

QIC GLOBAL INFRASTRUCTURE
RESPONSIBLE INVESTMENT REPORT 2018

QIC



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QIC RESPONSIBLE INVESTMENT

We believe that environmental, social and corporate governance (ESG) factors can have a material impact on the long-term returns of investment portfolios. This was the motivation for QIC becoming a signatory to the United Nations backed Principles for Responsible Investment Initiative (UNPRI) in 2008. We believe the expectations of our clients and the community are that we consider ESG as part of our long term investment framework and continue to improve the delivery of infrastructure services for all stakeholders.

ESG factors are integrated into our investment decision-making processes as part of our commitment to delivering strong, long-term returns for our clients. Our Responsible Investment Policy outlines our commitment to the six UNPRI principles.

The six principles are:

- 1 Incorporate ESG issues into investment analysis and decision-making processes.
- 2 Be active owners and incorporate ESG issues into our ownership policies and practices.
- 3 Seek appropriate disclosure on ESG issues by the entities in which we invest.
- 4 Promote acceptance and implementation of the Principles within the investment industry.
- 5 Work together to enhance our effectiveness in implementing the Principles.
- 6 Report on our activities and progress towards implementing the Principles.

The QIC Responsible Investment Policy is available on the QIC website at: www.qic.com/about-qic/corporate-information/responsible-investment

1 INTRODUCTION

QIC Global Infrastructure (GI) is committed to being a responsible investor. GI believes that the consideration of ESG factors when constructing and managing infrastructure assets can improve the robustness of returns and increase value maximisation for our clients.

This 2018 GI Annual Responsible Investment Report details the practice of integrating ESG factors into the GI investment process and the engagement with the various infrastructure companies that we manage on behalf of our clients. This report sets out key highlights for the 2017 calendar year.

We continue to engage with our portfolio companies, and have seen positive initiatives implemented throughout 2017 in environmental, social and governance areas.

At QIC, we recognise the importance of being able to provide our clients with investment opportunities that create positive social and environmental outcomes alongside attractive financial returns. To this end, we will continue to empower our portfolio companies and influence key stakeholders to deliver on this objective.

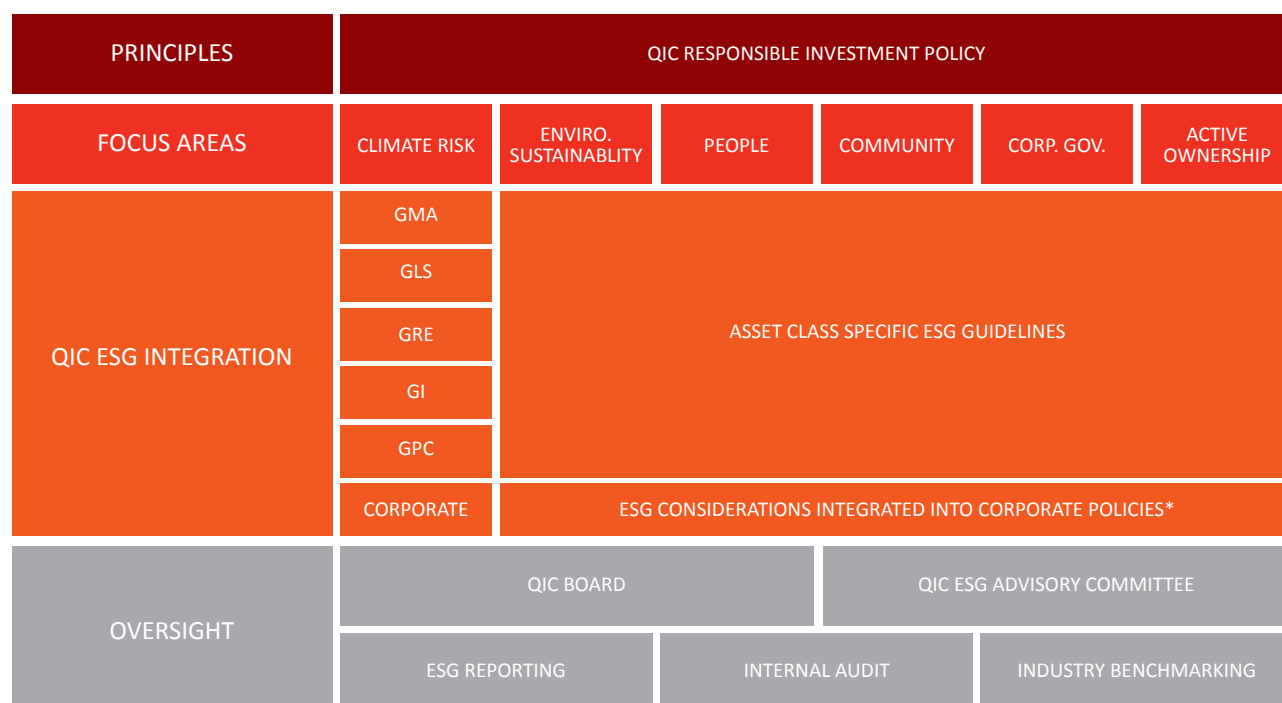
2 | QIC RESPONSIBLE INVESTMENT UPDATE

At QIC, we employ a culture of responsible investment which is driven at the board and executive management level throughout the business. In June 2017, the strategic focus on QIC's ESG program was enhanced with the establishment of an ESG Advisory Committee. This committee is chaired by QIC Board director Stephen Dunne and has business wide representation, including CEO Damien Frawley. The Committee provides advice to the QIC Board on ESG matters and oversight of QIC's overall ESG approach.

Key developments during the year included:

- The QIC RI team goes to two: In September 2017 we welcomed Andrew Saunders to QIC's Responsible Investment team. Andrew comes to QIC from Aurizon and has strong industry experience working in sustainability focussed roles across real assets. Together with Kate Bromley, Head of Responsible Investment, this brings the Responsible Investment team to two. Their task will be to continue to work with the Global Infrastructure team as well as the broader business to implement QIC's ESG strategy.
- QIC's ESG framework: Since July 2017 the QIC Board, in conjunction with the ESG Advisory Committee, has worked to refine and develop QIC's ESG framework and establish a set of key focus areas that represent material ESG considerations for QIC. This will enable us to further define and focus QIC's approach to ESG over time.

Figure 1: QIC ESG Framework



- Understanding climate risk: At the request of the QIC Board, the Responsible Investment team has worked closely with our network of ESG Champions over the past 18 months to advance our understanding of climate risk. This work is ongoing and focusses on building internal capacity to understand and respond to the risks and opportunities associated with climate change.

3 | QIC GLOBAL INFRASTRUCTURE: RESPONSIBLE INVESTING UPDATE

During 2017 we refreshed and updated our Global Infrastructure Responsible Investment Guidelines. These guidelines are available on the QIC website: www.qic.com/about-qic/corporate-information/responsible-investment

Across the portfolio QIC GI asset managers have actively engaged boards of directors and executive management teams to encourage them to incorporate material ESG initiatives and issues into strategic plans and to ensure that ESG risks are assessed and incorporated into risk management frameworks.

Each asset is different and the level and type of contact with the board and executive management of investee companies on ESG matters will vary. Section 5 of this document details a number of examples of engagement with our portfolio companies in 2017.

“Responsible investing is part of our investment culture and beliefs because it makes good business sense. We believe that by investing responsibly we can deliver long term sustainable returns to our clients.”

Leisel Moorhead
Partner, QIC Global Infrastructure
GI ESG Champion



3.1 ESG Reviews

Each year we undertake an annual ESG risk review across all of the assets in the portfolio. This year QIC GI undertook its first detailed and focussed ESG risk review of the Port of Melbourne. This review was undertaken by QIC's Head of Responsible Investment, Kate Bromley, in conjunction with the GI asset management team. This involved a detailed engagement with management to review policies, reporting and understanding of ESG risks. Interestingly what we found is that there were many of the required policies, procedures and adequate reporting in place. Our focus as a result was more on refreshing and providing a different perspective, influencing management to take a more proactive and forward-looking assessment of ESG risks and managing the port's social licence to operate.

3.2 QIC Risk Reviews

QIC undertakes Risk Reviews of assets within its portfolio. These reviews use a multi-disciplined team comprising personnel from QIC's GI team, Risk & Compliance, IT, QIC finance and operations teams to assess risks within the internal structure, controls and processes, finance, treasury, compliance and risk management functions within the relevant business. During 2017, two QIC Risk Reviews were undertaken, one at the Port of Melbourne and the other at Lochard Energy. The QIC Risk Review team prepares a report that goes to the board of the respective portfolio company. This provides an external perspective on risk management, drawing on QIC's own experience and experience from other assets.

3.3 Customer Stewardship National Exemplars

The University of Sydney John Grill Centre – Better Infrastructure Initiative released a policy paper in October 2017¹. This paper identifies that customer led infrastructure is a simple acknowledgement that what customers care about is not the physical infrastructure asset by the services delivered. The Better Infrastructure Initiative identified ten working principles in its Customer Stewardship Framework.

Figure 1: Customer Stewardship framework: ten working principles



Source: Better Infrastructure Initiative, John Grill Centre for Project Leadership

The Better Infrastructure Initiative identified eight industry exemplars who represent what good customer stewardship looks like and how it is being practiced in Australia. We are really pleased that the Port of Brisbane is one of the 2017 Customer Stewardship National Exemplars reflecting the port's consultative development approach and incorporating customer needs into infrastructure design and service delivery.

QIC is also a member of the Expert Reference Group that the John Grill Centre has formed to develop the case for policy reform and cultural change in support of customer led infrastructure.

In particular it is focused on developing a model framework to deliver quality long term customer outcomes for infrastructure.

¹ <https://sydney.edu.au/john-grill-centre/our-research/infrastructure/initiative-publications/why-customer-stewardship-matters.html>

4 | INDUSTRY ENGAGEMENT AND DEVELOPMENTS

QIC is a member of regional and international initiatives to give us guidance and opportunities to collaborate on some of the challenges of ESG implementation. Throughout 2017 we regularly engaged in these forums. There continues to be increased focus and momentum on the importance of responsible investment to the delivery of long term sustainable returns. One of the key developments during 2017 was the release by the Taskforce on Climate Related Financial Disclosures (TCFD) of its recommendations². The TCFD was focussed on the financial impact of the climate related risks and opportunities of an organisation and its recommendations provide a voluntary, consistent disclosure framework that improves the ease of both producing and using climate-related financial disclosures. QIC is having regard to these recommendations in its engagement with its portfolio companies on climate related disclosure.

4.1 PRI Infrastructure Advisory Committee

QIC Global Infrastructure has a representative on the PRI's Infrastructure Advisory Committee (IAC). The PRI has established this advisory committee to oversee the strategy for development of ESG integration in the infrastructure sector. The PRI IAC is made up of representatives from UN PRI signatory organisations. This PRI IAC has worked on developing a primer on Responsible Investment in Infrastructure and template set of DDQs. These items will be discussed at an upcoming Responsible Investment Forum hosted by the UN PRI in Melbourne in February 2018³.

4.2 PRI in Person – Berlin 2017

QIC attended the PRI In Person conference in Berlin. Leisel Moorhead spoke on the infrastructure panel on managing ESG issues in asset management. The PRI In Person conference provided a platform for PRI signatories and other investment professionals to learn, network and collaborate in person on ESG issues impacting investments. Some of our key takeaways from the conference included how “universal owners” are focussed on the delivery of the UN Sustainable Development Goals with the view to delivering long term sustainable economic growth and a stable financial system. Another theme was the focus on “S” within ESG considering the financial impacts of social disruption and upheaval caused by mass migration, the impact on the labour force from technology disruption and increasing income inequality.

4.3 IGCC Summit – Melbourne 2017

The QIC Responsible Investment team attended the Investor Group on Climate Change Summit in Melbourne in October 2017. Kate Bromley participated on a panel on the physical impacts of climate risk to real assets. Key takeaways from this conference were the increasing recognition among super fund trustees that climate change represents a material financial risk and the need for undertaking scenario analysis based on the TCFD framework.

4.4 Women in Infrastructure – London 2017

Matina Papathanasiou, Deputy Head of Global Infrastructure attended and spoke at the Women in Infrastructure Forum in London in November 2017. QIC is committed to increasing diversity and promoting inclusion. Building a diverse organisation is a critical business issue, reflecting our performance aspirations and driving our vision. QIC seeks to ensure that we have diversity across the investment team and we actively work with the management teams of the portfolio assets to promote awareness of the benefits of diversity and strategies and initiatives to improve diversity.

²<https://www.fsb-tcf.org/>

³<https://www.unpri.org/download?ac=4141>

4.5 Sustainable Development Goals: Making a Positive Impact Through Responsible Investment



The United Nation Sustainable Development Goals (SDG's) came into force in 2016. The 17 SDGs aim to address some of the world's biggest environmental and social challenges. Each goal has a specific target to be achieved over the next 15 years.

As a responsible investor in infrastructure assets we are exploring how we can work with our portfolio companies to ensure that they can be aligned with and contribute to the delivery of the SDGs. We see that investors in infrastructure are well positioned because infrastructure assets provide essential services to a community and drive economic productivity and growth.

"Infrastructure investors are well positioned to make a positive impact on the societies and economies in which they invest. Infrastructure assets provide wider social and economic benefits and are key enablers of any economy."

Matina Papathanasiou
Deputy Head of QIC Global Infrastructure



As a long term investor, long term economic growth is fundamental to driving long term sustainable returns. Environmental issues (climate change, resource scarcity and social challenges (income inequality, human rights)) can have financial implications over the long term which could impact economic growth. The SDGs can provide a risk tool for investors to manage these emerging risks.

QIC understands to meet some of these longer term challenges, responsible investors will need to consider not only how ESG risks and opportunities influence the risk-return profile of an investment portfolio, but also how those portfolio investments can contribute to broader societal objectives as expressed through the SDGs. The SDGs can help by drawing attention to the risks associated with unsustainable practices, and providing a common framework for referencing contributions to a more sustainable world. By way of example:



Improve water quality by reducing pollution, substantially increase water use efficiency

QIC asset managers work with the companies to develop initiatives to reduce potable water usage which is aligned with this SDG 6.

Brisbane Airport has implemented a number of initiatives to reduce water usage such as harvesting rainwater from its parking facilities and using recycled water in cooling towers and for irrigation of its green footprint.



Increase share of renewable energy in the energy mix, including the rate of improvement of energy efficiency

QIC asset managers work with the companies to develop initiatives to increase renewable energy and improve energy efficiency which is aligned with SDG 7.

QIC has a large exposure to renewables in the Powering Australia Renewable Fund. One of the assets in that fund is the Silverton Wind Farm which is expected to be constructed by mid-2018 will have an output equal to powering 137,000 houses.

Brisbane Airport has invested \$11m in Solar PV panels which once built will reduce carbon emissions at the airport by 8,000 tonnes per year.

Westlink M7 and CampusParc have investment in energy efficient lighting to reduce energy consumption from their operations.

4.5 Sustainable Development Goals: Making a Positive Impact Through Responsible Investment (Continued)



Build sustainable and resilient infrastructure and foster innovation

QIC GI, with its inhouse technology expert Tibor Schwartz actively works with each of the portfolio companies to explore the use of technology to reduce costs, improve operations or improve customer service.



Improving road safety and providing accessible and safe transport systems

Westlink M7 and Port of Brisbane are actively engaging with key stakeholders to reduce the road traffic incident rate on the motorways that they manage.

QIC GI has engaged with Powerco, Epic Energy and Lochard Energy to explore technology that could improve the safety of their workforces when engaged in driving activities.



Take urgent action to combat climate change and its impacts

QIC GI asset managers have actively engaged with each of the assets in their portfolio on their preparedness for managing climate risks. This is especially important as communities and the economy are reliant on the services that infrastructure assets provide.

5 | ASSET MANAGEMENT

ESG considerations are integrated within our asset management process. GI undertakes an annual ESG performance assessment for each of the assets in its portfolio and this informs the key ESG focus areas for the following year. Through board representation, GI seeks to influence the establishment of appropriate ESG policies and reporting for the portfolio company in which we have invested. We then seek to ensure that material ESG risks and opportunities are incorporated into business strategy and material investment decisions.

We have selected a number of examples of our active engagement on ESG matters during 2017. These are:

- A Focus on Safety: Lochard Energy
- Governance: Modernisation of shareholder agreements
- Environment: Active engagement when incidents occur

5.1 A Focus on Safety: Lochard Energy

QIC, on behalf of its clients, established Lochard Energy in 2015 to facilitate the purchase of the Iona Gas Plant from EnergyAustralia. Lochard Energy owns and operates the Iona Gas Plant and the associated facilities located near Port Campbell in the State of Victoria, Australia.

Following QIC's successful acquisition, Lochard Energy is the largest independent provider of gas storage to the East Coast gas market and also provides natural gas processing and compression services. Lochard Energy now exists as a standalone business, complete with an experienced Board and management team.

Whilst the Iona Gas Plant has had a good health and safety record over its 18 years of operations, the business has been on a journey in regards to safety improvement over the last 2 years, following QIC's acquisition in 2015.

“Workplace health and safety involves the assessment and mitigation of risks that may impact the health, safety and welfare of those in a workplace. Safety is no accident.”

Ross Israel
Head of QIC Global Infrastructure
and Director Lochard Energy



At QIC Global Infrastructure, we have a strong focus on workplace health and safety as works in and around infrastructure assets are often operating in high risk environments. Our focus is to ensure that the asset investments we manage have good safety systems and practices in line with industry best practice.

For Lochard Energy the safety journey began in 2016 when the board (which contains QIC representatives) and management team set a corporate KPI for Lochard Energy to conduct an external review of process safety plans and risk management processes. This review was completed in July 2016 and provided a number of recommendations.

In August 2016, the Lochard Energy management team set up a program called Project SafeX to build on and deliver the actions coming out of this review. Key areas of focus include updating critical safety documentation, addressing plant complexity and design issues, and improving staff training programs and competencies. The delivery of these actions was incorporated into the personal KPIs of key management personnel. Together with a number of operational and system improvements, one of the main reporting improvements of Project SafeX was the development of a more concise and effective Health, Safety & Environment (HSE) Dashboard that is now included and discussed in all Board meetings.

Following the establishment of Project SafeX, in July 2017, Lochard Energy also undertook a HSE deep-dive to develop an FY18 action plan. Part of this action plan was to focus on improving the safety culture by way of the implementation of a safety behavioural program, with the aim to identify and avoid behaviours that may increase the risk of an incident.

These are just a few examples of how the board and management have improved the safety culture at Lochard Energy. It demonstrates how QIC's active asset management approach, in conjunction with Boards and management, are focussed on ensuring improvements in the performance of portfolio companies on key ESG matters such as health and safety. QIC Board representatives and asset managers work closely with the portfolio company management teams to ensure that these ESG matters are factored into strategic planning and to ensure that alignment is created through Key Performance Indicators (KPIs) set to ensure that management is incentivised to deliver required outcomes.

Safety is a never ending journey for all companies. Lochard Energy is well progressed in its journey to deliver continuous safety improvements for its workforce.

5.2 A Focus on Safety: Safety Culture

The Board of each of the companies is ultimately responsible for ensuring that appropriate WHS systems are in place. Through QIC's annual ESG review we also check to ensure that reporting on safety performance is in place and that corporate KPIs are set to include a focus on safety. Two recent safety reviews demonstrated that having systems, reporting and KPIs in place are not the only way to achieve a positive safety culture.

Powerco Safety Review

DuPont recently reviewed Powerco's safety performance and assessed it as good overall, and at least in line with global peer averages.

What was interesting from this review was how well policies and procedures flow through to practice in the field (answer: not as well as we would like).

KEY TAKEAWAYS TO THINK ABOUT FOR OTHER ASSETS:

There is usually a lot of focus on having a well-documented system, processes and policies, but are the relevant documents sufficiently user-friendly to become embedded as work practices in the field? How is this being tested?

Is there a (reasonably) common understanding of degree of risk? In the Powerco case, DuPont found that almost everyone understood that safety is the #1 priority and that stopping work is the right thing to do if there are safety risks – but there was evidence of some materially disparate views on what constitutes a risk.

How well are the lessons learned from incidents and near misses communicated back to all levels of the organisation?

Port of Brisbane Board Workshop – Safety Interactions

A representative from DuPont conducted a workshop on Board members (and asset managers) undertaking safety observations. It reinforced that it is very important for safety culture that board members and senior executive management get out and engage and interact with employees on safety.

KEY TAKEAWAYS

Don't undertake a safety interaction/observation with a checklist – it will become about compliance rather than understanding safety culture.

Don't talk about rules and compliance – but rather share your own story about why safety is important to you.

Share safety stories – it is easier for people to connect and open up through a story.

Don't be afraid to admit that you are not the expert on safety in the area that you are observing – allow the person to talk to their expertise.

As a part of the GI asset management process, these lessons and takeaways are shared across the team. We are seeking to ensure that other asset managers across sectors share in these learnings and apply them to the assets that they manage.

5.3 Governance: Modernisation of Shareholder Agreements

Shareholder agreements provide a fundamental governance framework for private companies. These important agreements are put in place at the time of the acquisition and whilst they reflect the market practice of the day and the peculiarities of the circumstances of the deal – most aren't designed to keep pace with changes. Over time market developments, shareholder dynamics and the circumstances of a company do change. This means that a shareholder agreement can become out of date and therefore need to be modernised to ensure that it continues to provide an appropriate governance framework.

Modernising a shareholder agreement is not an easy task. All shareholders must typically agree and every party takes the opportunity to bring their wish list to the table. This may be further complicated by the presence of strategic or foundation investors, who may hold additional rights relative to other investors. QIC has considerable experience in negotiating shareholder agreements and has undertaken this type of modernisation project a number of times across assets in its portfolio.

During 2017, QIC drove the modernisation of the shareholder agreement for Brisbane Airport which was over 20 years old, a function of privatisation in 1997, when the infrastructure investment market was still in its infancy. This was a significant project requiring QIC to work closely with all shareholders (11 in total) and their advisers and consulting with the Board and management as required.

The aim was to modernise the governance terms to create a more flexible and market based framework. This included amongst other things an improved conflicts regime, revision of board appointment rights to reflect the shareholders' ownership levels, introduction of an independent Chairperson, clearer information rights for shareholders, significant improvement to the mechanics of the pre-emptive regime, enhancing the Board's ability to increase the size and frequency of dividend payments, addition of a dispute resolution mechanism, and increased flexibility for shareholders to manage their holding structure and a modernised list of shareholder reserved matters balanced with the desire to maintain sufficient flexibility for board decision making.

The result will be a modern shareholder agreement, providing Brisbane Airport with a best practice corporate governance framework and which will significantly enhance value to all shareholders.

"The shareholder agreement is essential to establishing a good corporate governance framework for an investment. Providing protections for investors (minority and majority), articulating the role of the board and setting out the basis for important decision making are just some of the reasons why we see the shareholder agreement as an important element of any investment."

Michael Angelini
Head of Legal
QIC Global Infrastructure



5.4 Environment: Active Engagement When an Incident Occurs

Thames Water is a regulated asset which provides essential services such as water and waste water. Like most regulated assets in developed countries, Thames Water has detailed systems and processes to manage many and varied, complex environmental risks. However, unfortunately sometimes incidents can and will occur which impact the company's ability to provide services to its customers and can adversely impact a company's reputation. How a company seeks to prevent such incidents and how it responds is important for a company's social licence to operate.

As a responsible investor, QIC through its active asset management will always seek to ensure that the appropriate risk systems and operational processes are in place. But when an incident occurs – that's when it's most important to engage directly with the company to ensure that we as investors have a detailed understanding of what occurred and why and what action is being taken to prevent an event happening again.

During 2017 there were two high profile incidents at Thames Water:

- Thames Water received a fine of £19.75 million from the UK water regulator, a record in the UK, relating to environmental pollution incidents at 6 facilities in the Thames Valley (out of its 355 sewage treatment works) during 2012-2014.
- Thames Water missed its leakage reduction targets by 47m litres per day in 2016-2017 – and incurred a fine of £8.5million. Although this was the first time that the company had missed its leakage targets in 11 years and although it had reduced leakage by a third from its peak in 2004, it led the regulator to open an investigation into the company's activities in June 2017.

Outside of the broader environmental and social responsibility that Thames Water has, these types of incidents have material cost implications in terms of investment required in people, systems and operational practices to address the issues that contributed to these incidences. In addition, there is the material reputational impact on Thames Water of these incidences.

What can investors do in these circumstances? Although a minority investor in the Thames Water investment, QIC actively participated in the Board's governance through representation on the regulatory entity Board as well as the shareholder Board's via Joint Director Agreements. In particular, to better understand the events which led to these disappointing outcomes, and the plans to ensure improved performance going forward, QIC was involved in establishing a number of active shareholder initiatives during calendar 2017:

- **Shareholder working group:** A shareholder working group was established in early 2017 which undertook to arrange a series of meetings with key executives in the water and waste business. In total there were over 30 hours of one-on-one management meetings with a number of executives with responsibility across key business lines. The scope of these meetings was analysis the current and future performance related to pollution incidents (within the Waste division) as well as leakage (within the Water division). The focus of these sessions was to better understand the KPIs related to these adverse events as well as the performance measures and practices being put in place to improve performance and mitigate the risk of these incidents occurring in the future.
- **Site Visits:** QIC attended two separate site visits during 2017. One of these was a full day visit to one of the key sewerage site implicated by the pollution fines levied back to the period of 2012-2014. During this visit we met local site management, explored the end-to-end operational process at the plant and also met local community stakeholders affected by the pollution incident (local fisheries and conservation association members). The outcome of the visit included a better knowledge

“Managing ESG risks involves active and regular engagement with all stakeholders. We all play a critical role in ensuring systems and processes are in place to promote environmental and social responsibility. I attended personally one of the sites of these incidences – engaging with staff and key local stakeholders to gain a deeper understanding of actions being taken to prevent them happening again.”

Giles Tucker
Partner
QIC Global Infrastructure



5.4 Environment: Active Engagement When an Incident Occurs (Continued)

and appreciation of the site's operations and a more informed approach and understanding of the key questions and challenges to be put to the Board related to these operational areas. The second site visit was to the Abbey Mills Pumping Station which plays a central and key role in the London sewerage system responsible for pumping waste to the treatment works at Beckton. Beckton is one of Europe's largest sewerage treatment works, treating wastewater from 3.4 million Londoners. The site visit included a physical inspection of one of the actual sewer tunnels to convey the sense and scale of the underground network that Thames is responsible for and the type of operational challenges that it faces to ensure the sewers remain 'unblocked' and the waste effectively transported for treatment.

As well as highlighting the importance to management of key areas such as pollution and leakage to investors, the aim of such shareholder led initiatives is to better inform shareholders regarding key operational risks which in turn should promote a better quality of dialogue and challenge at the board level.

6 | CONCLUSION

Responsible Investment and management of ESG factors continues to develop and evolve in terms of understanding the value that it can bring to investment portfolios as well as growing community expectations on businesses and the role it plays in its contribution to society. We expect that these trends will continue to gain momentum and be a key focus for the business going forward. Whilst 2017 has been an active year across our portfolio, we fully expect to build upon our Responsible Investment initiatives further in 2018 to provide improved infrastructure services to all our stakeholders.

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