data-access.pdf.

companies and risk management firms. The discussions underscored the need for a modern personal data protection framework that balances the interests of businesses and the privacy of consumers. It is expected that the Chinese market will gradually evolve into a tiered structure with a few real comprehensive credit bureaus, a number of specialized credit reporters and many other data and risk management companies.

Preparing the way for future cross-border credit information sharing

FIDN is currently undertaking preparatory work on the CAP's initiative to develop a pathway to a common data dictionary for the region, which is a key step toward making cross-border credit information sharing possible. At the APEC Seminar on Cross-Border Credit Information Sharing on 16 May, in Ninh Binh, Viet Nam, in conjunction with the APEC Senior Financial Officials' Meeting, as well as at the Roundtable Discussion on Cross-border Credit Information in the Mekong Region convened by ABAC and IFC/WBG on 13 July in Hoi An, Viet Nam, participants discussed the outline of the data dictionary.

FIDN is also hosting discussions about a pilot project on the sharing of cross-border credit information involving five economies in the Mekong region, including three APEC member economies (China, Thailand and Vietnam) and two others (Cambodia and Laos) that could potentially indicate a way forward for other APEC economies as well as help assess its beneficial impact on MSMEs doing business across borders. Following an initial workshop held in July 2016 in Bangkok, ABAC, IFC/WBG and the State Bank of Viet Nam jointly organized the previously mentioned Ninh Binh seminar.

The main objectives of the seminar were to (a) promote cross-border credit information exchange in the region, (b) address the key elements of cross-border credit information exchange mechanism, (c) present the Mekong initiative of the cross-border credit information exchange, and (d) discuss next steps. The seminar was attended by nearly 100 participants from 21 APEC economies' central banks, global credit reporting service providers (CRSPs), industry associations, local stakeholders and other international organizations.

During the seminar, the speakers discussed the following topics: (a) the need for cross- border credit information in the context of increasing trade and foreign direct investment flows and intra-regional migration; (b) economies' perspectives on the topic; (c) the World Bank Group's general principles on cross-border credit information exchange; (d) the legal and data elements in a successful mechanism; and (e) the way forward.

Participants shared experiences in the Mekong region as well as in Europe, particularly on the role of regulators in promoting cross-border credit information exchange, the relationship between regulators overseeing credit reporting and general data protection, and what CRSPs should advocate to the regulators. Speakers from the industry association and regional CRSPs discussed the conditions for successful cross-border information sharing and mechanisms for data subjects to exercise their rights in a foreign jurisdiction to amend incorrect information.

Participants discussed the next steps following the agreement on basic guidelines among eight regional CRSPs reached at the July 2016 meeting in Bangkok and the agreement on the text of a draft memorandum of understanding between two CRSPs in different jurisdictions.

Further discussions were held at the 13 July Roundtable Discussion in Hoi An. Participants discussed the challenges arising from laws in certain jurisdictions that prevent the transfer of credit information across borders as well as from regulators' hesitancy to allow such cross-border sharing of information in the absence of clear laws. Next steps identified to advance the pilot project include (a) the use of informal mechanisms such as exchange of letters among CRSPs that have been successfully implemented and allowed in participating jurisdictions; (b) informal outreach efforts to key regulators; and (c) undertaking continued advocacy efforts focused on communicating the benefits of cross-border credit information sharing to key decision-makers in participating economies.

Finally, a baseline analysis of the current state of credit information sharing across the 21 member economies of APEC is being undertaken for FIDN by PERC and the APCC. The survey instruments are currently being designed by PERC with input from the IFC/WBG and industry advisors, and will be in the field in late 2017. The baseline results will be published either in late 2017 or early 2018.

Secured transactions and insolvency regimes

The Secured Transaction Reform (STR) sub-stream of the FIDN aims to promote an enabling environment based upon clear and predictable legal frameworks for economic development and inclusive growth. Its work is specifically focused on facilitating a diverse set of financing solutions for MSMEs, market infrastructure projects and cross-border trade and supply chains. ABAC, IFC/WBG, partnering private sector organizations and the OECD are collaborating with a broad range of institutions including international organizations, public sector bodies, private sector firms, and academic entities within interested economies.

Through workshops, direct policy maker outreach, dialogues and studies, this sub-stream seeks to:

- *Support reform* and development of secured transactions systems and insolvency frameworks among APEC economies;
- *Promote good practices and internationally accepted principles* on secured transactions legislation, including comprehensive definitions of eligible collateral, the free assignability of claims for the purposes of financing, and other provisions shown to enhance the ease of credit for MSMEs;

- *Foster the establishment and development of effective modern collateral registries* and promoting pathways to single, central and online security interests notice filing systems and comprehensive coverage of security interests on movable assets, receivables and other forms of intangible assets within the economy; and
- Partner with local economy stakeholder to *improve the capacity of lenders* in structuring, delivering and managing credits based on movable assets, receivables and other forms of intangible assets as well as the *development of the necessary operational infrastructure* such as third-party collateral management industries, electronic finance platforms and credit enhancement services to support the expansion of such credits for MSMEs, agri-business operators, domestic and cross-border traders and infrastructure companies, among others.

Since its launch in November 2015, FIDN has developed a network of leading experts in secured transactions reform to support member economies. This network encompasses multilateral development agencies, leading industry trade groups, private sector lenders, academic think tanks and universities, leading legal experts, and collateral registry officials. This diverse network provides member economies with simple, cost efficient access to global best practices and expertise across the necessary elements to achieve modern secured transaction reform, including areas such as:

- *Legislative / Model Laws*: FIDN members include experts from IFC/WBG, UNCITRAL, the US Department of State, the Hong Kong Department of Justice, the United States Agency for International Development (USAID), National Law Center, university professors, and consultants with experience in working with economies to develop modern secured transaction regimes.

- *Collateral Registry Development*: FIDN members include the Australian Financial Security Authority (Collateral Registry Registrar), the Ministry of the Economy of Mexico, and the Land Registration Authority under the Philippines' Department of Justice.

- *Training / Capacity Building*: FIDN members include the Commercial Finance Association, the predominant industry trade group for asset-based lending; and the combined International Factors Group/Factors Chain International (IFG-FCI), the leading global factoring trade organization. These trade groups, additionally joined by IFC/WBG and its experts, have deep resources and experience in providing training and capacity building to lenders and factors globally.

FIDN has also actively engaged with the Strengthening Economic Legal Infrastructure (SELI) group of the APEC Economic Committee to promote reform efforts across APEC member economies. Members of SELI have actively participated in FIDN update calls and workshops (most notably, the FIDN Conferences on Credit Infrastructure in Manila in March 2016 and in Hoi An in July 2017). Additionally, FIDN stakeholders participated in the APEC Seminar on the Use of International Instruments to Strengthen Contract Enforcement in Supply Chain Finance for Global Businesses (including SMEs) in Nha Trang, Vietnam in February 2017.

2016 Legislative and Legal Updates

In 2016, modernized secured transactions laws in both Thailand and Brunei Darussalam became effective. Brunei Darussalam launched its modern collateral registry in December 2016. In July, a new modern secured transactions law was introduced in the Philippine Congress, with passage expected within 2017. Vietnam implemented its new modernized law effective as of 1 January 2017.

UNCITRAL completed work on the Model Law on Secured Transactions, which was adopted at its convention in July. Additionally, the previously adopted Convention on Assignment of International Receivables, adopted in 2001 but not yet ratified, was submitted by then-President Obama to the US Senate for ratification. If ratified by the US, it is expected that additional UN jurisdictions will quickly follow suit, clearing the way for its effectiveness.

2016-17 FIDN Activity Summary

Since its launch, FIDN has provided expert advice to interested member economies, including the Philippines, Brunei, China, Vietnam and Thailand. Following a number of activities outlined in the 2016 APFF Progress Report to APEC Finance Ministers, various follow-up activities were undertaken by FIDN in the area of secured transactions and insolvency.

In August 2016, FIDN co-sponsored a workshop with the Bank of Thailand, in partnership with the Thai Bankers' Association, to support the introduction of the recently enacted secured transaction law, the Business Collateral Act, for policymakers, regulators and industry participants focusing on supply chain finance.

In October 2016, FIDN partnered with IFC/WBG, the government of Viet Nam and the Vietnam Banks Association to hold a Supply Chain Finance workshop in Ho Chi Minh City to further capacity building and awareness among lenders and SMEs in Vietnam of the recently implemented secured transaction law.

In November 2016, FIDN cooperated with IFC/WBG and the Supreme People's Court of Viet Nam in holding the Forum for Asian Insolvency Reform (FAIR) in Hanoi to build cross-specialty support among regional insolvency practitioners of the current secured transactions reform efforts across the region.

In December 2016, FIDN members provided support to IFC/WBG in promoting moveable asset finance in the Mekong Region, continuing to build regional capacity building, awareness and support for development of modern secured transactions laws and related infrastructure in the region.

In December 2016, FIDN stakeholders again partnered with the Government of the

Philippines in holding the 3rd FIDN Conference on Credit Infrastructure in Manila in a two day conference widely attended by policymakers, regulators, financial institutions and MSMEs. The conference highlighted the progress of the pending legislation in Congress and showcased unique and related financial infrastructure support for expanding MSMEs' access to credit being developed in the Philippines showing continued development growth and capacity building.

FIDN participated in the 1st Secured Transactions Coordination Conference sponsored by the University of Pennsylvania Law School and National Law Center which brought together academic, professionals and experts from multilateral development agencies to share best practices and enhance the effectiveness of secured transactions reform globally.

In February 2017, FIDN stakeholders participated in an APFF Conference on Creating an Effective MSME Financing Ecosystem in partnership with the Thai Bankers Association. The conference leveraged the rich knowledge and real world experience of private firms, public agencies and international organizations to provide an opportunity to identify strategies to accelerate the expansion of MSMEs' access to finance, including the areas of digital finance, digital payment platforms for cross-border finance, sharing of best practices on improving policies and regulations to address disincentives for bank lending to MSMEs.

On 12 July 2017, APFF, the State Bank of Viet Nam and IFC/WBG jointly convened the 4th FIDN Conference on Financial Infrastructure Reform in Hoi An. This conference focused on secured transactions reform region-wide and in key APEC economies, focusing on progress in Vietnam and Philippines, with strong participation from both economies. Key sessions included discussions on tackling legal reforms through the legislature, key legal provisions of a modern secured transaction law, judicial support, interpretation and implementation, and the importance of valuation practices in secured transactions reform implementation. The conference presented views from a wide range of constituents, including regulators, policymakers and private sector practitioners.

FIDN is also currently undertaking work in collaboration with SELI in preparation for their 5th Meeting, where their work focuses on online dispute resolution.

FIDN and ABAC will co-organize with the IFC/WBG and CAWD (China Association of Warehouses and Delivery under the Ministry of Commerce) the 5th Warehouse and Collateral Management Conference, which will be a 1.5-day event for bankers, policy makers, collateral managers and other relevant stakeholders. The first half-day will be about the Property Law and advocacy on the upcoming secured transactions chapter of the Civil Code.

Additionally, FIDN will participate in the APEC SME Finance Forum on 11 September in Ho Chi Minh City, and the APFF Trade and Supply Chain Finance Workshop in Thailand on 17 October, as well as provide additional support in convening workshops and roundtables in member economies, such as the Philippines and Brunei.

FIDN stakeholders also participated actively in key industry conferences, in particular the Global trade Review conferences in Hong Kong and Singapore, to advocate wider support for the reform of secured transactions laws in APEC.

In the short period since its launch in November 2015, FIDN has built a broad network of experts, enhanced and expanded its support of the reform efforts in the Philippines, and initiated supporting activities with Brunei, Thailand, Vietnam and China. FIDN hopes to build upon these successes with each of the economies through continued workshops and capacity building, as well as further support additional interested member economies.

Trade and supply chain finance

This year's APFF Workshop on Trade and Supply Chain Finance, convened on 7 April 2017 in Singapore, focused on digital trade. The discussions were set against the backdrop of a global trading environment that has been shaped by continued austerity and is facing political headwinds. While there are economic cyclical improvements, the future remains clouded by uncertainties. In a Pacific Economic Cooperation Council (PECC) survey of APEC policy makers,[7] the top risks to growth (demand side) included a slowdown in global markets (particularly in China) and a failure to implement structural changes. Protectionism was noted to be on an upward trend. There are also supply-side constraints including infrastructure, institutional quality, education and capacity.

The workshop discussed inhibitors to digital trade which included paper-based manual processes and a lack of real-time information, as well as an emerging tool-set including the Internet of Things (IoT) and distributed ledger technology (DLT) that may provide solutions. Participants concluded that digital trade is more than just digital tools and that technology and business practices are moving ahead of laws and regulations. They also agreed that modernization of legal infrastructure is key to reducing legal risks and to ensuring long-term sustainability of digital trades. The workshop identified three key issues:

- *Legal environment for supply chain finance.* Participants agreed that a legal environment that facilitates supply chain finance and new technologies supporting it is necessary. As explained by one of the speakers,[8] supply chain activity involves banks, traders, transport entities, and customs officials, among others. Consequently, an enabling legal environment requires a fresh "whole of supply chain" approach, instead of treating each legal area impacting supply chain finance as a silo. It must encompass all relevant laws that govern digital/crypto-currencies, electronic transferable documents (such as digital bills of lading), cybersecurity and the issue of cross-border data flows, tax, and evidentiary value of digital documents and their ultimate enforceability in courts

7 Pacific Economic Cooperation Council (PECC), *State of the Region 2016-2017*.

8 Prof. Locknie Hsu, Professor of Law, Singapore Management University.

and other commercial tribunals. The legal status of digital trade documents is important as a fundamental facilitator of cross-border digital trade.

- *Cybersecurity.* Cybersecurity is the new "trust" and enabler for digital trade. Related to cybersecurity are the issues of cross-border data transfer and storage. In the region, various measures are currently being introduced to address cybersecurity risks, but these measures could end up creating new complexities if cross-border data flows become very costly and cumbersome. A healthy balance between cybersecurity and cross-border economic data flows needs to be found.

- *Trade ecosystem approach to anti-money laundering (AML).* Effective AML efforts in trade finance requires the collaboration of a wide range of participants across the trade ecosystem, including customs authorities, logistics firms and banks. Banks handle the financing documents and not the underlying goods that the documents represent. They do not have the wherewithal to ensure that the prices of the goods are not misrepresented, that there are no discrepancies between the quantity of goods being shipped and what invoices indicate, or that trade-based money laundering is not occurring in other similar ways. Banks recognize the need for trade-based AML and invest in such efforts. However, trade-based AML can only be effective with a trade ecosystem approach that digital trade can greatly facilitate.[9]

Overall conclusions and recommendations

Workshop participants made the following conclusions from the discussions:

- In the face of the growing digitalization of trade and supply chains, effective regulatory approaches will require a variety of expertise and skills and a holistic view of the trade ecosystem. Increasing demand for and wider adoption of cross-border digital trade will amplify this need.

- To encourage the healthy growth of cross-border digital trade, cross-ecosystem expertise should be harnessed in the earliest stages to develop digital trade-related law, cybersecurity and trade-based AML. This will be important for promoting a wider and more closely shared awareness of issues and better informed considerations leading to growth-centric measures.

Platform for regular public-private dialogue on fintech

The rapid evolution of advanced technologies in finance (fintech)[10] presents today's regulators with a critical challenge. New business models, new players

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[9] Bankers Association for Finance and Trade (BAFT), *Combatting Trade Based Money Laundering – Rethinking the Approach 2017.*

[10] These categories includes payments, insurance, planning, lending and crowd funding, block chain, trading and investment, data and analytics and security as described in OICV-IOSCO, *IOSCO Research Report on Financial Technologies (Fintech)*, February 2017., p. 4.

entering markets long dominated by traditional financial service providers, and the latter's embrace of new technologies are impacting regulators' mission of promoting financial stability, protecting consumers and privacy and maintaining the integrity of financial systems.

However, fintech also brings opportunities. Innovations are helping unbanked individuals and small businesses gain access to finance. New applications are enhancing business processes such as clearing and settlement, compliance, risk management and fund administration. Technologies such as blockchain and artificial intelligence are helping financial services firms improve their efficiency and responsiveness to customer needs. Emerging markets hoping to leapfrog their way to modernization will benefit from these innovations, but must adequately address emerging risks and concerns.

The impact of fintech has been most publicized in well-developed markets, particularly in Europe and North America, where favorable environments for start-ups exist and financial sectors are more diverse. In emerging markets such as those in Asia, the development of fintech has been uneven and concentrated in the areas of payments and credit, particularly marketplace or peer-to-peer (P2P) lending. Its impact is already being felt through greater access to finance in a growing number of economies. China still accounts for an overwhelming portion of fintech credit in Asia, while payments fintech has developed significantly across a broader range of markets.[11]

Nevertheless, the evolution and growth of fintech in Asian emerging markets continue to accelerate, requiring policy and regulatory attention. In two roundtables convened in 2016 under the auspices of the APFF,[12] policy makers and regulators agreed on the need to establish a regional platform to bring together stakeholders from the public and private sectors to help identify key issues in timely fashion as they arise. These stakeholders would include representatives from fintech startups and major financial institutions, related service providers, associations and experts, government and regulatory agencies and relevant international organizations.

To implement this agreement, ABAC and ADB jointly organized on 5 July 2017 at the ADB Headquarters an APFF workshop on the theme "Encouraging Innovation, Promoting Inclusion and Managing Risks" to bring together key stakeholders and discuss how to respond to this need. The workshop, held back-to-back with the ASEAN+3 Bond Market Forum (ABMF), was attended by financial regulators from

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[11] Sean Creehan and Nicholas Borst, "Asia's Fintech Revolution," *Asia Focus* (Federal Reserve Bank of San Francisco, February 2017). The APFF thanks the authors for insights that have helped in designing the structure of the workshop and guiding the discussions that are reflected in this section of the report.

[12] These were the ***APFF Roundtable on Financial Innovation: How can we harness innovation to build bigger, robust and inclusive financial markets?*** (24 February 2016, PayPal Corporate Campus, Silicon Valley, California, USA) and the ***APFF Roundtable on Financial Innovation: Fintech 2016: Challenges and Opportunities for Asian Industry and Regulators*** (15 July 2016, Co-organized by ABAC and ASIFMA and Co-hosted by the Hong Kong Monetary Authority, Hong Kong, China).

ASEAN+3 economies.

The workshop focused on two areas where significant disruption is already occurring in the region and where regulators are most concerned – payments and fintech credit. The workshop also discussed regulatory technology (regtech), where solutions in a number of key areas are being developed by industry and being tested or adopted by regulators, and provided an opportunity to share experiences in implementing regulatory sandboxes and discuss broader questions related to regulatory approaches and institutional arrangements.

Fintech Credit

Fintech credit (which includes marketplace or peer-to-peer lending, platform loans that are securitized and invoice trading) emerged to fill the financing needs of many households and small enterprises unable to obtain loans from traditional financial institutions. In Asia, this has mostly taken the form of online platforms that connect borrowers with investors. China has been by far the largest market for fintech lending in Asia, with characteristics that set it apart from other Asian markets, such as the predominance of consumer loans (as opposed to business loans) and retail investors (as opposed to institutional investors).

Despite its growth, however, fintech credit remains a small portion of the total credit market (only 3 percent in the case of China), and banks are expanding their presence by developing their online platforms or investing in start-ups. Regulation has been largely light-touch or negligible, with China among Asian markets having the most detailed focus on risk management, fraud prevention and consumer protection, while dealing with the challenge of a highly fragmented market that is not easily regulated. As fintech credit grows in volume and importance across the region, however, policy makers and regulators will need to pay increasing attention.

Participants discussed this issue, focusing on the evolution of technology, business models and regulatory responses in the areas of consumer and business fintech credit, and the use of data analytics and algorithms with respect to the development of financial identity.

Payments

The development of fintech in the payments sector is a major issue across various markets in Asia, as non-banks that largely played a supporting function vis-à-vis the banking sector in the past are now increasingly offering innovative financial services, driven by smartphone technology, Asia's huge market for payments and efforts to leapfrog old payment technologies. Many of these new services using mobile phone platforms do not alter the underlying structure of the payment system, as they continue to operate in conjunction with traditional bank accounts and credit or debit cards. However, others that provide digital wallets competing with banks and card networks for fee revenue or those offering new services such as insurance and investment promise to be more disruptive.

While still at a nascent stage, distributed ledger technology has the potential to provide speedier and more efficient clearing and settlement for trade finance, cross-border payment and syndicated lending, and smart contracts can fuel automatic payments and transfers. Wider adoption of these innovations would have disruptive effects as they replace legacy financial infrastructure currently being used, including trusted third parties such as clearing houses. The cost of remittances are likely to fall if mobile payment services, virtual currencies and pre-paid cards succeed in replacing bank-based transfers.

Adoption of these new technologies, however, face challenges in terms of regulatory frameworks (including compliance with AML rules), the lack of supporting infrastructure (e.g., availability of payment card readers) and issues intrinsic to the technology (e.g., volatility of virtual currency exchange rates). Asian regulators are responding to these challenges in various ways, undertaking research and conducting experiments. Participants discussed these issues and regulatory responses, particularly with respect to retail payments, distributed ledger technology for clearing and settlement, and digital currencies.

Regtech

While much attention has been given to the disruptive impact of fintech, technologies are being developed that can promote more effective and efficient attainment of key regulatory objectives and make compliance by regulated institutions with rules and regulations less costly and more aligned with the mission of providing inclusive and responsive financial services to the real economy. Regtech[13] solutions can help address a number of compliance and regulatory issues, including: risk data aggregation; modeling, scenario analysis and forecasting; monitoring payment transactions; identifying clients and legal persons; monitoring internal culture and behavior within regulated institutions; trading in financial markets; and identifying new regulations.

Among these solutions are those in areas such as machine learning, robotics, artificial intelligence, cryptography, biometrics, distributed ledger technology, application programming interfaces and shared utility functions and cloud applications.[14] Participants discussed regtech solutions that have been developed within the industry and are now being looked at by regulators, early results and responses so far, and the likely shape of future developments.

Regulatory Frameworks and Approaches

Even as fintech continues to evolve from its current early stages of development in the region, regulators are beginning to respond more proactively, especially in the

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[13] Regtech, as defined by the Institute of International Finance, is"the use of new technologies to solve regulatory and compliance requirements more effectively and efficiently," Institute of International Finance, *Regtech: exploring solutions for regulatory challenges*, Washington DC, October 2015.

[14] Institute of International Finance, *RegTech in Financial Services: Technology Solutions for Compliance and Reporting*, Washington DC, March 2016.

areas of payments and fintech lending. A number of regulators are turning to regulatory sandbox approaches that can support innovation by trusted partners, while closely monitoring and managing their impact on consumers and financial stability. The emergence of fintech has also lent greater urgency to finding practical solutions to key issues such as financial identity and the standardization of technology, and how existing regulations can be applied to new non-bank market participants.

Many regulators are revisiting fundamental questions, including whether to move away from regulating types of institutions toward regulating types of activities, how to achieve effective regulation across various institutions responsible for oversight of different financial subsectors and technologies, and what regulatory approach can best encourage innovation while enabling adequate risk management. Participants shared experiences and perspectives to contribute useful insights to regulators on how they can respond to the challenge of fintech.

The workshop also discussed the various responses of regulators to the emergence of new business models brought about by fintech. Regulators and industry participants agreed that it is still too early to make definitive conclusions on the way forward for the regulation of these new business models in the region, given the continuing rapid evolution of technology and the fact that fintech has not yet gone through a full credit cycle. However, regulators are responding by establishing mechanisms for cooperation to deepen their understanding of fintech, such as through the newly established ASEAN Financial Innovation Network (AFIN) and the continuing dialogue with industry and experts using the APFF platform.

CREATING DEEP, LIQUID AND INTEGRATED CAPITAL MARKETS

The capital market is a critical component of an economy's financial system. It plays a crucial role in promoting financial stability, economic growth, and the efficient channeling of long-term savings to investment in long-term assets like infrastructure. For this reason, the development of capital markets is indispensable for achieving the CAP's goals of promoting financial integration, resilience and infrastructure.

The lack of local currency bond markets was one of the main causes of the Asian Financial Crisis, which resulted from many economies' overdependence on bank lending in foreign currencies to fund long-term investments that yielded revenues in local currencies (the double mismatch problem). In the wake of the crisis, ABAC recommended to Finance Ministers the development of local currency bond markets, which gained traction a few years later with the launch of various initiatives that have led to the rapid growth of Asian government bond markets, a key stage in the process of capital market development.

To advance to the next stage, which would involve the expansion of private sector issuance and investment in and across markets, increasing market depth and liquidity will be critical. APEC Finance Ministers have incorporated into the CAP key initiatives to achieve this objective. These include the development of liquid repo markets, legal and documentation infrastructure facilitating risk mitigation, transparency of capital markets, a funds passport scheme, and a regional securities investment ecosystem to promote cross-border investment in capital markets.

Developing classic bond repurchase (repo) and OTC derivatives markets

This year, APFF continued to provide a platform for the private sector to dialogue with regulators and officials on practical steps to provide effective hedging instruments for market participants that can help improve market liquidity, especially repurchase agreements (repos) and over-the-counter (OTC) derivatives.

Developing classic bond repurchase (repo) markets is critical to the deepening of the region's capital markets and the real economy. Repo markets play an important role in increasing liquidity in local currency bond markets, expanding the pool of available finance, mobilizing collateral regionally, reducing funding costs for governments, pension funds, asset managers and other long-term investors and offering hedging tools which contribute to risk management.

Over the counter (OTC) derivatives also play important roles. They are used by firms to manage balance sheet liabilities and cash flows as well as hedge various economic risks, including interest rate and foreign exchange risks. A number of new regulations introduced to improve transparency, mitigate systemic risk and prevent market abuse are changing the landscape for these instruments, including in ways not intended but posing challenges in terms of their impact on hedging costs, bid-offer spreads and ease of trading. Emerging Asia faces additional risks of growing fragmentation with the emergence of a multiplicity of clearing systems handling relatively small transaction volumes.

Following previous seminars to undertake these dialogues in Manila, Philippines (in November 2015) and Jakarta, Indonesia (in April 2016), ABAC, the Asia Securities Industry and Financial Markets Association (ASIFMA) and the International Swaps and Derivatives Association (ISDA) convened further seminars on 22 February 2017 in Bangkok, Thailand and 16-17 March 2017 in Beijing, China in collaboration with other partner institutions.

APFF Workshop on Key Issues in Developing Thailand's Repo and OTC Derivatives Markets

This workshop, which was hosted by the Thai Bankers' Association, followed on the various steps that Thailand has already undertaken to create a classic repo market. Participants from the public and private sectors examined remaining actions to further develop the depth and liquidity of the repo market. During the workshop, experts from the industry and the private sector as well as government and regulatory agencies were on hand to discuss these issues.

Participants discussed the development of the private repo market, which consists of the repo transactions between dealers, or between dealers and clients without central bank participation. The Thai private repo market has many of the features which are essential for the development of a classic repo market, such as use of the Global Master Repurchase Agreement (GMRA) documentation and availability of close-out netting.

Nevertheless, market activity has not been as robust due to three main issues. First, market participants are not able to enter into cross border repo transactions. Second, the 0.46 percent surcharge imposed by the Bank of Thailand on deposits, including those stemming from repo business, has had a dampening effect on the level of activity. Finally, restrictions by the Securities and Exchange Commission on domestic funds (the country's largest investors) from lending out their bond inventory (as it is viewed as a form of borrowing) decrease the availability of bonds for repo transactions.

Participants also discussed a summary of the fundamental provisions of the GMRA 2000, key differences between GMRA 2000 and GMRA 2011, the 2011 GMRA Protocol, and recent case law relating to GMRA and repo documentation.

The discussions on OTC derivatives focused on the impact of the margin requirements for non-centrally cleared derivatives as agreed by the Basel Committee on Banking Supervision (BCBS) and the International Organization of Securities Commissions (IOSCO), and of the Basel capital reforms. Participants were briefed by ISDA on the timeline of the global regulatory roll-out of the margin requirements, a comparison of final rules by jurisdiction and the impact on Thai financial institutions.

Among the key messages from the discussions are the following: (a) Thai banks are caught by foreign regulations because of their trading partners. (b) Foreign trading partners contribute important liquidity to meet the hedging needs of the Thai economy; (c) The time required to negotiate new credit support annexes (CSAs), which are legal documents that regulate collateral for derivative transactions, should not be underestimated. (d) It is recommended to prioritize signing with one or more international counterparts first to maintain access to international liquidity. (e) Market participants should be prepared to meet the operational challenges of T+1 margin settlement.

The discussions on Basel capital reforms included a review of the evolution from Basel I to Basel IV, the key takeaways and industry concerns regarding the fundamental review of the trading book (FRTB), the leverage ratio and the net stable funding ratio (NSFR). The key message from the discussions is that the new Basel capital rules will have a disproportionate impact on emerging markets, and prudential regulators from these markets should carefully consider the proposals before casting their Basel Committee votes.[15]

APFF Workshop on Corporate Bonds, Repo and Derivatives Markets Development in China

ASIFMA hosted an APFF workshop convened jointly by ABAC, ASIFMA and ISDA on 16-17 March 2017 in Beijing. The conference was essentially divided into three streams: China bond market development, OTC derivatives market development and repo market development. The repo market development stream focused on how a centralized and unified repo market would work in China and on the development of China's repo market, which currently has three types of repos available, and the challenges facing the development of a classic repo market. It was concluded that the market is still overwhelmingly done on a pledged repo basis and there is a lack of clarity on close-out netting. Adoption of messaging standards and investment in infrastructure to handle margin management are some of the areas identified as helpful for the development of classic repo market in China.

Participants also discussed the legal documentation for repos, where a comparison of the repo documentations of China's National Association of Financial Market Institutional Investors (NAFMII) and GMRA repo documentation were made and similarities and differences were discussed. An outline of all the different taxes that

[15] Specifically, the conclusions of the discussions include the following: (a) Basel IV entails segmentation of banking and trading book activities. Standard approach is the new normal, supplanting use of internal models with significant implications for capital requirements. (b) Market studies suggest an aggregate increase in risk-weighted assets of 40 percent-65 percent from Basel IV. (c) Increased FRTB capital costs fall disproportionately on emerging market trading instruments. (d) Capital Requirements Regulation (CRR) II introduces a binding leverage ratio requirement of3 percent which must be met with Tier 1 capital. (e) The leverage ratio is generally overstated for derivative trades because collateral offsets are not recognized. This has negatively impacted client clearing, which runs counter to the G20 objective to promote clearing. (f) The leverage ratio does not recognize high quality liquid assets as eligible variation margin. (g) The NSFR limits fundable collateral to cash collateral that is nettable under the Basel III leverage ratio calculation. End users will be impacted since they typically rely upon the ability to post securities as collateral.

affect the repo market was also presented.

ISDA organized two panels during the conference: one on the importance of bankruptcy reforms and of recognizing netting and settlement finality for capital market development and other legal issues with collateral, and another on margin requirements. The first panel explored in depth the wording of China's Enterprise Bankruptcy Law in the context of what it means for contractual netting rights. The panel also discussed possible self-help contractual remedies and legislative amendments or regulatory fixes that would address the lack of certainty around netting enforceability. Some of the costs and inefficiencies of trading under a non-netting legal framework were also discussed.

The second panel focused on the practical challenges of signing new, regulatory compliant CSAs with Chinese counterparties given that (a) the requirement is driven by international regulation that is not being mirrored in domestic regulation; (b) lack of netting enforceability puts Chinese counterparties at a disadvantage under US and European regulatory requirements; (c) Chinese regulators do not want Chinese counterparties to agree to "unequal" contractual terms; and (d) without agreement on new CSA terms, many international counterparties will not be able to trade with Chinese counterparties after 1 September 2017 when the (delayed) requirements come into force.

Information in capital markets

The quality, comparability and availability of information are key ingredients in bringing together buyers and sellers of both debt and equity, and are thus critical to the deepening of capital markets. The APFF [16] created three self-assessment templates, covering the investment life cycle:

- before investment: disclosure –information about a company or security;
- while invested: bond market data –individual security and aggregate information; and
- exiting investment: investor rights in insolvency –property rights; insolvency process

Deciding upon and developing these templates, the group followed four principles. First, rules made by public policy makers are integral to well-functioning capital markets. Second, dialogue with the private sector can offer insight to the most effective policies. Third, an incremental method is more manageable and effective than a big bang approach. Fourth, given the varying levels of development across Asia Pacific markets, the approach must be applicable to capital markets in any stage of maturity.

In March 2015, the templates were presented to several officials from the Philippines'

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[16] The steering committee managing the APFF Capital Markets Information Sub-Stream is led by representatives of Moody's, supported by representatives from Deloitte, Asian Development Bank, the University of Hawaii, HSBC, Nomura, Standard Chartered, Clifford Chance, Nishimura & Asahi, PwC, Ernst & Young, CFA Institute and CLP Holdings.

Securities and Exchange Commission, who worked on their adoption. Following the successful engagement with the Philippines, APFF reached out to a number of regulators from other economies to both make them aware of and to fill out the templates. As to date no other economy has responded, the steering committee for this work stream will undertake a review and discuss future options on the way forward.

Supporting the Asia Region Funds Passport (ARFP)

The ARFP is a program aimed to provide a multilaterally agreed framework to facilitate the cross-border marketing of managed funds across participating economies in the region. The APFF Sub-Stream on the ARFP was established to support its successful launch. The channels for public-private collaboration created under the APFF has allowed the ARFP sub-stream to facilitate a discussion on the early enlargement of ARFP to include a critical mass of participating jurisdictions, as well as the interoperability of ARFP with other regional mutual recognition frameworks.

For the past years, the APFF convened several discussions with representatives from the international asset management and financial industries, as well as experts from the legal and consulting professions and international organizations, to provide industry feedback to regulators and officials as they worked to advance the ARFP. Among the views that garnered agreement are the following:

- *Enlargement of the ARFP*: The flexibility of the ARFP to enlarge is critical to its impact and success. The participation of as many economies as possible in the ARFP, particularly at the outset, and the opportunity for future enlargement would incentivize active participation by financial service providers in the ARFP, increasing the ARFP's coverage and thereby increasing intra-regional capital market integration, and allowing its benefits to be more widely enjoyed. ARFP's enlargement will increase investors' investment options and reduce cross-border investment costs through economies of scale.

- *Reciprocity*: Member economies should work towards according equivalent priority to promoting ARFP funds so that they are treated on a basis that is comparable to domestic funds. This spirit of reciprocity will allow the ARFP to facilitate greater financial integration.

- *Dispute resolution*: In the European funds passport arrangement – the Undertakings for Collective Investment in Transferable Securities (UCITS) – mechanisms exist for the European Securities and Markets Authority (ESMA) to resolve disputes over issues such as the interpretation of UCITS directives and disputes arising between home and host regulators or regulators and investors. There is a strong case for the creation of a resolution mechanism to help address uncertainties, disputes or issues of misinterpretation that may arise in the course of operation of the ARFP.

- *Standardization of fees and performance figures*: It is suggested that rules on the method of calculation of and disclosure of performance figures and fees in the prospectus of ARFP Funds be established in order to ensure investors are able to conduct a fair comparison of the available ARFP Funds.
- *International Recognition of ARFP funds*: It is suggested that APFF begin engaging with non-member regulators with a view to facilitating the cross-border distribution of ARFP Funds beyond member economies. ARFP Funds should eventually be permitted to be offered in non-member economies in the same way that UCITS funds may be distributed in non-EU jurisdictions.

The APFF established a Tax Task Force that completed an assessment of the key tax metrics in actual and potential ARFP participating jurisdictions. This was done to help regulators understand the detailed tax implications of ARFP, by making this assessment available to regulators in participating jurisdictions. Based on this assessment, the Tax Task Force made the following key observations, which it recommends be taken into consideration in the implementation of the ARFP:

- While there seems to be consensus that the absence of a permanent establishment (PE) created by either the passported fund or the foreign fund manager or both would generally limit adverse tax implications for either the passported fund or foreign fund manager or both, the challenge would be to align the rules and guidelines on what would constitute a PE.
- There are obvious differences in local tax rules. It is not practical to expect the alignment of tax treatment of funds in different economies under the ARFP regime. Instead, a reasonable task could be alignment within each participating economy of the tax treatment of domestic versus passported funds.
- In economies in which there are likely to be mismatches in tax treatment between domestic and passported funds, the task force looks forward to the local authorities revisiting and changing the rules to achieve tax neutrality for resident investors.

Recently, there has been a rise in regional bilateral mutual recognition agreements. Examples include the following:

- In July 2017, the Securities and Futures Commission (SFC) of Hong Kong and the Autorité des Marchés Financiers (AMF) signed a Memorandum of Understanding (MOU) on France-Hong Kong Mutual Recognition of Funds (MRF). Under this scheme eligible Hong Kong public funds and French UCITS funds will be able to be distributed to retail investors in each other's market through a streamlined authorization process. This is the first agreement between Hong Kong and a member of the European Union to establish the regulatory framework for distribution of eligible Hong Kong and French funds.
- In December 2016, the SFC and the Swiss Financial Market Supervisory Authority (FINMA) signed a MOU on the MRF between Switzerland and Hong Kong which provides recognition of asset managers and a framework for the mutual recognition of publicly offered funds in both markets.

It is important that the ARFP is flexible enough to interoperate with other regional investment schemes, such as the Hong Kong-China MRF, the ASEAN Collective Investment Scheme (CIS) Framework and other bilateral frameworks to facilitate the future convergence of the various initiatives and structures. Interoperability with other regional schemes would, as with the introduction of more economies into the ARFP, create greater economies of scale, reduce market fragmentation and improve financial market integration, while ensuring that alternatives continue to be available to retail investors.

The APFF welcomed the signing of the Statement of Cooperation on the establishment and implementation of the ARFP in June 2016 by Australia, Japan, Korea, New Zealand and Thailand. These participating economies have up to 18 months to implement domestic arrangements in accordance with the rules. The passport is expected to commence in early 2018. Over time, the aim is to ensure that all other eligible APEC economies are able to participate in the passport.

APFF collaborators conducted informal discussions with regulators in Hong Kong, Singapore, Malaysia and Chinese Taipei and spoke at industry events to encourage other member economies to join the ARFP. APFF also shared best practices, industry insights and relevant ARFP materials with the Pacific Alliance to potentially launch a similar passport arrangement in the South America region. Finally, APFF stakeholders support on-going efforts under the Financial Markets Infrastructure (FMI) work stream to address standardization of fund services (e.g., registration process, lexicons, platforms, etc.) between passporting economies.

The following are recommended to be given consideration to advance the ARFP. First, more member economies should join the ARFP by signing the Memorandum of Cooperation. APFF welcomes opportunities and invitations to provide private sector resource persons to dialogue with regulators and industry in economies that decide to consider joining the ARFP. Second, participating regulators should continue to engage the private sector on the implementation of the ARFP. Third, given that there are various mutual funds recognition initiatives in the region (Hong Kong-China MRF, ASEAN CIS, ARFP and bilateral initiatives), ARFP should explore interoperability between various initiatives to create synergies and economies of scale. Fourth, member economies that are unable to join the ARFP should be allowed to distribute ARFP funds, just as some non-UCITS member economies accept UCITS funds.

Developing the Asia-Pacific financial market infrastructure

Financial Market Infrastructures[17] or FMIs are the pillars of financial market integrity and market progress. FMIs withstood the strains of extreme volatility brought about by the global financial crisis (GFC). Since then, the importance of ensuring their continued robustness has become a foremost concern of policy makers and regulators, as manifested in the adoption of the CPMI-IOSCO Principles for FMIs. In recent years, FMIs have also increasingly taken on new roles as the global regulatory agenda focused on promoting greater transparency of transactions and greater standardization of financial products, among others. FMIs continue to stand as a bulwark against market disruptions.

Such an expansion of FMI roles is a response to new and rising complexities and costs, which need to be better understood and managed for markets to have higher levels of sustainability and economies of scale. For example, emerging capital markets can struggle with the tension between business case viability and the need for a CCP for nascent derivatives markets to avoid punitive balance sheet costs for banks operating domestically.

On top of the new changes, overseas investors continue to face existing account opening and repatriation processes that need to be streamlined, while there are funds post-trade paper-intensive services that serve as a contrast to the electronic speed of investments. Cybersecurity concerns and responses have emerged to add to this complexity that could lead markets to develop as stand-alone digital fortresses, inhibiting cross-border investment flows. There are no clear and easy answers to any of these, and other, dilemmas.

For a start, economies can consider a number of issues and needs that face FMIs, financial markets, intermediaries and cross-border investors. These include:

- how to promote transparency through a standardized and common platform for trade reporting;

[17] Traditional Financial Market Infrastructures (FMIs) encompass a variety of institutions and systems including payment systems that are systemically important, Central Securities Depositories (CSDs), Securities Settlement Systems (SSSs), Central Counterparties (CCPs) and Trade Repositories (TRs). FMIs are central to the clearing and settlement of transactions in the financial markets, the movement of money and securities, and centrally managing the counterparty risks around the world. Issues in Large Value Payment Systems (LVPS) are not included in this report since it could be discussed separately with the currency policy issues in the region.

- how to improve coordinated monitoring of markets through facilitation of cross-border data flows;
- how to maintain and broaden access to cross-border money transfer mechanisms providing the required transparency in an affordable and meaningful way;
- the standardization of market practices, account structures, operational and processing models; and
- consistent tax treatment of domestic and cross-border transactions.

Regulatory clarity and private-public sector collaboration will be key to realizing new value from untangling some of these complexities.

As reported by the Asian Development Bank's Asian Economic Integration Report 2016, "…[it] is essential to follow an FMI development strategy that is both tailored to the AEC [ASEAN Economic Community] and draws from global best practices. There is no one-size-fits-all approach for regional FMI development. While Europe primarily chose a top-down approach to financial market integration, this is not necessarily right for the AEC. Thus, existing multilateral initiatives should be intensified to provide a policy environment that is both enabling and prudent for the public and private sector to foster a balanced regional FMI development path". While this was written with reference to ASEAN, it remains equally applicable to the rest of the Asia Pacific region.

The potential benefits and goals of such collaborative efforts would be to improve market liquidity (a key issue for the growth of the region's bond markets), to streamline unnecessary costs and fragmentation of markets, to enable economies of scale, to be inclusive of economies and participants' involvement, to facilitate financing and investments, and to reduce the cost of funding from international capital markets.

In 2015, the APEC Finance Ministers called for a roadmap to improve the region's FMIs and create a regional securities investment ecosystem to facilitate cross-border investment in capital markets to deepen markets and increase economies of scale. This task was incorporated in the CAP, the Finance Ministers' multi-year blueprint for financial sector development in APEC. On 25 April 2017, an APFF symposium involving international private and public sector representatives was convened in Seoul, Korea.[18] The following are key highlights and messages from the Symposium's panels.

The roles of FMIs in the region

The panel observed that the roles of FMIs have been under the spotlight after the GFC. The GFC had prompted the G20 authorities to introduce a new suite of

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[18] This was the Asia-Pacific Financial Forum Symposium ***Developing APEC's Financial Market Infrastructure***, organized by the APEC Business Advisory Council (ABAC), hosted by the Federation of Korean Industries (FKI), and co-sponsored by PayPal and Nomura Research Institute (NRI).

regulations, which has influenced and reshaped global markets. Among its recommendations were those related to the use of CCPs in the management of counterparty and liquidity risks to markets. However, domestic CCPs may not be appropriate for all APEC markets. While post-GFC regulations and rules are driving financial transactions to be further collateralized, market participants report a scarcity of high quality liquid asset (HQLA)[19] collateral. Local currency collateral, including highly rated government bonds, is often not accepted internationally.

As a result, there is generally a high level of call for standardization in many areas and the panel viewed that standardization should not only be considered in technical terms, where it is perhaps more obvious (such as the utilization of ISO20022 for messaging), but also in terms of industry expectations: as an example, harmonizing issuance documents might both help issuers streamline multinational issues and increase investors' appetite to diversify through cross-border investments. At the same time, participants also recognized the widely varying levels of development among capital markets in the APEC economies, which means that a one-size approach cannot fit all.

The panel viewed that, on one hand, FMIs should be encouraged to cooperate in a similar manner to how central banks link to each other. This cooperation should not only be in large value payments and securities settlement systems, but also in electronic payments (e-payments) that need to be interlinked internationally. On the other hand, while regional initiatives include access programs and activities to achieve inter-operability of markets, new systemic risks could arise from markets becoming more interconnected.

The panel recommended that responsible authorities be encouraged:
(a) to support the harmonization of issuance documents and efforts to enhance the transparency of securities and tax rules (including efficient disclosure framework of ultimate beneficial owner) to the regulators and authorities through the custody chain;
(b) to monitor in coordination with the region's market participants the extraterritorial effects of developed economies' rules and consider ways to address potential conflicts of laws and economic viability, especially in smaller economies, such as through adoption of international best practices ;
(c) to collaborate together with international organizations to convene workshops for the purpose of better understanding the issues, particularly in view of global tapering now becoming a more distinct possibility, addressing considerations for regional HQLA collateral; and
(d) to promote inter-operability among FMIs and participants, including financial intermediaries, to more efficiently mitigate risk and reduce de-risking or hindering financial inclusion as a result of elevated compliance costs, and to evaluate the effects of interconnectedness between markets and their potential impact.

[19] HQLAs are assets with a high potential to be converted easily and quickly into cash.

An APEC Roadmap for the Development of Financial Market Infrastructure in the Asia-Pacific Region

Through a series of discussions before, during and after the APFF symposium, Participants agreed on the text of a proposed *APEC Roadmap for the Development of Financial Market Infrastructure in the Asia-Pacific Region*. This roadmap, which is attached to this report as Appendix 1, consists of sections dealing with securities markets' post-trade ecosystem; non-resident accounts, tax, investor identification and transparency; increasing market efficiency in relation to repo and lending as well as to derivatives; and fund services.

<u>Securities Markets: Post-Trade Ecosystem</u>

Driven by over a decade of new regulatory requirements at global and individual jurisdiction level as well as their implementation, in addition to legacy requirements, today's levels of post-trade operational running costs and complexities have significantly increased. Even as there are consistent analysis on the potentials of greater regional market interconnectivity[20], a cross-border market participant will face a significant level of costs that can act as a deterrent to higher levels of cross-border activities.

The panel recommended the following:
(a) The public and private sectors should collaborate to assess and promote the regional standardization of account opening documents like KYC/AML and tax reporting that needs to be completed by securities investors, be they domestic or cross-border. Standardization can only have meaningful impact if industry-wide implementation is at the regional level.
(b) Regulators should support (e.g., through clear guidelines) the use of third party industry utilities to store, manage and facilitate access of relevant parties to such standardized documents ("documentary industry utilities"). Public and private sectors should collaborate to explore the feasibility of such documentary information reuse/portability at the regional level and discuss how these goals can be better achieved and in what time frame.

<u>Non-Resident Accounts, Tax, Investor Identification and Transparency</u>

In capital markets, account structure refers to omnibus or direct holding under the beneficial owner name, and its requirements are often determined by macroprudential considerations related to management, cross-border tax, transparency, reporting and operational requirements. This panel discussed account structure in the context of cross-border investments and covered various stages of intermediation.

The panel recommended that responsible authorities be encouraged to consider the

[20] "An analysis of Asia's cross-border asset and liability holdings finds that Asia's financial links with the rest of the world remain stronger than those within the region", Asian Development Bank, *Asian Economic Integration Report 2016*.

following:
(a) Local markets should feel free to choose the account structure they consider appropriate, whether it be direct holding, omnibus or a mix of both. The omnibus account structure is the preferred option for attracting cross-border investment flows to the market. Both account structures can coexist. Ideally the omnibus account structure should be combined with the nominee concept legal structure.
(b) Cross-border investments are facilitated where there is either no tax or a simple tax scheme (i.e.: a withholding tax based on a Record Date principle); there is no capital gains tax based on a price difference or a tax calculated on a holding period (which is unmanageable on a cross-border basis); tax is imposed at source rather than refunded (refunds are best limited to corrections post payment), involves a one-time certificate instead of requiring yearly certificates or a certificate per payment, and local notarization of tax certificates or supporting documents are not required.
(c) It is important to find the right balance between transparency and market efficiency. Responsible authorities should review whether legal frameworks support requests to report investors' information and undertake legislative reforms if they do not. Securities regulators should introduce requirements for bond prospectuses to facilitate investors' information reporting requests.

Increasing Market Efficiency: Issues specific to Repo/Lending

Liquid and well-functioning repo and securities lending markets are essential to the efficient allocation and movement of capital and collateral through the financial system. They also play a role in facilitating the diversification of risk among different types of market participants across economies. The relatively diverse range of Asia-Pacific markets' growth stages gives rise to additional regional issues and challenges in developing consistent practices.

The panel recommended that both responsible authorities and market participants be encouraged:
(a) to continue to pursue various initiatives, including promulgation and promotion of international best practices and formulation of codes of conduct; and to further develop and improve the market, by ensuring very clear principles on regulatory expectations on capital raising and investment;
(b) to review the local practices if they adopt the international standard documentation such as the GMRA and the Global Master Securities Lending Agreement (GMSLA) and undertake promotionally initiatives if they do not, including reflecting some locality to be reflected in the standard contract document; e.g. in the form of annex, through the collaborative work with market practitioners and wide variety of stakeholders including industry associations; and
(c) to support constant dialogues with the industry representatives through public-private platforms including APFF, the Pan Asia Securities Lending Association (PASLA), International Capital Market Association (ICMA), ASIFMA, and ABMF to review current policies and practices could effect as a barrier and undertake reforms if they do.

Increasing Market Efficiency: Issues specific to Derivatives

Greater regulatory transparency in the OTC derivatives markets is a key public policy goal that was codified at the September 2009 Pittsburgh G20 summit. In order to help improve regulatory transparency, a number of critical milestones need to be met. The active support and cooperation of a range of stakeholders – regulators, market participants and market infrastructure providers will be required.

The panel recommended that capital market regulators be encouraged to:
(a) review whether their reporting requirements are harmonized, data requirements from market participants can be streamlined and consistent within and across jurisdictions, and undertake regulatory reforms if they are not;
(b) adopt standards for derivatives reporting, and those that have not yet deployed their rules should avoid introducing unique requirements;
(c) review whether current regulations hinder sharing derivatives trading information across borders, and undertake reforms if they do;
(d) defer to each other's regulatory regimes where their intended outcomes are consistent by adopting equivalence decisions;
(e) review the level of inter-operability between trade repositories and promote and incentivize the sharing of data; and
(f) leverage cooperation with other authorities to achieve their objectives: both for sharing lessons learnt, as well as sharing data by designating jurisdictional, regional and global leaders to spearhead the aggregation effort.

The panel also recommended the removal of barriers to sharing of data and information between regulators.

Fund Services

In an era where more investors are investing for retirement income and can benefit from the diversity of funds offered by funds passport initiatives like the ARFP, managing industry costs is important to facilitate these investors' activities. Automation is also required to bridge the "mismatch" between slower post-investment paper and inefficient spaghetti processes and the higher speed of electronic investments.

A regulator-supported funds back-office processing utility will be needed to progress this key industry that can support individuals' wealth management, pension accumulation and drawdown – in the later cases, reduction of unnecessary costs to preserve returns will be important.

Amid the call to better understand different fund services in the region and develop recommendations for standardized practices, a consultative body of CSDs was established under the name of Asia Fund Standardization Forum (AFSF) in 2015. However, it will be important to note that standardization activities will only have meaningful impact if industry-wide implementation is encouraged on the regional scale, as failure to do so will result in a development of multiple standards that are not harmonized.

The panel recommended that capital market regulators be encouraged to:
(a) establish standardized registration process for funds between passporting economies to ensure that benefits of streamlined regulations are felt by the market;
(b) lead the standardization in the terminology used between fund markets for market players to communicate and report effectively for cross-border transactions; and
(c) support the development of industry fund platform utilities

Data management and technology

In addition to the discussion focusing on FMIs, in order to promote the common understanding of the current status and priority issues to be addressed in the public-private platform in region, symposium participants discussed emerging issues in data management and technology in financial markets.

Fintech

Advanced technology in finance (fintech) is rapidly changing the shape of how financial services are delivered to clients as well as managed by institutions and monitored as a whole financial market. The discussions covered three key focus areas: KYC, e-payments, and cybersecurity.

Disruptive technologies / new FMI-like entities

Disruptive technologies such as distributed ledger technologies, robo-advisers or artificial intelligence bring promises of better data management, faster access to data and cost reduction for the usage of that information, benefiting a growing financial product customer base through digitization.

However, these new technologies also bring risks such as technological and operational risks arising from immature systems; fragmentation risks due to a lack of technical and data standardization for mainstream and cross-border usage; cybersecurity and data confidentiality risks; and legal risks, considering the existing regulatory uncertainty around their use, especially for cross-border activities, and the legal protections that are available (particularly in a consumer context).

As such, the panel urged FMIs and the private sector to continue experimenting and contributing to industry's awareness and knowledge to overcome the maturity challenge. Collaborative work with regulators will bridge the gaps with the needs for new regulatory frameworks.

The panel recommended the following:
(a) FMIs should experiment and contribute to the research and development exercise required to overcome the maturity challenge. They should work collaboratively with regulators, the financial industry and the broader public sector. Such collaborative experimentation is important not only to contribute to maturing

these technologies further but also to better understand them, ensure focus on the right problems to be solved and identify as well as understand the risks. It also helps getting the necessary buy-in for when an implementation decision needs to be taken. (b) Regulators and FMIs also need to collaborate across markets to agree on harmonized domestic legal frameworks supporting the implementation of such new technologies and ensure cross-border regulatory certainty.

Most recommendations presented in this report are suggested to be implemented starting within the next two to three years to further foster forward looking, robust and streamlined capital markets.

EXPANDING THE REGION'S LONG-TERM INVESTOR BASE

Retirement income and long-term investment

Insurers and pension funds play a critical role in the development of capital markets and financing of infrastructure projects. The long-term liabilities of insurers and pension funds are an ideal match for long-term assets such as infrastructure that can provide adequate returns to meet future emergency and retirement needs.

Mobilization of such large pools of long-term capital by insurers and pension funds to finance long-term infrastructure investment in Asia would represent a "triple win" for consumers, the financial sector and APEC member economies:

- Consumers receive high and stable returns for long-term savings.
- The financial sector is able to access deeper capital markets for infrastructure investment.
- Governments obtain relief from large contingent fiscal liabilities.

This "triple win" could be achieved by addressing three gaps that profoundly limit the development of both insurance and pension coverage and capital market development in APEC economies:

- **Pension/Protection Gap**: The 2015 and 2016 APFF Progress Reports listed high-level recommendations and measures that promote the development of retirement income system and ensure adequate retirement savings as well as adequate lifetime retirement incomes, and described three key means to address this gap: (a) mandatory provision for retirement savings at a sufficient replacement rate to fund retirement; (b) tax relief to promote long-term savings products; and (c) product and distribution innovation and financial awareness. Altogether the system promotes public financial awareness, ensuring a diverse range of retirement income products and improved financial security for the region's rapidly growing number of retirees.

- **Infrastructure/Investment Gap**: Inadequate infrastructure investment has been a long-standing issue in emerging Asia (outside of China). At the same time, Asia's huge savings are still being mostly channeled into short-term bank deposits and government securities in mature markets. The 2016 APFF Report noted the following possible solutions to address the dearth of investable assets in Asia, particularly in infrastructure: (a) promotion of infrastructure as a defined asset class; (b) increased fiscal spending by Asian sovereigns within macroeconomic parameters suitable for developing economies; and (c) adoption of various financing vehicles, with a broader public-private partnership framework to promote long-term infrastructure investment.

- **Regulatory/Accounting Gap**: The 2016 APFF Progress Report recommended that APEC economies should adopt accounting, solvency, investment, and securities standards supportive of the development of retirement savings and infrastructure investment. To encourage insurers and pension funds to engage in long-term investments and retirement solutions, barriers arising from regulations and accounting should be removed, and policies that are suitable for long-term business should be promoted. Global solvency and accounting standards should be designed in a way to incentivize companies to improve risk management and adopt best practice. The main regulatory issues identified by the APFF, in particular, for insurance companies and corporate pension funds, are: (a) bank -centric regulations; (b) short-term oriented economic regimes; and (c) one-size-fits-all model. Remaining key accounting issues identified by the APFF are: (a) level of aggregation; (b) scope of variable fee approach; and (c) transition.

- It was recommended that APEC Finance Ministers encourage the participation of all relevant public sector stakeholders in dialogues with the private sector to address barriers to long-term investment. APFF intends to promote active participation of the private sector in relevant conferences and to convene workshops in the region involving a wide range of stakeholders.

The 2017 work plan and its progress in each of the three areas are described below.

Pension/Protection

The APFF intends to coordinate with global initiatives (i.e. OECD, [21] World Economic Forum or WEF[22]) and the pension industry (i.e., Asia Pacific Investors Cooperation or APIC) and to hold dialogues with both pension and insurance regulators.

- ***APFF/APIC Regional Pension Funds and Social Security Systems Summit, 5-6 December 2017, Hong Kong, China***. The APIC Summit is a private and confidential, 360-degree in-depth coverage of the Asian pension funds and social security systems, with participation and support of key stakeholders: policy makers, regulators and asset owners (pension funds, social security systems, insurance), plan participants and investment management companies' leaders. This year, as

[21] OECD is currently planning to collaborate with the APFF to convene a conference on pensions, insurance and long-term investment in infrastructure in Asia.

[22] See the pension white paper from the World Economic Forum (http://www3.weforum.org/docs/WEF_White_Paper_We_Will_Live_to_100.pdf).

pension and retirement systems are pressured to focus on returns and sustainability, the APIC network of pension funds will also focus on infrastructure investments. Delegates include APIC network members (central banks, treasuries, ministries of finance, pension funds, social security systems, trusts and insurance companies) and their international counterparts. The APIC Summit provides an exclusive venue where strategies, successful implementation of innovative asset allocation, and concerns affecting the retirement industry are discussed in confidence. Summit highlights include asset owners and stakeholders presenting case studies of successful collaborative investments into infrastructure and other alternative assets. Regulators and asset owners present the latest initiatives in providing maximum fund choices to plan participants. High-level discussions and presentations by select Asian emerging economies' policy and capital markets delegation. The APIC Regional Pension Funds Infrastructure Investment Survey is also presented. APFF as Summit Co-Host shall invite APEC Finance Ministers and relevant senior leaders to speak and participate at the Summit, and intends to deliver key messages to the summit participants.

The APFF continues to study selected APEC economies and examine gaps and potential solutions on retirement income and longevity solutions. The following are some examples of the recent developments in the region:

- ***Thai Government introducing a new mandatory provident fund scheme***: The Thai government is planning to introduce a new mandatory provident fund scheme to address the issue of low coverage of the existing voluntary scheme. In 2016, only 2.8 million private company employees were taking part in the scheme out of a workforce of 38 million. The draft new scheme will require companies with 100 employees or more and without a comparable scheme to participate at the inception (estimated to be in 2018), and companies with fewer employees to comply at a later date. For the first three years, the new mandatory scheme will require employers and employees to each contribute 3 percent of the salary, with the contributions capped at 60,000 baht per month. Thereafter, the contribution rates for both employers and employees will gradually increase by 1 percent per year to a maximum of 10 percent over seven years.

- ***Malaysia's Employees Provident Fund (EPF) receives innovation award for its retirement advisory service***: Malaysia's EPF was awarded the 2016 World Pension Summit Innovation Awards in the Communications category for its Retirement Advisory Service (RAS). First introduced on July 1 2014, RAS serves as a platform for EPF members to obtain free personalized advice on their EPF savings and retirement planning from EPF's trained officers. The initiative has quickly expanded over the past years and is now serving customers through 43 advisers at 18 RAS branches nationwide. In addition to advice and investment counselling, RAS also conducts awareness and educational programs on basic financial and retirement planning. RAS is EPF's effort to enhance its service delivery, thereby transforming its traditional transactional services model into an advisory-based relationship with its customers.

- ***Australian government's consultation on the Discussion Paper:*** The Australian Government recently conducted a consultation on the discussion paper to develop a framework for the retirement phase of superannuation (see its one-page fact sheet[23]). The Australian government realized that retirees are faced with complex financial decisions and are often unsure what to do with their retirement savings. In addition, they have very limited post-retirement solutions that manage longevity risk. As a result, many retirees are drawing down their pension savings very conservatively, for fear of outliving their savings. To address this, the government is exploring a framework that meets 3 requirements: income, risk management and flexibility. The product would have a higher income (15-30 percent higher than Account Based Pensions), and it would be flexible, without increasing the risk of outliving retirement savings.

- ***Life Annuity Scheme in Hong Kong:*** With Hong Kong having the highest life expectancy in the world (87 years for females and 81 years for males, according to the Japanese Government's figures in 2016), it is important for retirees to have adequate savings saved up during the accumulation phase. But it is equally important to focus on the decumulation phase, with the ultimate objective of providing a steady income stream during retirement. Commissioned by the Hong Kong government, the Hong Kong Mortgage Corporation Limited (HKMC) announced the launch of a public annuity scheme in April 2017. It is a first step in helping retirees turn lump sum cash into lifelong streams of income. The scheme will provide guaranteed fixed monthly annuity payment to annuitants (aged 65 or above who are Hong Kong permanent residents) until his/her death. A lump-sum premium payment to the HKMC has a tentative cap and floor of HK$1 million and HK$50,000 respectively. An independent consultant has verified and validated the internal rate of return can be set at 4 percent, translating into monthly fixed payouts of HK$5,800 for male and HK$5,300 for female per HK$1 million premium paid. The scheme also comes with a death benefit provision – which guarantees each annuitant to receive monthly annuity payments with total amount equal to 105 percent of the premium paid and in the event an annuitant dies before receiving 105 percent of the premium paid, his/her beneficiary(ies) will receive the remaining unpaid monthly instalments or a lump-sum amount. The scheme is expected to be launched in mid-2018, subject to the support of the Hong Kong Monetary Authority and the authorization by the regulatory authority for the insurance sector.

Infrastructure/Investment

The APFF is coordinating with global (i.e. Global Infrastructure Hub, OECD, WEF) and ASEAN initiatives (i.e. ASEAN Insurance Council) and the securities industry (i.e.

[23] https://consult.treasury.gov.au/retirement-income-policy-division/comprehensive-income-products-for-retirement/supporting_documents/CIPR%20Factsheet.pdf.

ASIFMA), and undertakes dialogues with selected APEC economies (i.e. Indonesia, Vietnam, Philippines, Thailand).

- ***APFF/APIP Dialogue with Indonesian Government on PPPs in Waste Management on 14 March in Jakarta***: The APFF collaborated with APIP, the Government of Japan and the Government of Indonesia in capacity building to help promote a pipeline of bankable PPP projects in waste management in Indonesia.

- ***APEC Finance Ministers Process Seminar on Long-Term Investment in PPP on 17 May in Ninh Binh***: The APFF provided inputs to the work of FMP on risk allocation in PPPs, development of a pipeline of bankable infrastructure waste-to-energy projects, and promoting long-term investment in infrastructure from pension funds, insurance companies and Islamic financial institutions.

- ***APFF Roundtable on Long-Term Investment in Infrastructure on 25 July in Toronto***:[24] Confronted with aging populations, lengthening life spans and a low-interest rate environment, institutional investors are seeking greater portfolio diversification and more profitable investments in long-term assets that match their long-term liabilities. This Roundtable was held to help address issues, including the lack of capacity in many developing economies' public sector to bring bankable projects to the market, the dearth of deep and liquid local currency bond markets that are the usual channels for long-term investment in infrastructure, and the lack of capacity of most pension funds and insurers to directly manage infrastructure assets, especially in developing economiesIt brought together key stakeholders from the public sector, the investor community, infrastructure experts, and multilateral and specialized institutions to identify forms of collaboration that can directly facilitate investment in infrastructure.

The APFF continues to study selected APEC economies and examine possible improvements to attract long-term investors, including financing vehicles, green finance, and survey on infrastructure investments[25].

- ***Rethinking risk allocation in PPPs:*** Over the past decade, the flow of funds to infrastructure has increased dramatically and is now projected to continue to increase for years to come. Prequin reports that AUM grew from $25 billion in 2005 to $332 billion in 2015. Allocations to infrastructure are also increasing, from current allocations of 3.5 percent in 2011 to 4.3 percent in 2015. However, target allocations are still not being met, with a 2015 target allocation average of 5.7 percent and only 4.3 percent currently allocated. The bottlenecks in Asia preventing capital from flowing to meet demand include insufficient awareness

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[24] This is the APFF Roundtable on ***Expanding Trans-Pacific Opportunities for Long-Term Investment in Infrastructure***, co-organized by ABAC with the Asia-Pacific Foundation of Canada in collaboration with the GIH, OECD and World Bank's Global Infrastructure Facility and sponsored by the Governments of Canada and Ontario.

[25] APIC is conducting a survey on infrastructure investments in ASEAN region and intends to present the result at APFF/APIC Summit on 5-6 December in Hong Kong.

of investors, inadequate legal and regulatory frameworks, poorly structured and prepared projects, inequitable risk allocations, lack of capacity by governments to manage projects, and imbalance between risk and return. At the 2016 Executive Dialogue with APEC Finance Ministers in Lima, there was an acknowledgement by Ministers that governments need to rethink how risk is allocated between the public and private sectors in PPPs. Key to growing and incentivizing long-term investment in infrastructure is a deeper understanding by policymakers of the risk appetite of different investors. PwC has undertaken a qualitative survey to provide an investor perspective, and preliminary findings were presented at the APEC Seminar on Long Term Investment held in Ninh Binh on 17 May. The seminar underlined the need for further dialogue between stakeholders on how to address regulatory, foreign exchange, construction and other types of risks so that they do not deter investment.

- ***The IFC/WBG's PPPs in infrastructure***: IFC/WBG has partnered with insurers Prudential and Allianz to create a new fund that allows institutional investors to increase their exposure to emerging market infrastructure with managed risk. Institutional investors establish and fund special purpose vehicles for co-investment with IFC in emerging market infrastructure. When IFC/WBG provides debt financing for infrastructure projects, it offers a portion of each new loan to the special purpose vehicles on the same terms and conditions as IFC/WBG's lending. This approach helps to overcome one of the major barriers to institutional investors allocating more of their assets to infrastructure, which is their preference and/ or regulatory requirement for investment-grade risk/return profiles. The joint fund addresses this by providing a first-loss tranche of up to 10 percent of each partner's portfolio, supported by guarantees from the Swedish International Development Cooperation Agency (SIDA). The partnership enables each US$1 invested by IFC/WBG and SIDA to mobilize an additional US$8-10 from a third party. East Spring Investments, the Asian asset management business of Prudential plc, has raised $500 million for the fund.

<u>Regulation/Accounting</u>

The APFF participates in global and regional conferences and meetings to discuss relevant regulatory and accounting issues. The following are some examples of external conferences, for which the APFF provided or plan to provide inputs:

- 17th OECD/ADBI Roundtable on Capital Market and Financial Reform, Tokyo, 2-3 March
- 3rd Indonesia Infrastructure Finance Conference, Jakarta, 17-18 May
- OECD/NAIC/OIC Joint Roundtable on Insurance and Retirement Savings in Asia, Bangkok, 20-21 September
- 5th Insurance China International Summit, Shanghai, 22-23 September
- OLIS 50th Anniversary Life Insurance Symposium, Tokyo, 25-26 October
- 24th IAIS Annual Conference, Kuala Lumpur, 2-3 November
- 36th FIDES Conference, El Salvador, 12-15 November
- 27th CNSF International Conference, Mexico City, 16 November

- 28th Pacific Insurance Conference, Hong Kong, 19-22 November
- 20th ASEAN Insurance Regulators' Meeting and 43rd ASEAN Insurance Council Meeting, Vientiane, 21-24 November
- 4th NAIC Asia Pacific International Forum, Honolulu, 29 November – 1 December

In its 2014 Interim Report, the APFF identified regulatory and accounting issues and high-level recommendations to implement approaches in promoting long-term investment and longevity solutions by insurers and pension funds. The APFF also supported ABAC in drafting a comment letter to the International Association of Insurance Supervisors (IAIS) on the risk-based global insurance capital standards (ICS) on 20 January 2015, a comment letter to the IASB/FASB on insurance contracts on 10 October 2013 and a comment letter to the IASB on the Conceptual Framework for Financial Reporting. As the 2015 and 2016 APFF Progress Report also highlighted, the APFF has engaged in continuous outreach and dialogue with policymakers, regulatory authorities and accounting standard setters, international (i.e. IAIS, IASB, OECD, World Bank) and regional institutions (i.e. ADB, ASEAN, NAIC, ASSAL), based on the list of identified issues and recommendations:

- ***IAIS work on risk-based global ICS:*** On July 21, the IAIS released the risk-based global insurance capital standard (ICS) Version 1.0 for extended field testing. This represents a significant step towards the development of ICS Version 2.0 in late-2019. ICS Version 2.0 is expected to achieve a greater global convergence as the IAIS continues progressing towards the ultimate goal of a single global standard delivering substantially the same outcome across jurisdictions.

- ***Dialogue with IAIS:*** The APFF held bilateral meetings with the IAIS Secretariat and key IAIS members and participated in various IAIS conferences and meetings to be engaged in active discussions on key issues for the Asia-Pacific region. The APFF's key messages included the following: (a) ICS should take into account the specific nature of the insurance business, avoid bank-centric capital weighted rules, and consider the characteristics of long-term assets supporting long-term liabilities as well as the effect of asset diversification. (b) An economic based regime should have a long-term vision. Short-term oriented mark-to-market valuation may produce significant volatility for long-term business, which may not be conducive to the insurers' capacity to meet long-term obligations. Insurers should be allowed to invest in assets with long-term growth opportunities, such as infrastructure investments. (c) International standards should be principles-based and aim to achieve comparable outcomes by taking into account the region's diversity. Regulators are now generally aware of the issues identified by the APFF, and are considering various measures to mitigate their negative impact on long-term business and investments. A number of IAIS members in the region noted the relevance of APFF's recommendations to promote long-term investments and business, and requested the APFF to provide more inputs.

- ***IASB issued IFRS17:*** On 18 May, IASB published a new standard, IFRS 17 (Insurance Contracts), which would require insurance liabilities to be measured at a current fulfillment value and provide consistent and principle-based accounting requirements for insurance contracts. IFRS 17 supersedes IFRS 4 (Insurance Contracts) and is effective for periods beginning on or after 1 January 2021, with earlier adoption permitted if both IFRS 15 (Revenue from Contracts with Customers' and IFRS 9 'Financial Instruments) have also been applied.

- ***Dialogue with IASB:*** The APFF held bilateral meetings with some IASB Board Members and engaged in constructive discussions on key issues, which may ultimately facilitate the implementation of IFRS in the region. As a result, we observed some improvements in the final IFRS17 from the 2013 Exposure Draft, including the permission of optional OCI, a measurement model for participating contracts under some conditions where changes in the estimate of the future fees that an entity expects to earn from participating contract policyholders are adjusted against the CSM (so-called "variable fee approach"), and alternative approach for CSM at transition. These changes would address some of the issues identified by the APFF. Remaining key issues include level of aggregation and scope for variable fee approach. While the IASB made some improvements on these areas, there are some technical and practical aspects yet to be addressed. The APFF intends to be involved in the interpretation and implementation processes, in cooperation with European and North American representatives, who share similar concerns, and assist the IASB in reflecting economic reality and long-term nature of the business, and avoiding the creation of disincentives for insurers in undertaking long-term investments and business.

- ***Dialogue with regulatory authorities in the region:*** The APFF has engaged in dialogues to exchange views on regulatory and accounting issues with the insurance regulatory authorities in the region, including Brunei, China, Chinese Taipei, Hong Kong, Indonesia, Japan, Malaysia, Singapore, Thailand, and the United States.Most recently, the APFF convened a dialogue with the Indonesian insurance regulator (OJK) on 19 May in Jakarta to discuss retirement, long-term investment in infrastructure, regulatory and accounting issues.[26]

- ***Coordination with ASEAN:*** The APFF and the ASEAN Insurance Council have coordinated to make consistent recommendations and communicate with the ASEAN Insurance Regulators. The APFF also had a dialogue with the ASEAN Secretariat on 19 May to discuss key issues and emphasize the collaboration between APFF and ASEAN to promote sustainable, resilient and inclusive long-term growth of the APEC and ASEAN economies.

- ***Coordination with other stakeholders:*** The APFF has coordinated with the Geneva Association, Institute for International Finance (IIF) and Hub Group so that their global positions properly reflect Asia-Pacific perspectives.

The APFF continues to study selected APEC economies and examine regulatory and

[26] The APFF is planning to have a similar dialogue with Thai insurance regulator (OIC) in September in Bangkok.

accounting issues and consider possible implementation support:

- ***APFF Roundtable on Insurance Regulations and Accounting on 31 October in Hong Kong***: To better understand key issues and support implementation on recent development, including IFRS17, the newly published standards on insurance contracts, the ICS, and new solvency regimes in the region, the APFF is holding a roundtable hosted by Deloitte China in collaboration with the Hong Kong University of Science and Technology to allow the IASB and key stakeholders in public and private sectors to exchange viewpoints and discuss key issues on insurance regulations and accounting in the region. Unlike Solvency II in Europe, a number of local regulators in the Asia Pacific region are considering IFRS 17 as the basis for the solvency balance sheet, in which case the impact of IFRS17 would go beyond financial reporting, and may produce unintended consequences. The APFF intends to assist in analyzing such indirect impact, identifying issues (i.e. choice of discount rate, treatment of CSM/risk adjustments), and considering possible solutions in selected APEC economies.

Communication Strategy

The APFF intends to enhance communication with stakeholders by focusing on key messages and explore various effective communication tools (i.e. video interviews, short movies, cultural performances) to promote sustainable, resilient and inclusive development with diversity in APEC economies.

Enabling Islamic financial institutions to expand cross-border investment in infrastructure

Islamic finance has significant potential to meet long-term funding needs for infrastructure projects, which are suitable for its asset-based and risk-sharing nature.[27] At the 2015 APEC Finance Ministers' Meeting hosted by the Philippines in Cebu, ministers and the private sector discussed the development of an Islamic Infrastructure Investment Platform (I3P), in order to facilitate the mobilization of capital in Islamic institutions to fund infrastructure across the region.

In October 2015, the government of Brunei Darussalam hosted a workshop in collaboration with the APEC Business Advisory Council (ABAC) Brunei, the Asia-Pacific Infrastructure Partnership (APIP) and the Asia-Pacific Financial Forum (APFF). In May 2016, the government of Malaysia, in collaboration with ABAC Malaysia, hosted an APFF workshop to develop concrete proposals on the structure and mission of the I3P. In February 2017, ABAC Thailand and the Thai Ministry of Finance led discussions in Bangkok on the way forward to advance this initiative. Participants in these

[27] The World Bank's latest global report on Islamic finance estimated total Islamic banking assets at US$1.9 trillion, outstanding sukuk issuance of US$310.9 billion and Islamic assets under management at US$60.6 billion in 2014. Growth rates have been high and the future is promising as financial access increases among the mostly young 1.5 billion Muslim customers in coming years. World Bank Group, *Islamic Finance: A Catalyst for Shared Prosperity*, 2016.

discussions agreed on the following proposed features of I3P:

- I3P would provide a platform for collaboration among public, private, international and academic experts to address the key obstacles to the expansion of cross-border investment by Islamic financial institutions, especially long-term investment, in infrastructure projects in APEC economies.

- I3P would be developed under APFF with the support of Brunei, Malaysia, Thailand and other interested APEC member economies, and will be open to participation by other APEC members as it develops. It is hoped that I3P's success in addressing key issues would lead to more cross-border investment in infrastructure among participating economies, as well as more investment from leading Islamic financial centers to the region.

- Stakeholders will include experts drawn from Asian Development Bank, World Bank Group, Islamic Development Bank, the Sustainable Infrastructure Foundation, the APFF's Retirement Income and Insurance Work Stream, the APIP, institutional investors, financial institutions, industry associations, legal and consulting firms, government agencies, academic organizations, regulatory bodies and other relevant institutions.

- I3P will have a small secretariat based in a location agreed upon by the pathfinder economies. The funding for the secretariat may be provided by the public or private sector or both, or may be shouldered by an existing organization. During the initial stage, a small APFF task force led by the Brunei private sector would play a provisional secretariat role, while undertaking activities and discussions leading to the establishment of the secretariat. The role of the secretariat would be mostly coordination, maintenance of a directory of experts participating in the initiative, and collection and management of information related to definitions, projects and others needed to meet the goals of the initiative.

- Actual work would be undertaken by stakeholders on a volunteer basis, organized around a number of work streams led by volunteer Sherpas agreed upon by the pathfinder economies. Activities would be undertaken on a self-funded basis. Participating organizations will be encouraged to host activities. Participants will be responsible for financing their own travel and accommodation through their own institutions or sponsors. Funding may be solicited from appropriate sources for projects that require significant dedication of time and effort, such as research projects or surveys.

Participants have identified priority issues that need to be addressed by dedicated work streams, which are as follows:

- development of ***common definitions*** of Sharia-compliant infrastructure projects and financial instruments acceptable in all pathfinder economies;
- development of Islamic ***hedging instruments***;
- development of ***financial instruments suitable for infrastructure investment*** from Islamic pension funds and takaful;

- identification of discriminatory ***tax policies*** in pathfinder economies and actions to address them; and
- development of ***project preparation tools*** for participating economies and possible pilot projects.

An APFF conference will be convened in 2017 to discuss how these priority issues could be addressed in concrete terms, and develop a proposed initial work program for the I3P.

Fostering Financially Resilient Communities

The Asia-Pacific is the world's most natural disaster-prone region on the planet. For decades, it has recorded the biggest number of natural disaster events. Their economic consequence has been enormous, which is attributable to growing concentration of population and economic activities in hazard-prone areas. In addition to their vulnerability to natural disasters, many people belonging to the low-income segments of society, including owners of micro- and small enterprises, do not have access to insurance services.

To address these issues, APEC Finance Ministers included in the CAP deliverables to establish and promote private disaster insurance schemes and to develop a roadmap and network of experts through the support of APFF for expanding the coverage of microinsurance in member economies. This report highlights the work being undertaken in APFF with respect to disaster risk financing and insurance (DRFI) and microinsurance. In particular, APFF this year completed the draft of a proposed roadmap for expanding the coverage of microinsurance in the region, which is attached to this report as Appendix 2.

A roadmap for expanding the coverage of microinsurance in APEC

Effective risk management through microinsurance is critical for low income individuals and micro and small enterprises, especially in developing economies. However, only around 5.2 percent of people in emerging markets worldwide are currently covered by micro-insurance. Related to this, Asia-Pacific policy makers need to develop financial instruments to mitigate the impact of natural catastrophes in the world's most disaster-prone region. To help implement the CAP's deliverable on microinsurance, the APFF Microinsurance Sub-Stream[28] convened an international group of microinsurance experts, practitioners and regulators to draft a proposed roadmap for expanding the coverage of microinsurance in the region, referred to henceforth as the Microinsurance Roadmap (MIR).

[28] This APFF Sub-Stream is led by the Deutsche Gesellschaft für internationale Zusammenarbeit (GIZ) - Regulatory Framework Promotion of Pro-poor Insurance Markets in Asia (RFPI Asia).

Table 1: The Process of Developing the APEC Microinsurance Roadmap

Activities/Date/Location	Collaborators	Results
1. APFF Workshop on Microinsurance Development Roadmap for Asia-Pacific Emerging Markets /16 March 2017 / Hanoi, Vietnam	Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) - Regulatory Framework Promotion of Pro-poor Insurance Markets in Asia (RFPI Asia), Ministry of Finance -ISA Vietnam, ABAC	✓ Identified the issues that will be addressed by the MIR ✓ Defined the elements of MIR ✓ Created the interim MIR drafting group (DG)
2. Discussed the concept of MIR in a panel session in the Catastrophe Insurance and Risk Management Summit/23-24 May 2017/ Singapore	Organizer: Equip Global	✓ Raised awareness
3. Drafting the MIR and consultation calls with the DG/June-July 2017/ Various	GIZ RFPI Asia and the MIR DG"	✓ MIR was drafted. Comments collected in the consultation calls with the DG
4. Presented the concept of MIR during the MiN June Members Meeting/28 June 2017/Luxembourg	Microinsurance Network (MiN)	✓ Raised awareness ✓ Campaigned for volunteers to the MIR Drafting Group
5. MIR panel session in the ABAC Financial Inclusion Forum /11 July/ Hoi An, Vietnam	GIZ RFPI Asia, The Foundation for Development Cooperation (FDC), ABAC, Central Bank Vietnam	✓ Gathered inputs and comments to the draft MIR from 4 expert panellists and from the participants of the ABAC FI Forum ✓ Added new members to the DG ✓ Submitted the draft MIR to ABAC for inclusion in the 2017 APFF report to APEC FMs
6. **Coming soon** – APFF MIR Roundtable meeting / 7 Nov 2017/ Lima, Peru	GIZ RFPI Asia, Asociación Peruana de Empresas de Seguros (APESEG), Microinsurance Network (MiN), Munich Re Foundation, Superintendencia de Banca y Seguros (SBS), ABAC	✓ Will gather inputs and comments to the draft MIR from Latin America stakeholders

** The drafting group (DG) is composed of volunteer officials from Asian insurance regulators, regional insurance companies, international network of insurance regulators, global network of microinsurance stakeholders, national association of insurers, international foundation, international consulting/service company, and international development organizations.*

The MIR aims to address the following issues

1. Lack of responsive policies and proportionate regulations supportive of microinsurance;
2. Dearth of scalable business models that takes advantage of large aggregators and the use of fintech;
3. Need for sustainable financial literacy measures that will inform and educate key stakeholders on microinsurance; and
4. Inadequate public-private sector collaboration and poor inter-agency cooperation.

As such, the MIR identifies four key result areas or pillars that will guide APEC member economies in developing an inclusive insurance market. These are:

1. Establishment of policies and proportionate regulations for inclusive insurance and microinsurance;
2. Adoption and replication of scalable business models using fintech for inclusive insurance;
3. Establishment of inter-agency coordination and private-public sector coordination mechanism supportive of inclusive insurance; and
4. Adoption and implementation of financial literacy and consumer protection measures for insurance clients.

The MIR suggests priority action plans that maybe implemented in the short-term, medium-term or long-term depending on the level of enabling environment in the member economy. *See Appendix 2 for a full draft of the MIR.*

Under the current APEC chairmanship of Vietnam and in the upcoming APEC chairmanship of Papua New Guinea in 2018, the APFF wishes to issue the following Recommendations

1. Include the MIR in the 2018 agenda of the Finance Ministers Process and in the 2018 Meeting of Economic Leaders;
2. Collaborate with APFF in identifying stakeholders that would champion the adoption and implementation of MIR in their respective APEC member economies;
3. Mobilize public and private resources that could contribute to the implementation of MIR; and
4. Form oversight groups in each member economy that would steer and monitor the implementation of MIR.

Disaster risk financing and insurance

The Asia-Pacific continues to be the most disaster-prone region on the globe. The year 2016 saw severe earthquakes in Japan's Kyushu Island and New Zealand's South

Island, flooding in the Southern US and China, a large scale wildfire in Canada, and a winter storm in Australia. Their economic consequence has been enormous, largely due to growing concentration of population and economic activities in hazard-prone areas, and recovery from devastation may often take years. It not only slows down economic activities, but also has the potential negative impact on sovereign risk ratings. APEC Finance Ministers are aware of the situation and recognize the need to develop coordinated disaster risk management strategies and to improve their approach to Disaster Risk Financing and Insurance (DRFI) as a means to build resilience in the region.

Consequently, Asia-Pacific policy makers are setting their sights on developing financial instruments to help mitigate the impact of disasters *ex ante*. This complements ongoing efforts to improve disaster response and disaster risk management strategies. It was therefore not a coincidence that the APEC Finance Ministers selected DRFI as one of the priority issues in the CAP. The Ministers identified initiatives and expected deliverables, and how they should be carried out in terms of short, medium, and long-term objectives over the course of ten years. It is worthy of note that CAP recognizes the role of private sector players, and stresses the importance of public and private sectors working closely together. The three sets of deliverables were laid out as follows:

- Establish and promote private disaster insurance schemes (medium/long term).
- Deepen insurance penetration within their economies and develop regional risk sharing measures (long-term).
- Develop a roadmap and network of experts through the support of APFF for expanding the coverage of micro-insurance and disaster risk finance in member economies (medium term).

In response to the CAP's request to study the possibility of constructing a disaster risk data base, it was deemed necessary to start with framing the scope and granularity of what constitutes a database. In order to avoid overlapping or duplication of work with existing initiatives, this needs to be approached mindfully of the limited resources. Meanwhile, APFF continuously stays in contact with international institutions such as the Asian Development Bank (ADB), OECD, WBG, the Insurance Development Forum (IDF) and the Geneva Association to support policymaking efforts pertaining to DRFI.

APFF also collaborates with ASEAN Natural Disaster Research and Works Sharing (ANDREWS), a Working Committee of the ASEAN Insurance Council (AIC). APFF's DRFI expert was invited to the 2nd ASEAN Insurance Summit on 23 November 2016 in Yogyakarta, Indonesia, where DRFI was discussed intensively. It was agreed that the two communities work closely by sharing knowledge and experience with each other.

Under the APEC's 2016 Peruvian presidency, the subject of DRFI was highlighted in APFF's Dialogue with APEC Finance Ministers, which took place as part of the APEC Finance Ministers Meetings in October 2016. In its opening remarks, APFF called for enabling regulatory mechanisms to help private sector companies comfortably write natural disaster risks, by citing catastrophe reserving and risk-based capital systems as examples. Finance Ministers of Japan, Chile and New Zealand each shared their experience in how effectively their national disaster insurance scheme responded in the occasions of large scale natural disasters. The Ministers took note of the importance of designing an *ex-ante* disaster risk insurance system that meets the domestic needs, while putting in place an enabling regulatory system that facilitates private sector insurance companies write more natural disaster risks.

APFF has been encouraging each economy to strategize its financial risk management pertaining to disaster risks. The Peruvian Ministry of Economy and Finance demonstrated leadership in this regard by releasing a report entitled "Peru: A Comprehensive Strategy for Financial Protection Against Natural Disasters." The report lays out strategic lines of action which are specifically designed for Peru, and can be referred as a benchmark for other disaster-prone economies with a view to promote DRFI domestically.

In response to the high level of interest expressed by the Ministers, and building on its milestone, APFF continues to offer its views and expertise through continuous dialogues with officials involved in the APEC-FMP, along with interested stakeholders.

Among a number of potential engagement opportunities in the future, APFF plans to hold a multi-stakeholder dialogue at the World Bosai Forum in Sendai, Japan on 27 November, 2017. The forum is expected to attract government officials, academia and disaster risk practitioners from all over the world. With the accumulated knowledge on disaster risks, APEC and APFF have much to offer to enable a practical and in-depth debate on how to better mitigate financial concerns arising out of natural disasters.

APFF continues to abide by its recommendations as set forth in its 2015 & 2016 Progress Reports. While the APFF's previous recommendations on DRFI remains valid, the timeline is adjusted and reformatted as follows in alignment with CAP and the pace of its progress. Our focus remains with identifying which economies and risks should be prioritized in designing a DRFI scheme. To that end, APFF continues to make itself available for a constructive dialogue between public sector officials and private sector experts towards designing practical DRFI solutions.

CAP Deliverables	APFF Activities	Proposed Timeline		
		2017 (Vietnam)	2018 (PNG)	2019 (Chile)
1. Establish and promote private disaster insurance schemes	✓ Contribution to APEC DRFI seminars	● Presented private sector perspective (@APFF WS on Microinsurance 16 March, Hanoi, Vietnam)	● Continue as an annual effort	● Continue as an annual effort
	✓ Assist APEC in identifying economies and perils of priority	● Initiate discussions with APEC FM officials	● Identify economies and perils of priority*3	● Communicate with relevant officials towards implementation
2. Deepen insurance penetration within their economies and develop regional risk sharing measures	✓ Enhance the availability of risk exposure data (in collaboration with the World Bank)	● Initiate stock-taking on the availability of risk exposure data*1	● Complete stock-taking*4	● Study on risk pooling among APEC Economies
3. Develop a roadmap and network of experts	✓ Formalise an expert group	● Invite core expert members*2	● Broaden the geographical scope	● Continue efforts to expand the network
	✓ Contribute to the drafting of the roadmap	● Plan and organize a multi-stakeholder dialogue @World Bosai Forum, Sendai, Nov 2017	● Initiate the drafting process	● Complete the roadmap

*1 Design a template for stock-taking (ideally through a face-to-face meeting of the DRFI SS experts, to be held by year-end)
*2 APFF's DRFI Sub-stream has so far received support from OECD, the World Bank, the Geneva Association, ASEAN Natural Disaster Research and Works, Citi, Munich Re, Swiss Re and Tokio Marine
*3 To be worked out in conjunction with the 2nd deliverable "deepen insurance penetration" and its identification process of economies and perils of priority (ideally through a workshop-style meeting with the presence of finance ministry officials from the economies prone to natural disasters, to be held by first-half of 2018)
*4 Completing the template for stock-taking (ideally through a workshop-style meeting as indicated above, to be held by first-half of 2018.

DIALOGUE AND RESEARCH ON THE FUTURE OF FINANCIAL REGULATION

APFF continues to provide a platform for research and discussions on the present conditions and future directions of financial markets and regulations, which help authorities and industry deepen their knowledge of markets and anticipate emerging issues. This year, research and discussions were undertaken by various stakeholders under the leadership of the University of Melbourne Team through their Financial Regulation in Asia Project,[29] which seeks to examine, from a multi-disciplinary perspective, the regional architecture for financial regulation in Asia and, in particular, the various ways in which regional coordination and integration can be strengthened.

Following are high-level recommendations and conclusions of these discussions to date:

- The purpose or focus of coordination changes depending on the area concerned. One size does not fit all. In the case of shadow banking, for example, the focus is on information-sharing and monitoring; in the area of consumer financial dispute resolution, on the other hand, the focus is on promoting convergence and harmonization of best practice.

- There are benefits in utilizing and expanding the mandate of existing regional bodies for the purpose of achieving greater regional coordination; e.g. ASEAN+3 Macroeconomic Research Office (AMRO) in the area of shadow banking; SEACEN Research and Training Centre in the area of banking resolution; ASEAN Committee on Consumer Protection in the area of consumer financial dispute resolution.

- There is a need to adopt a flexible approach that takes into account different levels of development and allows different markets to progress at different rates (i.e. a multi-track approach). This is consistent with the ASEAN model of cooperation with its multi-track approach that allows more developed countries to progress towards regional integration at a faster rate while less developed countries implement reforms as and when they have the capacity. A multi-track approach needs to be supported by capacity-building and resourcing support. The post-GFC regulatory response has fostered regulatory divergence in important areas (e.g. Basel III) and, by adding substantial new burdens to regulated entities and regulators, has also increased the divergence in implementation across jurisdictions with large differences in capacity. ASEAN's flexible approach makes a virtue of necessity.

- The ASEAN Banking Integration Framework will face significant challenges in implementation due to the differential financial sector development across the region and differences in the nature of regulatory and institutional arrangements

[29] The team is composed of the following members: Professor Kevin Davis (Finance), Professor Andrew Walter (International Relations), Professor Andrew Mitchell (Law), Professor Ian Ramsay (Law) and Associate Professor Andrew Godwin (Law).

– and is something that warrants more study.

Areas examined to date include Basel compliance and international standards relating to bank supervision, the Asia Region Funds Passport scheme, shadow banking, bank resolution regimes, OTC derivatives market reforms, financial benchmarks, trade in services, consumer finance, and prudential provisions in international trade agreements. Working papers and journal articles have been published and are available on the project website: https://government.unimelb.edu.au/financial-regulation-in-asia.

Areas currently under examination include fintech (coordination and regulatory sandboxes), deposit insurance schemes, the changing politics of regulating systemically important banks, Asia's institutional architecture for financial regulation, bank resolution regimes, Islamic finance, convergence in finance law, cross-border insolvency, financial inclusion, supervision and enforcement under the IOSCO Multilateral Memoranda of Understanding (MMoU), methodologies for coordination and integration, and international commercial courts and coordination.

Another area where research and discussions are being undertaken in conjunction with the APFF is Islamic finance. The work program on Islamic Finance at Harvard University which is being conducted in collaboration with the Capital Cooperation Project Group continues to be focused on the policy mechanisms for capturing Islamic Capital for investment in and the development of long-term essential service projects such as infrastructure.

Recommendations being developed by the Capital Cooperation Project Group are concerned with promoting Islamic investors' interest in infrastructure and in infrastructure related enterprises and with characterizing and positioning infrastructure to comply with Islamic investors' goals and needs. These Recommendations will complement previous Recommendations made by the Capital Cooperation Project Group regarding Sharia compliant interpretations of infrastructure and of a real asset. The recommendations will reflect the import and meaning of making infrastructure investments in the APEC economies within the context both of Islamic finance and of the integration of Islamic capital with conventional capital.

A Harvard University paper, titled "Value and Values of Islamic Finance" which will be completed by late August 2017, will provide the basis for the recommendations currently being framed."

CONCLUSION

The foregoing report highlights the growing interest of APEC member economies to engage with the private sector in a wide variety of areas and confirms the importance of the CAP to the region's economic development. This year, the APFF made progress in starting new collaborative activities with various economies, such as in capital market development (with China and Thailand) and credit information and secured transactions (with Vietnam). The APFF also commenced work on two deliverables under the CAP – the roadmap for developing financial market infrastructure in the Asia-Pacific region and the roadmap for expanding the coverage of microinsurance, both of which are appended to this report.

Progress also continues to be made in the ongoing work on credit information and secured transactions work in the Philippines and Thailand, advancing a pilot project on cross-border sharing of credit information in the Mekong region, the development of a platform for public-private sector dialogue on fintech, support for the Asia Region Funds Passport, creating a platform for enabling Islamic financial institutions to expand cross-border investment in infrastructure, expanding the role of pension funds and insurance firms in infrastructure, and promoting a more active private sector participation in disaster risk financing and insurance.

To help advance the implementation of the CAP in coming years, this report recommends the following to the APEC Finance Ministers:

1. **Encourage relevant officials and regulators to collaborate with APFF's capacity building activities in:**
    - **promoting deep and liquid bond, repo and derivatives markets;**
    - **modernizing credit information, valuation, secured transactions and insolvency systems;**
    - **developing pilot programs for cross-border supply chain financing; and**
    - **expanding long-term investors' roles in infrastructure development.**

2. **Support APFF's efforts to develop a regional platform for public-private dialogue on harnessing fintech to create inclusive, sound and efficient financial systems.**

3. **Encourage senior finance officials to work with APFF in 2018 to finalize the roadmaps envisioned in the CAP for:**
    - **developing the region's financial market infrastructure;**
    - **expanding the coverage of microinsurance; and**
    - **promoting greater private sector participation in disaster risk financing and insurance.**

4. **Encourage more economies to host discussions on the Asia Region Funds Passport (ARFP) where APFF can convene experts from regulatory, industry, multilateral and academic institutions.**

5. **Encourage relevant authorities to collaborate with APFF in finalizing in 2018 a work program for the Islamic Infrastructure Investment Platform (I3P) to help expand cross-border investment by Islamic financial institutions in infrastructure.**