Australian Government

NAIF

Northern Australia Infrastructure Facility

# Environmental and Social Review of Transactions Policy

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# 1. Overview

The Northern Australia Infrastructure Facility (**NAIF**)'s function is to provide financial assistance in relation to the development of *northern Australia economic infrastructure* as defined in the *Northern Australian Infrastructure Facility Act 2016* (**NAIF Act**).

This Environmental and Social Review of Transactions Policy (**Policy**) applies to all requests for finance considered by the NAIF. This Policy provides a framework to guide the NAIF Executive in assisting the Board in making Investment Decisions and the Board in discharging its functions in each case in relation to assessment of a proposed Project's relevant environmental and social and related Project governance risks (**ESG** and **ESG Risks**). Governance in this context refers to a Project Proponent's policies, management systems and resources that it has in place to manage environmental and social risks.

This Policy operates alongside related NAIF policies, such as the NAIF Risk Management Framework, Anti-Corruption Policy, Fraud Control Policy, and the Public Benefit Guideline and Indigenous Engagement Strategy Guideline.

Environmental, social and governance issues relevant to NAIF's own organisation are addressed in separate policies.[1]

# 2. Definitions

Definitions in the NAIF Act and the Northern Australia Infrastructure Facility Investment Mandate Direction 2018 (**Investment Mandate**) apply.

# 3. Background

## 3.1 NAIF Context

NAIF applies this Policy in the context of its overarching statutory functions and purpose. There are a number of unique features of NAIF as a government entity which inform the NAIF and its Board in the discharge of its functions. They are set out in the NAIF Act or Investment Mandate and include the following.

- NAIF is a corporate Commonwealth entity established by the NAIF Act. The NAIF Board is responsible for deciding, within the scope of the NAIF Act and Investment Mandate, the strategies and policies to be followed by NAIF and to ensure the proper, efficient and effective performance of NAIF's functions.[2]
- NAIF was established to assist in addressing financing market gaps for the construction of infrastructure to develop northern Australia. Traditionally this has been a function of government in relation to infrastructure development more broadly.
- NAIF does not itself finance projects. It assesses projects to determine whether or not financing for the project should be advanced (effectively making a decision that NAIF financial assistance should be offered or not offered (an Investment Decision)).
- The NAIF financial assistance is provided by the Commonwealth and the actual lender of record is the northern Australia jurisdiction(s) (Queensland, Western Australia or the Northern Territory) where the project is located.[3] Commonwealth moneys are contributed through the relevant jurisdiction to the project borrower under a framework agreed in a Master Facility Agreement entered into between the Commonwealth, NAIF and each jurisdiction.
- The NAIF Act and Investment Mandate incorporate a significant number of requirements which NAIF must comply with and also a number of matters which it must have regard to or be satisfied as to in making Investment Decisions ('NAIF Requirements').

[1] For example, NAIF Code of Conduct

[2] NAIF Act Section 14(1)

[3] Investment Mandate Section13(2)

- The Investment Mandate requires NAIF to develop a Risk Appetite Statement (RAS) to guide its Investment Decisions, in consultation with the responsible Minister and the relevant northern Australia jurisdictions.
- The RAS must align with Commonwealth Government policy: the Investment Mandate specifies that the RAS is to be reviewed annually to address emerging risks, changes to existing risks and changes to that Commonwealth Government policy.[4] Consistent with this NAIF cannot bias NAIF financial assistance to one industry or another outside of the guidance contained in the NAIF Requirements.
- NAIF also functions within an environment of extensive prescribed consultation with the relevant jurisdictions as well as Infrastructure Australia and as appropriate with other government stakeholders including Commonwealth departments.[5]
- NAIF makes Investment Decisions independently but those decisions are able to be vetoed by the relevant jurisdiction on any ground and by the responsible Minister on the grounds that the decision would be inconsistent with the objectives and policies of the Commonwealth Government or have adverse implications for Australia's national or domestic security or its international reputation or foreign relations.[6]

## 3.2 Reputation and NAIF Corporate Governance

The NAIF Investment Mandate includes the following provisions:

- **Section 16 Reputation**: NAIF '*must not act in a way that is likely to cause damage to the Commonwealth's reputation, or that of a relevant State or Territory government*'.[7]

  Assuming that NAIF:

  (a) undertakes appropriate due diligence on projects including as to ESG Risks as contemplated in this Policy; and

  (b) consults with government as appropriate;

  in compliance with the NAIF Requirements NAIF will regard itself as having satisfied Section 16 noting that the Commonwealth or the relevant jurisdiction is able if it chooses to exercise its veto rights.

- **Section 17 Corporate governance**: In performing its functions, NAIF must have regard to Australian best practice government governance principles and Australian best practice corporate governance for Commercial Financiers including developing and annually reviewing policies with regard to environmental, social and governance issues.[8]

  NAIF staff will actively seek out opportunities with relevant industry bodies, peak bodies, relevant government entities and Commercial Financiers to develop insight into trends in relation to ESG Risk issues relevant to NAIF's statutory mandate.

# 4. Approach to Risk Assessment

In undertaking its due diligence for any Investment Decision NAIF analyses a broad spectrum of relevant risks. This will include identification of material ESG Risks and opportunities. This analysis partly overlaps with and helps inform the NAIF public benefit assessment undertaken (refer to the NAIF Public Benefit Guideline) under which both beneficial and adverse environmental and social externalities of the Project are included in the assessment.

- In line with industry practice, the nature and extent of due diligence is tailored to reflect the inherent level of risk associated with an Investment Proposal. Factors that NAIF will consider in scoping its review include the: type of environmental and social assessment required under Commonwealth, State or Territory laws;
- the size and complexity of the project; and
- the Project's relationship to any associated developments.

Some NAIF transactions will only require a short desktop review while others will require detailed risk evaluation.

[4] Investment Mandate Section 12 (4)

[5] Investment Mandate Section 14

[6] Investment Mandate Section 13(1) – (5) and 14, NAIF Act Section 11(4)

[7] Investment Mandate Section 16

[8] Investment Mandate Section 17

NAIF’s risk assessment will include assessment of how the Project Proponent will manage, mitigate or avoid material ESG Risk impacts. The reasonableness and likely effectiveness of the Project Proponent's intended mitigation strategy in respect of ESG Risks (including the role of third parties such as contractors or insurers) will be assessed.

NAIF implements a staged process with the level of analysis increasing as an Investment Proposal proceeds through the NAIF application and approval process.

During the preliminary assessment stage for a Project, potential ESG Risks associated with the location, nature and scope of the Project may begin to be identified. The NAIF application and approval process then involves a high level strategic assessment stage and a later more comprehensive due diligence process.

In undertaking its due diligence, NAIF has the opportunity to request detailed information from the Project Proponent and its contracting parties. NAIF will undertake its own analysis using internal resources and, if it requires, seek expert advice relevant to the nature and magnitude of a Project Proponent’s Investment Proposal’s ESG Risks and impacts. Consultation as appropriate with government bodies with special expertise relevant to a Project, including the Commonwealth Department of the Environment and Energy may be undertaken.

# 5. ESG Policy Approach

NAIF‘s approach to analysing ESG Risks in undertaking its due diligence for the purpose of the NAIF Board making an Investment Decision is as follows. The actual due diligence undertaken will be determined on a case by case basis in line with Section 4 and as relevant to the particular Project and proposed financing arrangements.

## 5.1 Regulatory approvals

Under Section 15 of the Investment Mandate the NAIF Board has a discretion to make an Investment Decision prior to a Project obtaining all relevant regulatory, environmental and Native Title approvals as required by the relevant jurisdiction. It will be a condition precedent to the making available of financial assistance to a Project Proponent that NAIF is satisfied that the approvals have been obtained on acceptable conditions.

The requirements of Section 17 of the Investment Mandate are additive to the Section 15 obligations.

## 5.2 Capacity to comply

- NAIF will satisfy itself that there are reasonable bases to conclude that a Project Proponent will be in a position to comply with laws and permits that pertain to regulatory ESG Risk issues and as to a Project Proponent’s capacity to manage material ESG Risks impacting the Project and its financing obligations.
- NAIF will consider the nature and scope of relevant State, Territory and Commonwealth assessment and approval processes. NAIF will examine the regulatory environment within which an Investment Proposal is put forward and matters taken into account in determining to grant the approvals (for example assessment of whether the Proponent is a fit and proper person) and conditions attaching to approvals.
- The grant of approvals will not necessarily be determinative in NAIF satisfying itself of the suitability of the Project Proponent to receive financial assistance and its capacity to meet the various obligations imposed on it under the finance documentation.
- NAIF will investigate the Project Proponent’s systems, plans, policies and procedures for managing its oversight of and compliance with relevant regulatory standards and financing obligations.
- A Project Proponent's track record of compliance with relevant ESG regulatory requirements, both within Australia and where relevant abroad, will be considered including the Project Proponent’s response to any non-compliance or incidents. Historical non-compliance will not necessarily rule out a favourable Investment Decision, although a pattern of non-compliance suggesting a lack of regard for regulatory requirements will be considered. The track record of other related entities or executives in the Proponent’s corporate group may be assessed to the extent NAIF determines it to be relevant.
- Where a Project is likely to involve significant rehabilitation costs (including at end-of-life), the robustness of the Project Proponent’s financial provisioning for these rehabilitation costs will be reviewed.
- This section also applies to matters referred to in Section 5.3 and 5.4.

## 5.3 Assessment of climate related ESG Risks

- NAIF will appropriately consider the likelihood of the occurrence of, potential impacts of and key mitigants for, climate related ESG Risks and opportunities on the Project Proponent's business and the NAIF financial assistance specifically related to physical, transitional and liability impacts.
- Physical impacts may include for example the impact of coastal inundation, changes in weather patterns and increased extreme weather events. This risk assessment will take into account that the Investment Mandate provides that NAIF's RAS may have a high tolerance for factors that are unique to investing in Northern Australia Economic Infrastructure including northern Australia's climate.[9]
- NAIF will consider, where this is material, and form a reasonable view as to the likely trajectory of changes in regulation, technological innovation, changing sources of supply and demand for a Project's products or services and changes in revenue and costs in relation to a particular Project ESG Risk.
- Liability risks to be considered will be known or identified potential claims against the Project Proponent, or other Project parties in relation to losses suffered by third parties from the effects of climate change.
- NAIF will seek information on the Project Proponent organisation's awareness of climate related risks, the governance its organisation has around those risks, its understanding of how climate risks impact its business, and the resilience of the business strategy for managing these risks. This may be relevant at the Proponent's board or management level or through understanding key contracting parties. This may include assessment of the background experience and expertise of relevant personnel or entities.
- NAIF will assess the relevant risks in the context of the appropriate tenor and other terms for any NAIF financial assistance. This includes the potential impact of those risks on the ability of the Project Proponent to satisfy the NAIF Act and Investment Mandate requirements particularly the requirement for NAIF to have an expectation for the loan to be repaid and the ability of the Project Proponent to meet its obligations under the finance documentation.
- For that purpose, as part of its due diligence NAIF will sensitise key financial modelling assumptions under various plausible scenarios to test a range of assumptions in relation to the Project including relevant climate related ESG Risk factors. The development of scenarios may involve expert advice.

## 5.4 Assessment of Social issues

- In relation to social issues these will be assessed as appropriate for the particular Project to assess whether the Project has identified and developed responses to any reasonably foreseeable social impacts directly related to the Project.
- Projects must comply with all Australian laws.
- Project Proponents will be required to provide full disclosure about any instances of poor corporate governance, encompassing corruption, bribery, human rights abuse or damage in World Heritage Sites and other high value conservation areas of the Proponent or any associated entity at any location within the last ten years.
- For certain High Risk ESG sectors to be identified by NAIF in its RAS the Proponent will also be required to disclose to NAIF the risk of modern day slavery in its Project supply chain risk management assessment.
- NAIF will look to confirm that the Project Proponent has undertaken reasonable stakeholder consultation. NAIF will also expect to see appropriate management of social issues, including commitment to ongoing stakeholder consultation and complaints handling during construction and operation.

## 5.5 Contractual commitments

- Investment Decisions will be subject to suitable contractual commitments under the finance documentation to provide NAIF with comfort as to the Project Proponent's ongoing management of ESG Risks. For example:
  - **Covenants to comply**
    NAIF will require contractual covenants from the Project Proponent to comply with Project approvals and other applicable regulatory requirements and risk management plans, and to report to NAIF on material ESG Risk management compliance and incidents.

[9] Investment Mandate Section 12(3)

- **Covenants to meet benchmarks**
  The ESG Risk impacts of a Project will depend on the manner in which infrastructure is constructed and operated. In circumstances where risk mitigation strategies are identified by the Project Proponent to avoid unacceptable impacts, NAIF will generally require contractual commitments to implement these mitigation strategies and meet appropriate associated benchmarks.

- **Covenants as to transparency**
  NAIF recognises that transparency as to ESG Risk impacts is demanded of Project Proponents through domestic legislation dealing with State and Territory pollution incident reporting requirements, the National Pollutant Inventory, the National Greenhouse and Energy Reporting Scheme, and others, as well as the conditions of approvals issued in respect of a particular Project.

# 6. Review and Approval

The NAIF Board is responsible for this policy.

This policy is reviewed annually in accordance with the NAIF Act and Investment Mandate but may be reviewed more frequently if required.

The NAIF Board is briefed at least annually on emerging trends in environmental and social and related governance issues in line with the annual review of this Policy by the Board.

Where material changes are made as a result of a review, Staff will be given training on the revised Policy.

# 7. Seeking Assistance

If staff have any queries or need any assistance in relation to their responsibilities under this Policy, they should discuss them with the CEO.