Prioritisation of Work to Inform Effective Implementation Approaches of G20/OECD High Level Principles on Long-term Investment Financing by Institutional Investors

For further information, please contact Mr. André Laboul, Head of the Financial Affairs Division, OECD; [Tel: +33 1 45 24 91 27; Fax +33 1 44 30 61 38; E-mail andre.laboul@oecd.org] or Mr. Raffaele Della Croce, Lead Manager, Long Term Investment Project, OECD [tel: +33 1 45 24 14 11; E-mail: raffaele.dellacroce@oecd.org]

OECD
BETTER POLICIES FOR BETTER LIVES

Organisation for Economic Co-operation and Development,
2 rue André-Pascal, 75775 Paris cedex 16, France
www.oecd.org

G20/OECD TASK FORCE ON INSTITUTIONAL INVESTORS AND LONG TERM FINANCING

PRIORITISATION OF WORK TO INFORM EFFECTIVE IMPLEMENTATION APPROACHES OF G20/OECD HIGH LEVEL PRINCIPLES ON LONG-TERM INVESTMENT FINANCING BY INSTITUTIONAL INVESTORS

[Note by the chair (Mr Damien Dunn, Australian Treasury), revised on the basis of comments expressed at the 5th meeting of the G20/OECD Taskforce on Institutional Investors and Long Term Financing, held on the 26th of November 2013 and through written comments.]

Overview

Since its inception, the key focus of the Task Force has been the development of the joint G20/OECD High-Level Principles on Long-Term Investment Financing by Institutional Investors (the Principles). The Principles were endorsed by G20 Leaders at their Summit in St Petersburg in September 2013. At the same time, G20 Leaders asked their Finance Ministers and Central Bank Governors to identify approaches to their implementation working with the OECD and other interested participants by the next Leaders' Summit, in November 2014 in Brisbane, Australia.

In order to develop implementation approaches for the Principles, it appeared necessary for the Task Force to prioritise those Principles which members see as most important to focus on in the first instance to allow the Task Force, the OECD and G20 membership and other interested participants to utilise their resources effectively.

In addition to the Principles, the OECD delivered three reports to the G20 Study Group on Financing for Investment in 2013. Over the next 12 months, the OECD is due to lead on, and deliver, seven further reports to the G20 on various aspects of the investment agenda, and provide contributions to five reports led by other international organisations. The Task Force could assist the G20 to deliver Leader-like outcomes in 2014 by providing guidance on prioritising those reports most relevant to the Principles. It could then draw together the findings of the most relevant reports to identify possible approaches to the implementation of the Principles.

Prioritisation of work on the Principles based on discussion held at the Task Force meeting on the 26th November 2013

Delegates were encouraged to identify issues related to the Principles, on which the Task Force should focus its work in 2014. Different ways of progressing this work were also suggested.

The Task Force will first focus its work on a few of the principles that relate most closely to G20 priorities for investment and require delivery in 2014 to achieve outcomes by the September G20 Finance Ministers and Central Bank Governors Meeting, and November Leaders Summit. Principle 5 was broadly recognised as a key area where the Task Force could add value; as were Principles 2 and 3 and elements of Principle 1 and 4. The other principles (Principles 6, 7 and 8) and the remaining elements of the key principles will be dealt with at a later stage by the Task force and/or in parallel, by the G20 Infrastructure and Investment Working Group and relevant international organisations. The Task Force will review/coordinate those effective approaches related to the Principles possibly developed by other fora/IOs in order to make sure they are consistent with the Principles and the other approaches.

Principle 1: Preconditions for long-term investments.

While the scope of this principle is quite large, the objective would be to first focus on some key issues, noting that a number of the issues will also be considered through other G20 work, including 1.3 on stable macroeconomic conditions and 1.8 on private investment incentives. Issues that could warrant further consideration by the Task Force at this stage include: 1.1 on the consistency of policies promoting long-term investment with the best interest of the relevant stakeholders, security , diversification etc. objectives , including risk-return analysis (with the objective to set up a check-list) and 1.5 on business regulation and supervision. Tax neutrality as reflected in 1.4 may also be included.

Principle 2: Development of institutional investors and long-term savings.

Effective approaches would especially focus on the various incentives listed in paragraph 2.2 (with many of the issues to be addressed in the forthcoming survey on instruments and incentives for funds for long-term investment). They would inter alia be identified with inputs from the International Network for Financial Education.

Principles 3: Governance of institutional investors, remuneration and asset management delegation.

The identification of effective approaches will benefit from existing OECD guidelines on governance of insurance companies and pension funds. Issues on remuneration will need to take into consideration work developed by other fora, including the FSB.

Principle 4: Financial regulation, valuation and tax treatment.

Implementation approaches for this principle will be developed taking into account discussions at international level. Several delegates noted the importance of the principle (particularly 4.1, but also in relation to principle 1.2, 1.4 and 3.8), but also the risk of duplication with work already undertaken by the FSB or other IOs. To ensure proper coordination it was suggested for the next Task Force meeting, that the OECD, FSB and IMF could provide a roadmap on potential work to be developed by the Leaders summit in 2014.

Principle 5: Financing vehicles and support for long-term investment and collaboration among institutional investors.

Based on research presented at the meeting and current work underway at the OECD, delegates expressed support for further work by the Task Force in this area. The work on this principle could focus on risk mitigation, pooled vehicles (also promoted in Principle 2) and other instruments for long-term investment (i.e. project bonds or securitised assets) and a supportive policy environment for long-term investment in SMEs and infrastructure.

Comments were made on the importance of focusing on new projects (greenfield projects) and the relevance to include all the stakeholders in the analysis of financing vehicles: institutional investors but also banks and asset managers. In relation to public intervention in long-term investment projects a few comments were made on the role of MDBs in leveraging private sector capital. The chair requested that the

WB report back to the next meeting of the Task Force on the state of current research on optimization of MDBs and regional banks' balance sheets.

Principle 7: information sharing and disclosure

A major issue is also related to the lack of adequate data and information on LTI, negatively affecting the investment conditions for investors and ultimately constraining allocation to long term assets. The Task Force would be expected to explore ways to promote further information sharing and disclosure essential at macro and micro level. Additional data collection on institutional investors should take into careful consideration the issues raised in principle 7 of the High Level Principles.

Modalities

Data on potential effective approaches to the implementation of the Principles will be collected from current national and international evidences as well as through a dedicated survey to be developed based on the discussions held on 26th November.

Prioritisation of OECD reports that relate to the Principles

Most OECD reports requested by the G20 relate in some way to the Principles. However, some are particularly relevant, and it was agreed that these should be prioritised by the Task Force. Furthermore, some principles are lacking any analysis by the OECD or other international organisations and may require new work to ensure that approaches to implementation are sufficiently informed. A summary of each report and the Chair's view on relevance to the Principles, endorsed by the Task Force, are detailed further below. The reports are ranked from most-to-least relevant in terms of developing approaches to implementation of the Principles.

It was also noted that given the time required to develop effective approaches, the delivery of some of these reports may have to be postponed.

Revised timetable – OECD reports to Study Group – as proposed by Chair of Task Force on Institutional Investors

Item and ranking	Revised timetable for delivery	Relates to which OECD Principles	Rationale
(1) Analysis of Government and Market-Based Instruments and Incentives to Stimulate Long-Term Investment Finance (see also the summary record of the 26 November 2013 meeting of the Task Force) ***OECD (lead), with input from WBG***	The report will have two components a)inventory of instruments and incentives b) thematic issues on --1. institutional investors --2. corporate financing --3. bank lending models November 2013 (draft of first thematic part of the report on *Infrastructure Investment by Institutional Investors see 2)* Autumn 2014 (consolidated report)	1 – Pre-conditions for long-term investments 2 – Development of institutional investors and long-term savings 4 – Financial regulation, valuation and tax treatment 5 – Financing vehicles and support for long-term investment and collaboration among institutional investors 6 – Investment restrictions	The first thematic part of the report is highly relevant to the high priority principles and their implementation. The second and third thematic parts are not strictly applicable to institutional investors and not directly relevant to implementation of the Principles. The overarching analysis will be based on a survey of existing instruments and incentives relevant to the principles. All parts of report could guide the G20 towards practical deliverables in 2014. NB: Will draw on the report *Insurers and Pension Funds as Long-Term Investors: An Approach to Infrastructure Investment* (also a high priority for the Task Force)
(2) Insurers and Pension Funds as Long-Term Investors: An Approach to Infrastructure Investment **OECD (lead) with input**	November 2013 (draft) 2014 (final)	1 – Pre-conditions for long-term investments 5 – Financing vehicles and support for long-term investment and collaboration among institutional investors	Highly relevant to high priority principles and their implementation. Content could be very useful for many G20 countries looking to create an enabling environment for institutional investment in infrastructure. Could also guide G20 towards a practical deliverable in 2014.

Item and ranking	Revised timetable for delivery	Relates to which OECD Principles	Rationale
from WBG			
(3) Regulations and Incentives Affecting Long-Term Institutional Investors **OECD (lead), with input from FSB, WBG, IMF and UN DESA.**	Early 2014 (modelling) June 2014 (draft) Late 2014 (final)	1 – Pre-conditions for long-term investments 3 – Governance of institutional investors, remuneration and asset management delegation 4 – Financial regulation, valuation and tax treatment	Highly relevant to several Principles and their implementation.
(4) Trends in Global Asset Allocation of Institutional Investors **OECD (lead), with input from IMF and WBG**	March 2014 (draft) H2 2014 (final) Delay from original	7 – Information sharing and disclosure	Highly relevant. Provides evidence –based information and analysis
(5) What are the Risk-Return Characteristics of Private Infrastructure as an Asset Class? **OECD (lead), with input from WBG**	First results sometime in 2014; final delivery unknown	7 – Information sharing and disclosure 4 – Financial regulation, valuation and tax treatment	Relevant to some Principles.

Item and ranking	Revised timetable for delivery	Relates to which OECD Principles	Rationale
(6) Good practices in addressing policy impediments to FDI in infrastructure (preliminary report) **OECD (lead), with input from UNCTAD and WBG**	2013	1 – Pre-conditions for long-term investments 6.2 – Barriers to international investment	Though not strictly applicable to institutional investors, may be broadly relevant to implementation of the Principles. Drafting of report should be well underway and close to circulation.
(7) Improved methodology for measuring FDI, including green FDI **OECD (lead) with input from UNCTAD and WBG**	First results sometime in 2014; final delivery unknown	n/a	Not directly relevant to the Principles.

OECD reports already delivered			
Item	**Delivered**	**Relates to which OECD Principles**	**Useful for implementation**
Survey of Pension Funds' Long-Term Investments	To Finance Ministers and Central banks Governors October 2013	1 – Pre-conditions for long-term investments 5 - Financing vehicles and support for long-term investment and collaboration among institutional investors 7 – Information sharing and disclosure	Provides evidence –based information and analysis; directly relevant for the Principles
Policy guidance for investment in clean energy infrastructure	To Finance Ministers and Central banks Governors October 2013	Most – but particularly: 1 – Pre-conditions for long-term investments 3.8 – governance by regulatory and supervisory authorities 4 – Financial regulation, valuation and tax treatment 5 – Financing vehicles and support for long-term investment and collaboration among institutional investors 6 – Investment restrictions 7 – Information sharing and disclosure 8.1, 8.2 – financial inclusion/education and consumer protection frameworks	Provides policy guidance useful for delivering implementation approaches on high and medium priority principles.
Institutional Investors and Green Infrastructure Investments: Selected Case Studies	To Finance Ministers and Central banks Governors October 2013	1 – Pre-conditions for long-term investments 3.4 – Identifying, measuring, monitoring and managing the risks associated with long-term assets as well as any long-term risks 4 – Financial regulation, valuation and tax treatment 5 – Financing vehicles and support for long-term	Directly applicable to the Principles and provide broad lessons for governments on the policy setting which could support the implementation of the Principles .

		investment and collaboration among institutional investors 6 – Investment restrictions 7 – Information sharing and disclosure	

APPENDIX 2 – DESCRIPTION OF SELECTED OECD "LEAD" REPORTS (SOURCE G20 WORKPLAN ON FINANCING FOR INVESTMENT, SEPTEMBER 2013)

1. Analysis of Government and Market-Based Instruments and Incentives to Stimulate Long-Term Investment Finance – OECD (lead), with input from WBG

Building on the identification of Government and market-based instruments and incentives to stimulate long-term investment finance, the report will provide analysis and policy good practices for addressing related challenges. It will also develop more thematic approaches in three main areas that are critical to long-term investment finance: infrastructure investment by institutional investors, corporate financing and bank lending.

a) inventory of instruments and incentives

The final report will provide an international comparative in-depth policy analysis and overview of main types of government and market-based instruments and incentives used to stimulate the financing of long-term investment, based on existing international overviews and new surveys when relevant.

b) sub-themes

The report will also thematically address three main areas of long-term investment financing: infrastructure investment by institutional investors, corporate financing (including issues related to corporate governance) and bank lending (and related business model issues). These three specific outputs will be delivered in different parts.

The first part, on infrastructure investment, will draw on the report Insurers and Pension Funds as Long- Term Investors: An Approach to Infrastructure Investment (see above item 3 of the summary record).

The second part will address issues related to the changing nature of capital markets and their role in financing long-term investment by corporations. It will examine the ability of new firms to come to public equity markets and the explanations for falling IPO numbers and volumes. It will also examine the extent to which companies are issuing bonds to buy back shares and increase dividends as opposed to investing in the business. It will include issues related to corporate governance and the value chain.

The third part of the report will address the question of bank models and how leverage, derivatives operations and other aspects of a bank's business may affect its ability to engage in long-term lending.

2. Insurers and Pension Funds as Long-Term Investors: An Approach to Infrastructure Investment—OECD (lead) with input from WBG

The report will focus on the financial instruments, models, and regulatory and institutional conditions that can make infrastructure investment attractive for pension funds and insurers.

The paper aims to contribute to the current discussion on the prospects of new infrastructure models and the potential role of institutional investors. The analysis would consider models for infrastructure adopted by selected countries and new models currently in discussion, both on the equity and fixed income side, in OECD and G20 countries.

Starting with the analysis of old models still of relevance today (listed funds, private equity and monoline guaranteed project bonds) to new forms (direct/co-investment, club format investment, i.e. pooling of pension funds, new set of infrastructure funds, open-ended model (IFM in Australia, PIP initiative in the UK), EU/UK project bonds initiatives, debt funds and institutional investors' direct lending. The report will address the role of policymakers in promoting financing instruments and models for infrastructure investment by institutional investors that are efficient and sustainable and contribute both to delivering good performance to investors and to a positive economic impact.

The work would draw on practical experiences by institutional investors around the world, bringing a high level of practical relevance to the work.

This report will also be an input for the paper requested by the G20 on Analysis of Government and Market-Based Instruments and Incentives to Stimulate Long-Term Investment Finance

3. Regulations and Incentives Affecting Long-Term Institutional Investors—OECD (lead), with input from WBG, FSB and UN DESA.

The report addresses the impact of different prudential regulations such as governance, investment and solvency on long-term investment by institutional investors. It will also look at other policy drivers of long-term investing such as taxation and institutional factors.

The report will include a specific practical exercise on the impact of risk-based solvency regulations on investment strategies of pension funds and insurers "funds", based on asset610 liability stochastic modeling.

The report will provide evidence and supporting analysis on the implications of regulations and incentives for long-term investment, covering three main types of institutional investors (pension funds, insurers and sovereign wealth funds).

The analysis will draw on country experiences and will provide input for the identification of good practices regarding regulation, drawing also on existing international standards including the OECD and IOPS work on pension funds, and OECD and IAIS work

4. Trends in Global Asset Allocation of Institutional Investors (including from Survey of Pension Funds' Long-Term Investments) —OECD (lead), with input from IMF and WBG

Assessment of trends in asset allocation by pension funds, life insurers and sovereign wealth funds (main long-term investors), focusing on infrastructure investments.

The G20 Finance Ministers and Central Bank Governors communiqué from February welcomed the OECD survey on pension funds' long-term investments.The report will provide evidence on the extent to which long-term investors are taking up opportunities to invest in infrastructure and green projects.

The responses will also help inform policymakers regarding the practical challenges faced by institutional investors (in particular pension funds who will reply to the questionnaire) and the needs of such investors to channel their funds to long-term projects.

5. What are the Risk-Return Characteristics of Private Infrastructure as an Asset Class?—OECD (lead), with input from WBG

The general objective of this research proposal is to determine the risk-return characteristics of private infrastructure as an asset class. Initially the focus will be on private infrastructure equity (henceforth 'infrastructure'). At a later stage, risk-return on infrastructure bonds can be considered. The way to achieve this is by estimating systematic risk exposures of the realized cash flows (as well as reported NAVs) of a large sample of infrastructure investments by institutional investors. Scarcity and confidentiality of performance data is a problem for these investments, but by combining anonymous estimates from the various institutional investors with the OECD acting as an independent and objective intermediary, it is possible to compare the outcomes for the different investors and achieve a better understanding of the risk-return properties of infrastructure as an asset class.

The data will be collected from institutional investors, some of whom have already committed themselves to providing such information.

Through this project, the OECD will support stronger efforts in independent data collection and objective information provision in the field of infrastructure investment. While the quantitative and qualitative evidence collected through the survey will be of prime value to the ultimate investors, it will also be used to inform regulators and other policy makers, complementing national and supra-national statistical data collection with a view to better capturing infrastructure flows.

6. Good practices in addressing policy impediments to FDI in infrastructure—OECD (lead), with input from UNCTAD and WBG

The OECD undertakes a great deal of work aimed at helping host countries identify and tackle country-specific obstacles to FDI in infrastructure. Relying on policy instruments such as the OECD Principles for Private Sector Participation in Infrastructure and the OECD Recommendation on Principles for Public Governance of PPPs, as well as on the experience mobilized by networks of PPP practitioners such as the SADC PPP Network or the OECD Network of Senior Budget Officials on PPPs, the OECD is undertaking work aimed at highlighting how to address obstacles to FDI in infrastructure.

The study will identify policy lessons regarding FDI in infrastructure. FDI is growing in importance as a source of financing for infrastructure, but major policy impediments still exist in some countries.

7. Improved methodology for measuring FDI, including green FDI—OECD (lead) with input from UNCTAD and WBG

The OECD's Working Group on International Investment Statistics, which sets the world standards for measuring FDI, has started work to develop a methodology to measure green and climate-specific FDI as part of official statistics. This work will be an extension of the OECD Benchmark Definition of Foreign Direct Investment, 4th edition (2008).

Public finance was the main driver for investment in cleaner and low-carbon infrastructure technologies. However, there is a general recognition that public finance will not be sufficient to overcome environmental challenges, highlighting the need to mobilize private investment, of which the large majority is FDI.

Many countries are making efforts to put in place policies to stimulate environmentally-friendly investments and to scale up the financing and implementation of green technologies and infrastructure projects. In the absence of adequate statistics, governments face major challenges in assessing the real impact of their policies.