

## **Financing the Expansion of the Region's Infrastructure**

- Development of Bankable Infrastructure PPP Pipelines
- Advancing the I3P
- Expanding the Region's Long-Term Investor Base
  - Infrastructure Investment
  - Regulation and Accounting
- Developing Deep and Liquid Capital Markets

## ADVISORY GROUP MEETING PAPER 6-A

### FINANCING THE EXPANSION OF THE REGION'S INFRASTRUCTURE

The expansion of opportunities for the region's businesses to participate in global supply chains will require massive investments in infrastructure. This in turn requires the development of capital markets, the long-term investor base and bankable infrastructure projects. To this end, APIP and APFF are promoting cross-border financing of infrastructure through the development of a pipeline of bankable projects in key sectors, reforms to expand the investor base (including pension funds, insurance firms and Islamic financial institutions), and expanded cross-border portfolio investment and availability of risk management tools to improve depth and liquidity of bond markets.

#### 3.1. DEVELOPMENT OF BANKABLE INFRASTRUCTURE PPP PIPELINES

Since its establishment in 2011 as a policy initiative of the APEC Finance Ministers, the APIP has brought together high-level officials, experts and private sector advisory panelists from a wide range of relevant fields to collaborate in identifying practical and concrete measures to facilitate private sector participation in infrastructure projects. Since then, the APIP has undertaken several high-level dialogues with a number of economies – with Mexico, Peru and the Philippines in 2011, Vietnam and Indonesia in 2012, the Philippines (second dialogue), Thailand, Indonesia (second dialogue) and Malaysia in 2013, Indonesia (third dialogue) in 2014, the Philippines (third dialogue) in 2015, Thailand (second dialogue) in 2016 and Indonesia (fourth dialogue) in 2017. *This year, the APIP held its first dialogue with Chinese Taipei on 31 July 2018 in Taipei.*

The APIP also continues its work on assisting economies develop pipelines of bankable infrastructure projects in waste management. Last year, the APIP jointly with the APFF held a dialogue on waste-to-energy PPP projects with the Government of Indonesia. A follow-up dialogue with Indonesia is currently being scheduled either in late 2018 or early 2019.

#### 3.2. ADVANCING THE ISLAMIC INFRASTRUCTURE INVESTMENT PLATFORM (I3P)

Since the idea for the Islamic Infrastructure Investment Platform (I3P) was first discussed at the 2015 APEC Finance Ministers' dialogue with the financial industry, it has steadily progressed through a series of conferences and discussions. In October 2017, ABAC Malaysia hosted a conference among key public and private sector stakeholders to discuss the I3P work program. This conference led to the identification of deliverables that can be advanced in six work streams. These are as follows:

##### Work Stream 1: Harmonizing Investment Requirements and Regulations

- Minimum benchmarks for Islamic contracts (e.g., mudaraba, musharaka, ijara), sharia-compliant infrastructure projects and concession agreements
- Adoption of benchmarks by interested APEC member jurisdictions

##### Work Stream 2: Addressing Tax Policy Issues

- Minimum benchmarks for promoting tax neutrality between Islamic and conventional finance, including the following: (a) tax treatment of profits (e.g., whether interest payments qualify for tax deductions); (b) tax treatment of multiple transactions between company and sukuk-issuing SPV, with respect to disposal issues, sale and leaseback); (c) stamp, withholding, value added/goods and services taxes, real property gains tax vs. capital gains tax; (d) establishment of tax neutrality committees that can grant specific approvals (while awaiting legislative reforms); (e) approaches (e.g., product-by-product, case-by-case or blanket legislation, formulating tax neutral policy framework, white list of transactions qualifying as tax neutral, coordination between legislators and supervisors)
- Tax incentives to facilitate transactions (e.g., for borrowers or issuers on a stand-alone basis or in conjunction with conventional products, whether tax incentives for infrastructure projects should be treated differently from other commercial transactions)
- Regional minimum benchmarks for sharia auditing and sharia advisers

##### Work Stream 3: Risk Mitigation Instruments

- Legal reform to facilitate use of derivatives (e.g., those related to certainty and enforceability of derivatives transactions, clarity of insolvency and enforceability of netting provisions, clarity of treatment of collateral, role of courts and/or arbitration tribunals, treatment of foreign law-governed contracts and foreign-based counterparties, set-off rights, financial collateral arrangements, guarantees, letters of credit, insurance, credit derivatives)

## ADVISORY GROUP MEETING PAPER 6-A

- Adoption of standardized documentation (e.g., ISDA/IIFM TMA)
- Regional minimum benchmarks for legislation governing derivatives
- Best practices in enabling policies for new Islamic derivatives for equity risk management (e.g., hedging against market downturn)

### Work Stream 4: Enabling Financial Innovation

- Addressing key legal and regulatory barriers to hybrid/blended financial instruments combining different types of contracts that address different issues and mix/match parties' interests with cash flows and contract design (e.g., musharaka with other types of structures like ijara embedded, combining sukuks with different characteristics such as those for construction and those for leasing), which may include regulations on: (a) equity or corporate bond investment; (b) pension fund, insurance company and asset manager investments; (c) investment in unlisted infrastructure companies; (d) direct investments in projects; (e) infrastructure funds or investments; (f) alternative investments; (g) minimum ratings for bonds; (h) foreign exposure; (i) hedging of transactions involving multiple currencies

### Work Stream 5: Developing Project Preparation Capacity and Pilot Projects

- Best practices in embedding sharia-compliance into design of projects for wider investor base
- Improved capacity of relevant officials to use project preparation tools (GIH InfraCompass, GIH Risk Allocation Matrices, GIH Project Pipeline, SIF Source)
- Starting benchmark/pilot projects with support mechanisms (e.g., obtaining foreign investment through MIFC, wraps to address cross-border and political risk, MDB guarantees and project enhancements) and embedded sharia-compliance in design

### Work Stream 6: Establishing the I3P Secretariat

- Terms of reference for I3P Secretariat
- I3P Network Directory
- I3P Online Resource Center, including database of (a) sharia-compliant infrastructure projects, (b) sharia-compliant infrastructure funds, (c) case studies, (d) experts in Islamic finance in the areas of financial products, law, valuation, tax, audit, ratings, insurance, pension funds, asset management, (e) common definitions.

*This year, the APFF I3P Network plans to convene stakeholders to discuss concrete activities in 2019 and 2020 to begin working on the deliverables. The conference will be hosted by ABAC Malaysia on 2 October in conjunction with the 2018 Global Islamic Finance Forum at Sasana Kijang, Kuala Lumpur.*

### 3.3. EXPANDING THE REGION'S LONG-TERM INVESTOR BASE

The 2017 Joint Finance Ministerial Statement described actions to be implemented by APEC economies over the next year to achieve strong, sustainable, balanced and inclusive growth. It included measures to address long-term infrastructure investment, financial inclusion, disaster risk financing and insurance. It also contains an annex on diversifying financing sources and fostering private sector involvement in infrastructure investment in APEC economies. Since 2013, APFF has been working on promoting the role of long-term investors, including insurers and pension funds, to support sustainable, resilient and inclusive growth and development of the Asia-Pacific region. The following describes the progress of work in this area:

#### ***3.3.1. Infrastructure Investment***

The APFF continued dialogue with policymakers and authorities to expand quality infrastructure investments by insurers and pension funds, including the development of financial vehicles and regulatory changes to treat infrastructure as an asset class. The APFF contributed to roundtables and workshop meetings throughout the year in collaboration with global and regional initiatives. The APFF examined possible improvements, including financial vehicles, sustainable investing, and specific areas where regulations can be amended to remove unnecessary burdens.

#### ***3.3.2. Regulation and Accounting***

The APFF engaged in continuous outreach with policymakers, regulatory authorities and accounting standards setters, focusing on the adoption of solvency and accounting regimes that do not discourage insurers from engaging in long-term business and making long-term investment in infrastructure and capital markets.

Among other activities, the APFF successfully organized the APFF Roundtable on Insurance and Regulations and

## ADVISORY GROUP MEETING PAPER 6-A

Accounting in October 2017 in Hong Kong, inviting IASB, insurance supervisory authorities, accounting firms and industry experts in the Asia-Pacific region. Topics included implementation of IFRS17, solvency reform in the region. Issues identified during the roundtable were used as basis for further dialogue with standard setters and stakeholders. *The APFF plans to hold a follow-up Roundtable in November 2018 in Hong Kong.*

The APFF will continue dialogues with insurance regulators in specific APEC economies, including Thailand, Indonesia, Hong Kong, and Chinese Taipei regarding the implementation of IFRS17 ('Insurance Contracts') and IFRS9 ('Financial Instruments'), including its impact on solvency assessment. Although IFRS17 has been issued on 18 May 2017, there are some technical and practical aspects yet to be addressed. The APFF continues to work on regulatory and accounting issues with global and regional bodies in reflecting economic reality and long-term nature of the business, avoiding disincentives for insurers in undertaking long-term investments and business and in financing sustainable growth in the long-run.

### 3.4. DEVELOPING DEEP AND LIQUID CAPITAL MARKETS

Deep and liquid capital markets play important roles in financing infrastructure. Since 2015, APFF has focused its work on implementing the CAP deliverable to support the improvement of capital market depth and liquidity, promoting the development of liquid repo markets, legal and documentation infrastructure facilitating risk mitigation, and the development of a roadmap to improve regional financial market infrastructure.

APFF supported the development of the Asia Region Funds Passport (ARFP). Among the activities and achievements are the following:

- In 2017, 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 *engage regulators and officials as they worked to advance the ARFP.*
- In October 2017, The APFF *met with members of Chinese Taipei Financial Supervisory Commission (FSC)* to provide updates on ARFP developments and shared best practices from jurisdictions with similar fund passporting schemes such as UCITS.
- APFF shared insights with representatives of the Pacific Alliance as they look to develop a similar funds passporting arrangement, and participated in various ARFP regulator working group meetings and industry events to *provide updates on issues related to taxes, fund back office operations, redemption fees, and market trends*, among others.

Last year, APFF completed the draft of the Roadmap for the Development of APEC's Financial Market Infrastructure. The Roadmap was presented to the APEC Finance and Central Bank Deputies in March 2018 and incorporated suggestions that were received from officials. It is proposed that APEC Finance Ministers encourage public sector stakeholders to collaborate with the APFF in implementing the Roadmap.