Comments Template on EIOPA-CP-15-004 Consultation Paper on the Call for Advice from the European Commission on the identification and calibration of infrastructure investment risk categories		**Deadline 09.August.2015 23:59 CET**
Company name:	Long-Term Infrastructure Investors Association (LTIIA)	
Disclosure of comments:	EIOPA will make all comments available on its website, except where respondents specifically request that their comments remain confidential. Please indicate if your comments on this CP should be treated as confidential, by deleting the word Public in the column to the right and by inserting the word Confidential.	Public
	Please follow the instructions for filling in the template: ⇨ Do **not** change the numbering in column "Reference". ⇨ Please fill in your comment in the relevant row. If you have no comment on a paragraph, keep the row empty. ⇨ Our IT tool does not allow processing of comments which do not refer to the specific paragraph numbers below. ○ If your comment refers to multiple paragraphs, please insert your comment at the first relevant paragraph and mention in your comment to which other paragraphs this also applies. ○ If your comment refers to sub-bullets/sub-paragraphs, please indicate this in the comment itself. **Please send the completed template to CP-15-004@eiopa.europa.eu, in MSWord Format, (our IT tool does not allow processing of any other formats).** The paragraph numbers below correspond to Consultation Paper No. EIOPA-CP-15-004.	
Reference	**Comment**	
General comments	LTIIA welcomes the contents of this paper following the previous round of consultations (CP-15-003), noting the recognition by EIOPA of a need for tailored treatment of (low-risk) infrastructure investments in general as well as recommendations for lowering Equity Risk Charge and the introduction of a discount for the Spread Risk Charge for infrastructure debt, specifically.	

	We believe that the EIOPA's analysis and recommendations can benefit from drawing a deeper distinction between listed and unlisted equity investments in infrastructure and from being more explicit about the prevalence of substance over (legal) form in some of the EIOPA definitions and criteria. We believe in particular that regulators should leave some flexibility to insurers in assessing if an infrastructure investment qualifies under the newly created category. In other words, not meeting one criterion as identified by EIOPA should not automatically lead to disqualifying one specific investment if not meeting this criterion does not lead to material deviation from the infrastructure features that EIOPA has intended to capture. This minimal flexibility will be essential, should EIOPA advise maintaining a detailed list of qualification criteria. In our view, the criteria proposed tend to limit the infrastructure space to PPP and renewables, to the exclusion of projects with material demand risk. In terms of new asset finance per year, PPPs and renewables in Europe represent only ca. €20 billion each (sources: *Market Update. Review of the European PPP Market in 2014*, by EPEC and *Global Trends in Renewable Energy Investment 2015*, by UNEP/Bloomberg), or less than 20% of the total infrastructure investment needs in Europe estimated by EIB (source: *Private Infrastructure Finance and Investment in Europe*, EIB Working Paper 2013/02). We therefore suggest a more inclusive approach in setting and implementing the infrastructure criteria by EIOPA to avoid limiting the application scope for this standard to a minor part of the market. Our specific comments on these and other topics are captured below.	
Section 1.1.		
Section 1.2.		
Section 1.3.		
Section 1.4.		
Section 1.5.	Para 1.22. Using listed infrastructure equities as a proxy of unlisted infrastructure leads to significantly overstating the volatility of the latter – especially, in the context of long-term hold with a very low probability of a forced sale. While data series on unlisted infrastructure equities are still relatively scarce, in-house research by some of our members based on ca. 10 years of observed	

	performance of Australian unlisted infrastructure assets suggests that unlisted infrastructure features 'smoothing and lagging effect' similar to that since long recognized in unlisted real estate (see, for example, an overview in Geltner D, MacGregor BD and Schwann GM. *Appraisal Smoothing and Price Discovery in Real Estate Markets*, Urban Studies May 2003 40: 1047-1064). LTIIA, together with EDHEC-Risk institute, has been developing a platform that would enable collection and tracking of historic unlisted performance data for long-term investments in infrastructure. Next year, we expect that platform to provide additional quantitative evidence on the volatility of unlisted infrastructure. In the meantime, a 'rule-of-thumb' view on the volatility of unlisted infrastructure assets adopted by some of investors has been that it equals half of the volatility of the listed peers. With that assumption in mind, a further reduction in recommended Equity Risk Charge for *unlisted* infrastructure can be justified – potentially down to the 15-20% range. This rule of thumb approach is not inconsistent with observations of the listed PFI portfolio researched by Dr. Blanc-Brude on a monthly basis (20-25% VaR), and we believe that considering monthly behaviour is already conservative given the above smoothing and lagging effect of unlisted infrastructure.	
Section 2.1.		
Section 2.2.		
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Section 2.5.3.		
Section 3.1.		
Section 3.2.		
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Section 3.2.2.		
Section 3.2.3.		
Section 3.3.		
Section 3.3.1.	Para 1.70. While we support defining infrastructure primarily by its purpose rather than by sector, we think that listing actual infrastructure sectors as they are commonly known, is an important part of the definition. We suggest mentioning the following sector titles: transport, energy, utilities, telecommunications and social infrastructure (such as hospitals and schools). Para 1.71. While we agree that serving the public good is an important differentiating feature of infrastructure, we consider it critical that the *form* of contracting infrastructure assets does not alone condition the judgement of whether the public good is served or not. For example, in the provided illustration of electricity plant contracted by a single factory, it would be important to establish whether the generation is passed-through to manage disbalances in the public grid. Para 1.72. We would suggest that this paragraph reads: "For the purpose of defining infrastructure investments with a better risk profile than implied by their current standard formula treatment the requirement of monopolistic or oligopolistic position has to be included." This wording clarifies the notion of "limited competition" used in the paper without using the example of a parallel toll road, which we find questionable and, potentially, misleading. Given the significant capital outlay involved in the development of infrastructure projects, cases of infrastructure assets	

	competing with each other in the 'free market' sense are typically limited to oligopolistic situations facing lower-than-expected demand. In the toll road example, the road would never be built if the existing routing provided multiple alternatives at the expected traffic volume in the corridor. So the competition is not driven by the number of incumbent players or entrants but rather by the fluctuation in demand in the monopolistic or oligopolistic setting. Also, for the sake of good order, many infrastructure projects feature *very low* operational leverage – including roads, social infrastructure, telecommunication towers, power cables etc. Advice. The meaning of "substantial degree of control" need to be clarified. Lenders tend to apply much tighter controls for greenfield assets (especially, during the construction phase) compared to the brownfield assets.	
Section 3.3.2.		
Section 3.3.2.1.		
Section 3.3.2.2.	Para 1.89. Requirements regarding predictability of expenses have limited relevance for assets with low operational leverage (unless expected DSCR is very low).	
Section 3.3.2.3.		
Section 3.3.3.		
Section 3.3.4..		
Section 3.3.4.1.		
Section 3.3.4.2.		
Section 3.3.4.3.	Para 1.104. The matching of amortization schedule to the remaining life of the contract governing revenues of an infrastructure asset could be relevant in this context. However, in certain sectors (e.g., port terminals, mobile towers) the revenue contracts are customarily limited to periods much shorter than the expected economic activity of the assets – with a view for both asset owners/operators and asset users to maintain a degree of flexibility and upside at re-contracting. In such circumstances, it is important to assess the remaining economic life of the assets rather than the remaining life of the contract alone, taking into account past customer churn rates amongst other	

	factors. In certain contexts, residual asset value at the end of the contract or expected economic life can be established with a great certainty. For example, in the Danish PPP market the government can commit to a Terminal Value payment. A strong visibility on such residual values can justify partial amortization (if any), with bullet repayment or refinancing in the end carrying limited risk.	
Section 3.3.4.4.	Advice. Suggest widening the language of sub 2(a) to allow entry into construction contracts with "risk-sharing arrangements between contractor and developer that substantially indemnify the developer from financial consequences of construction delays and cost overruns occurring for no developer's fault".	
Section 3.3.4.5.	Advice. In our view, the mitigation of operating risks depends primarily on the expertise and incentives of those handling the operations, whether they are contracted via a separate entity or not. For example, it can be more beneficial for all investors in an infrastructure project entity if the entity self-performs operations and maintenance in a situation when one of the investors has significant expertise in this field. Also, it is a common market practice for gas and electricity grid companies to self-perform O&M, and we do not believe they should be excluded on that basis. We suggest augmenting the advice with an endorsement of self-performance of the operating activities by an infrastructure project entity provided the expertise and incentive requirements have been met.	
Section 3.3.4.6.	Ramifications of design and technology risk can be broader than operational non-delivery. Another important aspect – imposing a revenue risk – is the development of new technologies. For example, mobile telecommunications infrastructure, such as telecommunication towers, is exposed to the risk of new technologies for provisioning digital bandwidth rendering the tower networks obsolete.	
Section 4.1.		
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Section 6.1.		
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Section 6.2.1.		
Section 6.2.2.		
Section 6.2.3.	We consider it important to emphasize that conclusions from the analysis presented in this section (and detailed in Annex V) can be drawn for listed infrastructure equities only. While we are not suggesting that conclusions for unlisted infrastructure would necessarily be qualitatively different,	

	however the VaR and worst drawdown estimates established using monthly and daily volatilities are not descriptive of unlisted infrastructure performance whose valuations are typically subject to a yearly revision cycle, smoothening and ±6 month lag to the general market conditions.	
Section 6.3.	See comment to Section 1.5 above. We also believe that greenfield projects having satisfied the construction and revenues risks management criteria should benefit from a treatment similar to that of operational projects, in particular at portfolio level (since construction risk is idiosyncratic).	
Section 7.1.		
Section 7.2.		
Section 7.3.		
Section 8.		
Annex I		
Annex II		
Annex III Sections:		
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Annex V		