First State Investments

Colonial First State Global Asset Management

Responsible investment report

2009 calendar year

Contents

About Colonial First State Global Asset Management

Colonial First State Global Asset Management (CFSGAM) is the consolidated asset management division of the Commonwealth Bank of Australia. We are committed to delivering quality investment solutions which enhance the wealth of our investors. Entities within CFSGAM provide asset and investment management services to institutional and wholesale investors, as well as retail investors.

References to CFSGAM in this report include references to entities which manage or own assets of various types, depending on circumstances.

CFSGAM is one of the largest Australian-based investment managers, with a growing presence in selected international markets. Our specialist investment teams manage portfolios across a diverse range of asset classes, including Australian equities, global equities, global emerging markets, global resources, global property securities, global listed infrastructure securities, global fixed interest and credit, short-term investments, direct property and infrastructure investments.

Our approach to investment is driven by a commitment to providing the best possible outcomes over the long term for our investors. To achieve this, we ensure our interests are aligned with our investors and uphold a culture of always acting in our clients' best interests. CFSGAM became a signatory to the PRI on 1 March 2007, and has embedded responsible investment processes within each asset class and in investment teams where investments are managed. CFSGAM defines responsible investment as investment decision making which gives full consideration to ESG issues.

CFSGAM key features

- Distribution capabilities throughout Australia, New Zealand and Japan via CFSGAM and operating in Asia, Europe, the UK and the Middle East as First State Investments.
- A$149 billion in funds under management as at 31 December 2009.
- Guided by the expertise of more than 200 investment professionals around the world.
- Strong risk management and compliance framework, designed to meet or exceed required standards of governance as mandated by legislation.
- Signatory to the UN Principles for Responsible Investment since March 2007 with a dedicated Sustainability and Responsible Investment team.

Letter from the Chief Executive Officer

Welcome to CFSGAM's third annual responsible investment report. This report is for the 2009 calendar year, which was one of the most challenging and volatile periods for global financial markets in recent times.

The unprecedented conditions we experienced were partly the consequence of a long period of deteriorating standards of corporate governance, an imprudent approach to risk and conflicting priorities between companies and their stakeholders. As some of the dust settles it is clear that our industry needs to get back to basics and refocus on its fiduciary role.

The United Nations Principles for Responsible Investment (PRI) provide a framework for us to consider environmental, social and governance (ESG) issues across our own business and in companies in which we invest. The proper consideration and integration of ESG issues into our investment process will enable us to be a fiduciary and make decisions in the best interests of our investors.

There was a great deal of uncertainty during 2009 and we had to rapidly adjust to unprecedented conditions. With so many difficult and pressing issues to deal with, it was a stern test of the industry's commitment towards sustainability and responsible investment.

To engage our people on this issue we held a staff debate on whether sustainability and responsible investment were relevant during the financial crisis, or whether our energies should be focused elsewhere. Issues such as the materiality of ESG issues, the ability to quantify ESG measures and availability of evidence to support ESG considerations were all discussed. These are important issues for our industry and it was valuable to openly discuss them.

It was a pleasing outcome that attendees were 100% behind our ongoing commitment to sustainability and responsible investment. I believe ESG issues are now more relevant than ever for our industry and we are witnessing a renewed focus from investors on ESG performance.

With a long track record in responsible investment, CFSGAM is well positioned to service and respond to clients' needs in this new environment. CFSGAM is proud of its track record in the consideration of ESG issues and was amongst the first Australian investment managers to become a signatory to the PRI in early 2007. CFSGAM was the first Australian investment manager to release a detailed report on its progress of PRI implementation, now in its third year.

After having taken a back seat for many years, social issues came to the fore in 2009. People lamented the moral bankruptcy in the financial services sector, while investors' patience ran out with executive largesse and poor corporate behaviour at their expense.

More usually associated with polluting industries or large infrastructure operations, a social licence to operate became a front-of-mind issue for all listed companies, from childcare centres through to high street banks. As reputations were shattered and investor trust was lost, a social licence to operate was no longer a given. Rather, it was something that had to be earned by assuring a sceptical public that there was a genuine desire and commitment to have a positive impact on society.

Despite the turmoil taking place in financial markets, environmental issues remained high on the agenda, especially with the Copenhagen climate summit taking place towards the end of 2009. While there was much anticipation leading up to the summit, reactions to the outcomes were mixed.

Some viewed the Copenhagen summit as a diplomatic failure, while others viewed the incremental improvement as a great step forward. Despite these stark differences in opinion, there was a shared eagerness felt across the financial services industry for international agreement to be reached swiftly. Even in the absence of a treaty, governments representing 80% of global emissions committed to reducing emissions, giving a clear sense of direction towards a new, clean-energy economy. The long-term nature of the investment management industry requires certainty and commitment from policymakers and government.

Consideration and integration of environmental issues in the investment process remains a long-term focus for CFSGAM and we are committed to demonstrating leadership in this area. I attended the UN Investor Summit, which came at an important time for our industry, following the international climate treaty talks in Copenhagen and amid cautious optimism that economic conditions were returning to normal. With representatives of more than $9 trillion of investment, the UN Investor Summit was a valuable opportunity to consider climate risk as an investment issue. A key item on the agenda was to consider the scale and urgency of climate change investment risks and to analyse emerging investment strategies and opportunities in the wake of the Copenhagen summit.

In many ways, addressing the climate change challenge is about making the most efficient use of resources, which is something that is already part of good management practice and fiduciary responsibility. There is still much work to be done and scepticism remains, but this is a real opportunity for the investment industry to demonstrate leadership and make the most of the opportunities presented by a move towards a low carbon economy.

As we reported last year, the limited availability of high-quality ESG research was a stumbling block to implementing the PRI. With this in mind, we are pleased with the progress of ESG Research Australia, whose membership comprises 42 institutions managing over $100 billion in Australian equities, including some of Australia's largest fund managers and superannuation funds.

ESG Research Australia's objective is to increase the quantity, quality and scope of ESG research on Australian companies. Brokers have responded to the demand for ESG research and it is an increasingly important part of the mainstream investment processes. The ESG Research Australia Awards are an important part of encouraging ESG research through recognising excellence in ESG research and service, and CFSGAM was pleased to chair the judging panel and host the inaugural ESG Research Australia Awards presentation night.

CFSGAM's leadership team is passionate about delivering global best practice in our whole-of-business approach to responsible investment. An important development to help realise this goal was the strengthening of our PRI governance by embedding PRI performance into the business's balanced scorecard.

This step means the PRI is now part of CFSGAM's business strategy and is used to measure our own performance and set key performance indicators throughout the business. Our balanced scorecard target is that we will be top quartile across five of the six Principles for responsible investment by the 2011 reporting year.

It is encouraging to see that we are making good progress towards this goal. We achieved ranking improvements in each of the six Principles in 2008 and currently sit in the top quartile in three of the six Principles relative to global investment managers. This progress is especially pleasing considering we had no top quartile rankings in the 2007 survey and the difficult operating conditions we experienced during the period.

Our progress in implementing the PRI across the business is driven by CFSGAM's PRI Steering Committee. I am chair of this committee and am pleased for the opportunity to help shape our responsible investment policy and strategy. I succeeded Neil Cochrane in the role of chair during the year, and I would like to thank Neil for his important contribution to our business's approach to responsible investment and the PRI.

As a consequence of the financial crisis, many investors became disillusioned with the financial services industry. There is much work to be done to repair our industry's reputation and restore the trust of investors. The financial services industry is built on trust and it is at the core of everything we do; without the trust of investors our industry cannot function.

To restore investor confidence, nothing groundbreaking needs to be done. We simply need to focus on the fundamentals of our industry that have taken a back seat for the past decade. With the PRI providing the framework, rebuilding work in the industry has already begun. But it will be a long and challenging process to regain investors' trust while their scepticism is at an all-time high.

We are proud of our progress so far and look forward to working with others in the industry to ensure continuous improvement. CFSGAM remains committed to fulfilling its fiduciary role by providing the best possible outcome for investors through the successful implementation of the PRI.

Mark Lazberger
Chief Executive Officer

Global operations
At 31 December 2009

UK/Europe

FUM A$25.1 billion
Investment staff 49 (186 total)

As at 31 December 2009	A$ billion
Total funds under management	**149.0**
Australian Equities	23.0
Global Equities	42.3
Property Securities	4.7
Listed Infrastructure Securities	0.4
Total equities	**70.4**
Fixed Interest and Credit	24.6
Short term Investments	34.5
Total debt	**59.1**
Listed and Direct Property	17.1
Infrastructure	2.2
Total alternatives	**19.3**

Funds under management shown as source of funds. Figures do not sum due to rounding.

USA

Nil FUM
Investment staff 3 (3 total)

Australia/NZ

FUM A$105.8 billion
Investment staff 159 (975 total)

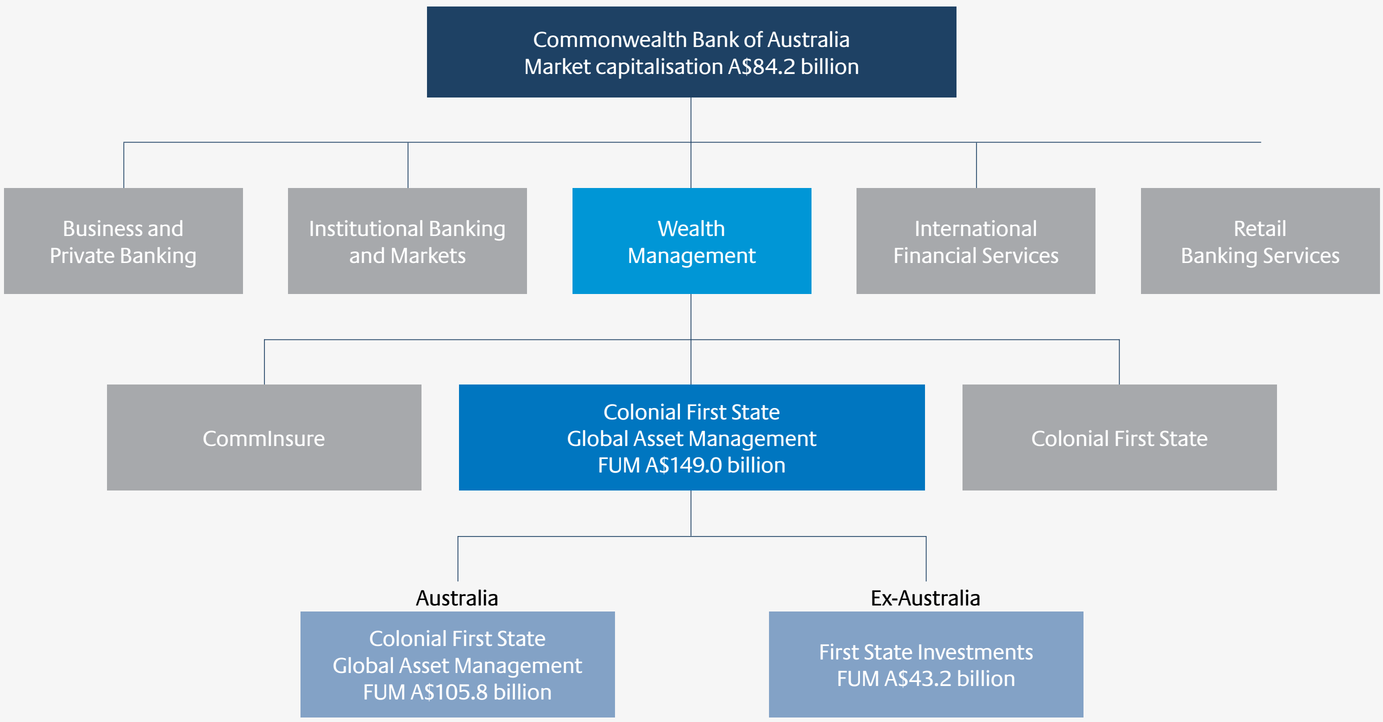
Asia

FUM A$18.1 billion
Investment staff 20 (109 total)

Total global investment staff 231 (1,273 total, including 634 asset management staff listed and direct property).

Ownership structure

At 31 December 2009



Source: Colonial First State Global Asset Management.

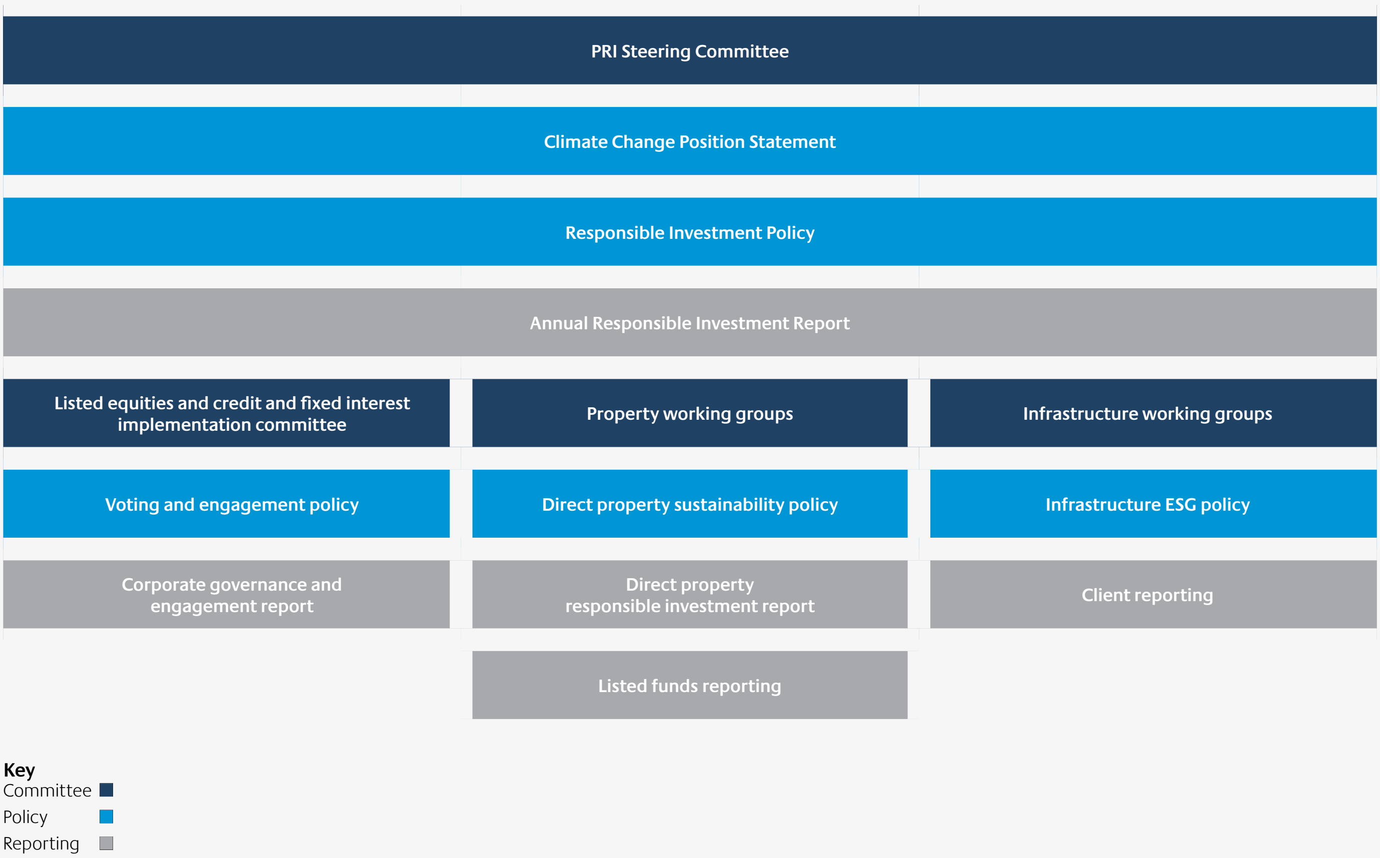
Governance, policy and strategy

Since signing the PRI in March 2007, a governance framework has been established to ensure there is responsibility across CFSGAM for the relevant aspects of the PRI.

A PRI Steering Committee, which is comprised of senior representatives from across the business and chaired by the Chief Executive Officer, is responsible for setting the organisation-wide responsible investment policy and strategy.

Supporting the PRI Steering Committee are sub-committees and working groups that deal with asset-class-specific ESG issues. These sub-committees ensure the tangible work is undertaken to implement the PRI into the different investment strategies across the organisation. Every investment team has a staff member allocated to ESG considerations who spends a notional 10% of their time on responsible investment-related activities. There are also asset-class-specific policies and reporting is undertaken against these policies.

Governance structure



Our approach towards best practice

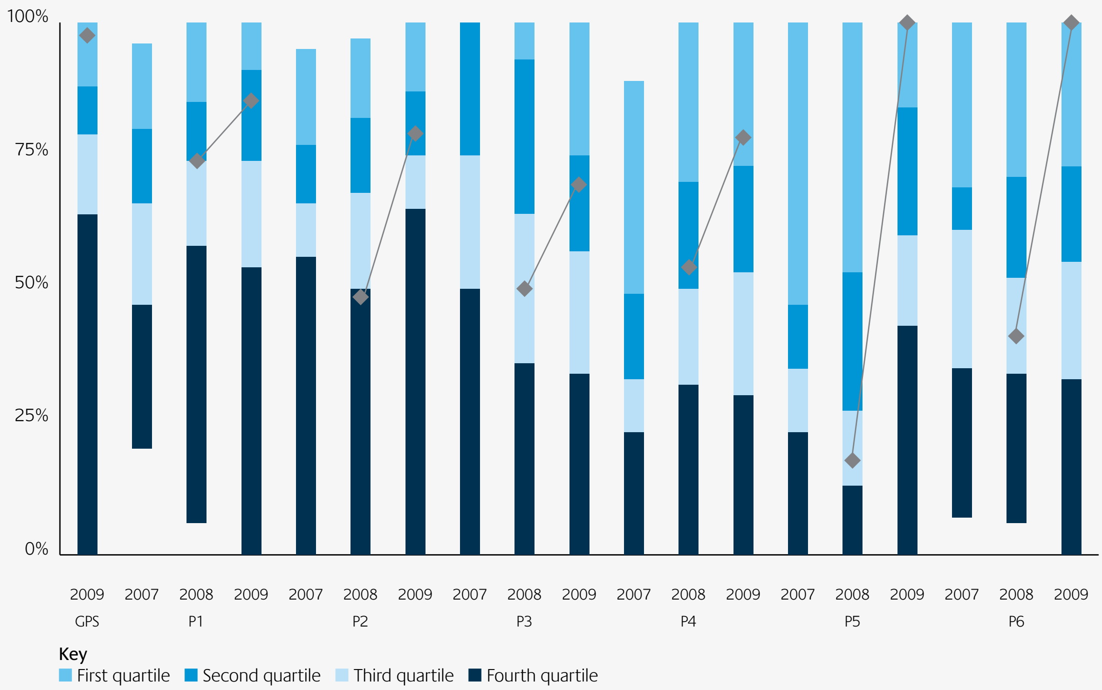
CFSGAM is working towards global best practice in our approach to responsible investment. We believe the best way to measure this is through feedback we receive during the PRI survey process.

In 2009, we strengthened our PRI governance by embedding our objectives into the balanced scorecard for CFSGAM. Our balanced scorecard target is that we will be top quartile across five of the six Principles for responsible investment by the 2011 reporting year.

This effectively means that successful implementation of the PRI is used to measure our own performance and set employee key performance indicators. Relevant areas of the business have specific targets that help the whole business achieve the business-wide target. For example, the Chief Investment Officer has the most influence over Principles 1, 2 and 3 and so is responsible for those, while the distribution and sales functions of the business are responsible for aspects of Principles 4, 5 and 6.

The chart below shows how we are tracking on our objective to date. Note to table: Scores have been calculated based on signatories' self assessment and using the scoring methodology approved by the PRI Assessment Group. Although a limited verification exercise was undertaken with a proportion of signatories, responses have not been independently audited by the PRI Secretariat, PRI Assessment Group, or any other third party. Individual results including comparisons to the overall results (quartiles) are indicative and do not imply an endorsement of signatory activity. While this information is believed to be reliable, no representations or warranties are made as to the accuracy of information presented, and no responsibility or liability can be accepted for any error, omission or inaccuracy in this information.

The chart below shows how we are tracking on our objective to date.



Supporting policies

There are a number of entities within CFSGAM and these entities may have their own responsible investment policies. The responsible investment policies outlined below are publicly available on CFSGAM's website.

Responsible investment policy statement

CFSGAM has had a standalone responsible investment policy statement since 2007. This policy outlines the approach to responsible investment across CFSGAM funds offered globally.

Colonial First State Asset Management (Australia) Limited guidelines and principles for corporate engagement on governance, environment and social issues

This document outlines the guidelines and principles for engagement on governance, environment and social issues as they apply to the funds managed by Colonial First State Asset Management (Australia) Limited (CFSAMAL) ABN 89 114 194 311.

CFS Managed Property Limited and its corporate governance practices – Unlisted funds

CFS Managed Property Limited (CFSMPL) ABN 20 085 313 926 is the Responsible Entity of a number of registered and unregistered managed investment schemes for our property and infrastructure capabilities.

From 30 June 2008, CFSMPL adopted corporate governance disclosures for its unlisted managed investment schemes equivalent to those applicable to Australian Securities Exchange (ASX) listed schemes. Where applicable, we will adhere to the same standards as those outlined in the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations released in August 2007 (2nd Edition).

Climate change position statement

Climate change is an environmental issue that is likely to affect our investments over the long term and is also of a high level of interest to our stakeholders. As an investor, we recognise the need to approach climate change in a rigorous manner, based on a thorough understanding of the risks and opportunities created for the companies we manage and invest in globally. Our Climate change position statement outlines how we will integrate ESG considerations, including climate change, into our investment processes.

Commonwealth Managed Investments Limited and its corporate governance practices – Listed funds

Commonwealth Managed Investments Limited (CMIL) ABN 33 084 098 180 is the Responsible Entity of the listed property funds CFS Retail Property Trust (CFX) ARSN 090 150 280 and the Commonwealth Property Office Fund (CPA) ARSN 086 029 736. CMIL is a wholly owned subsidiary of Commonwealth Bank of Australia ABN 48 123 123 124.

The corporate governance practices of CMIL are in place throughout the reporting period for its listed funds and are fully compliant with the Australian Securities Exchange (ASX) Corporate Governance Council's Principles and Recommendations. CMIL has opted for early adoption of the Revised Corporate Governance Principles. The information available on the CFX and CPA websites is provided in accordance with the second edition of the Principles, released in August 2007.

CMIL corporate governance report, June 2008 – Unlisted funds

From 30 June 2008, CMIL adopted corporate governance disclosures for its unlisted managed investment schemes equivalent to those applicable to Australian Securities Exchange (ASX) listed schemes. Where applicable, we will adhere to the same standards as those outlined in the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations released in August 2007 (2nd Edition).

Direct property sustainability policy

CFSGAM has enhanced its treatment of ESG issues in the management of its direct property portfolio by incorporating ESG considerations into its property sustainability policy statement. This policy recognises the physical impacts that direct property assets can have on the environment and society, and offers direction for the management of these assets by making commitments to manage and minimise the effects of these impacts.

Through setting benchmarks and targets, the policy seeks to further align sustainability and ESG considerations for the long-term benefit of our clients and investors.

Implementation strategies

In our approach to sustainability and responsible investment in our investment process, we do not look to build socially responsible or ethical strategies that screen out particular companies or sectors.

ESG issues are considered in the same way that we consider traditional financial issues. We highlight this because there is still considerable misunderstanding across the industry around the definitions of mainstreaming ESG versus socially responsible or ethical investing.

In our approach to sustainability and responsible investment in our investment process, we do not look to build socially responsible or ethical strategies that screen out particular companies or sectors. ESG issues are considered in the same way that we consider traditional financial issues. We highlight this because there is still considerable misunderstanding across the industry around the definitions of mainstreaming ESG versus socially responsible or ethical investing.

Our strategy for Principles 1 and 2 is focused on information and education. Investment teams can only effectively integrate ESG issues into processes when they have quality information and they understand the issues.

We will continue to source ESG information from specialist ESG research providers, but we also look to our traditional financial research providers, namely the sell side, to also provide some analysis. We also look to continually educate our investment teams through monthly briefings from ESG specialists, which support learning through the practical application of ESG considerations in day-to-day business.

Our strategy for Principle 3 is based on collaboration. By working with other large investors we believe we can most effectively communicate our information needs to companies. We look forward to working further with IFSA and Australian Council of Superannuation Investors during 2010 on encouraging better reporting by companies.

Our strategy for Principles 4, 5 and 6 is driven by client and industry engagement and collaboration. To effectively mainstream ESG we need to work throughout the investment supply chain to make sure the right incentives are in place. This means working with:

- our clients to ensure they understand our approach and to provide them with high quality reporting
- our service providers to ensure they understand our requirements, and
- our peers to ensure we are communicating consistent messages to investee companies.

The scope of ESG considerations

The following definitions explain the scope and context of ESG as we refer to it in this document and consider it in our business.

Environmental

These considerations include the immediate environment in which companies operate, as well as the wider community and region. We take a broad consideration of environmental issues, such as considering the track record of how companies have dealt with past environmental issues, how companies have acted in environmentally-sensitive areas and public leadership on environmental issues. We do not seek out 'environmentally friendly' companies, but rather look for evidence that companies have effective management, processes and behaviours in place to mitigate any environmental impacts.

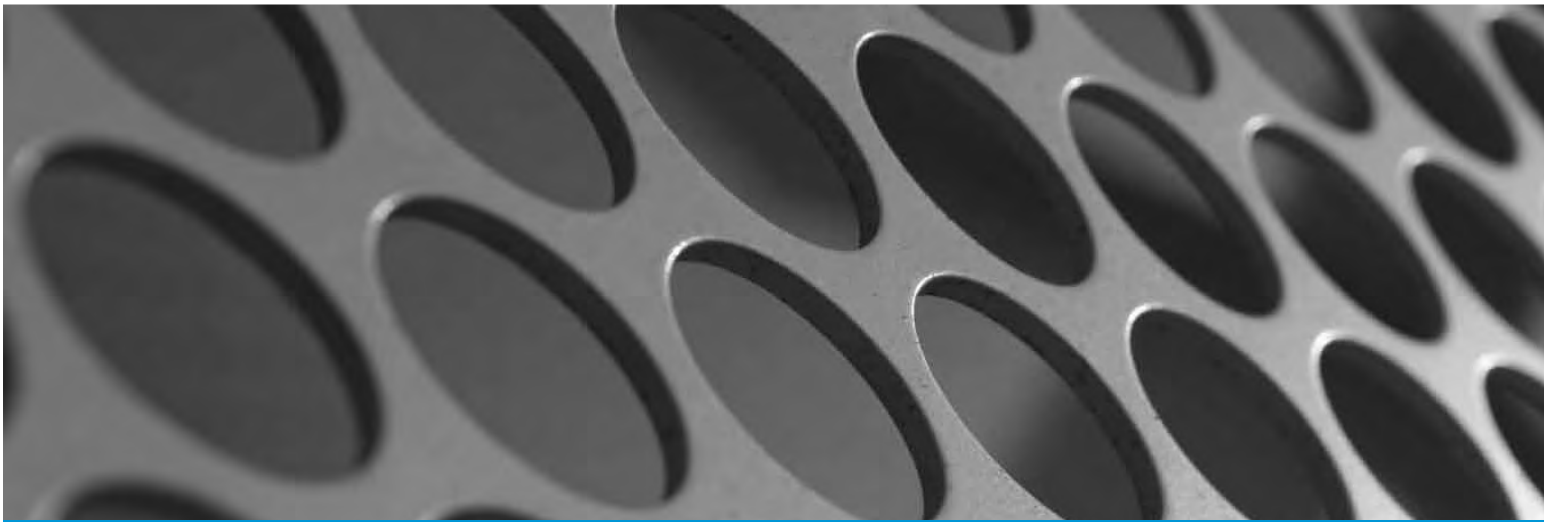
Social

Social considerations cover the human aspect of a business's operations, whether it be employees, suppliers, customers, the local community or wider society. It is important that companies are supported by the people they affect, in order to be able to operate without undue interference or hindrance. This concept is referred to as a 'social licence to operate' and is especially important in large organisations and infrastructure operations.

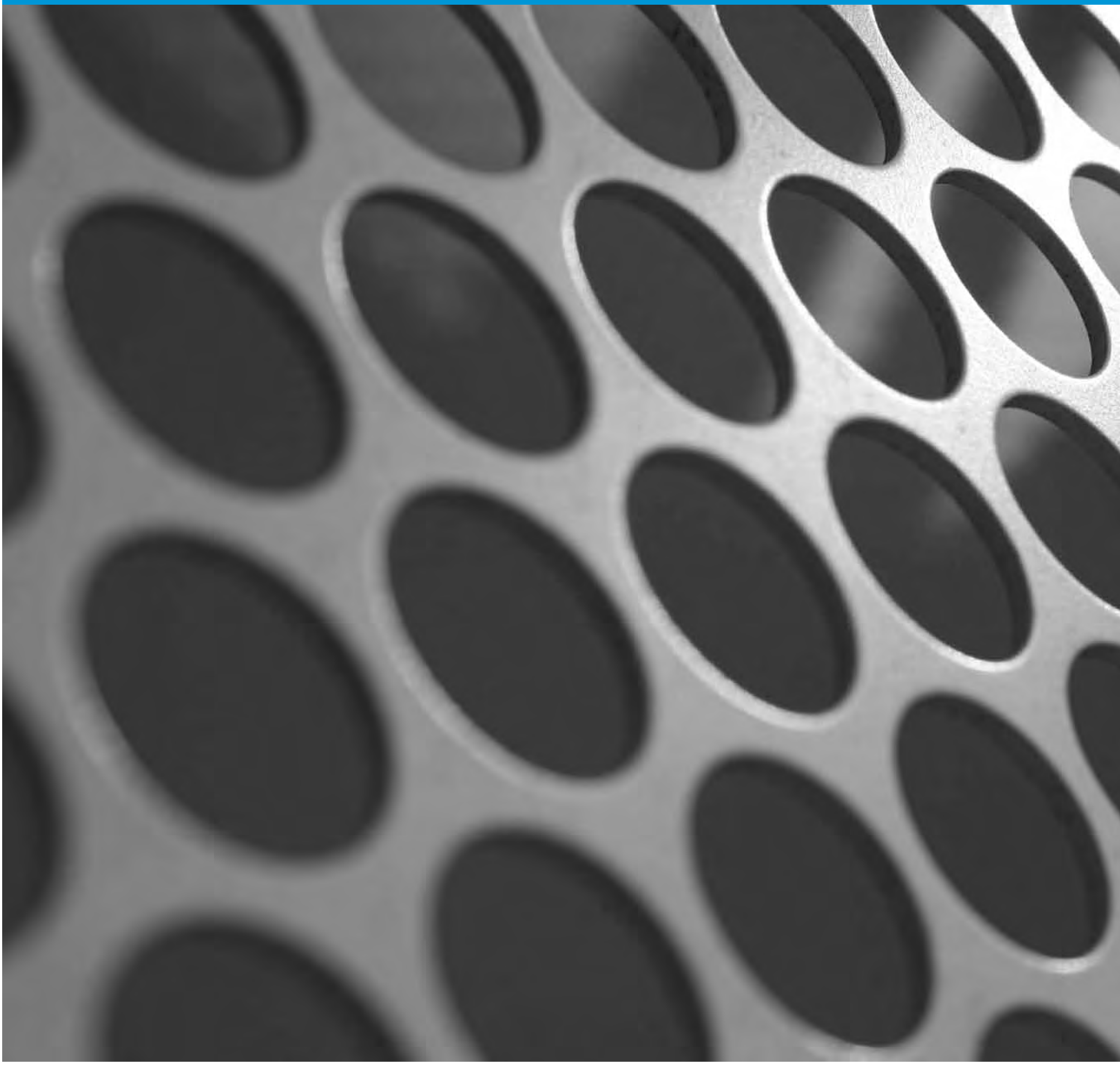
As a shareholder in many large organisations and direct owners of large property and infrastructure assets, a social licence to operate is an important part of our ESG considerations. In addition to companies being good corporate citizens, we may look for strength of community relationships, employee safety records, sensitivity when dealing with vulnerable communities and public leadership on social issues.

Governance

The scope of governance, in relation to ESG considerations, covers the impact that management, processes and behaviours have on the long-term interests of the business, its investors and the community in which it operates. It complements the required standards of governance as mandated by regulation and legislation.



Principle 1



"We will incorporate ESG issues into our investment analysis and decision-making processes"

PRI action points*	Reference
Advocate ESG training for investment professionals	1, 2
Encourage academic and other research on this theme	3
Address ESG issues in investment policy statements	4, 5, 6, 7, 8
Assess the capabilities of internal investment managers to incorporate ESG issues	5, 6, 7, 8
Support development of ESG-related tools, metrics and analyses	8, 9
Ask investment service providers to integrate ESG factors into evolving research and analysis	20
Assess the capabilities of external investment managers to incorporate ESG issues	N/A

* The PRI action points at the start of each Principle chapter are taken from guidance provided by the PRI to help signatories fulfil their fiduciary obligations under the PRI. Where action points have been addressed, they are referenced by number.

Principle 1 is a key area of focus for CFSGAM. By successfully implementing it throughout our business, we aim to ultimately realise the full investment proposition of responsible investment, which is to make the best possible investment decisions on behalf of our investors and so fulfil our fiduciary role. We are committed to integrating ESG considerations into every asset class and investment product. Each listed investment team is responsible for implementing PRI into their investment process and every team takes a slightly different approach. This is important as it empowers each portfolio manager with responsibility for integrating ESG into their investment process.
To support the investment teams, the business provides a number of resources, including responsible investment education sessions, dedicated internal resources, policies, and external research providers. The governance process we have in place ensures continuous improvements in our activities under Principle 1.

We also expect our service providers to support our ESG initiatives. Good progress has been made to integrate a consideration of ESG issues across all asset classes; however, some challenges remain. By fostering a culture of continuous improvements and innovation we seek to improve our expertise and effectiveness of ESG consideration and integration.

Implementation

1. Engaging staff with the great debate

One of the most frequent questions asked in early 2009 was whether responsible investment was still relevant despite the global financial crisis. To address the issue, the question was put forward to staff and a panel debate was held. With half the panel 'for' and half 'against', investment professionals debated the relevance of responsible investment in light of the global financial crisis.

Before the debate, we took an online poll of staff and 93% said that responsible investment was still relevant despite the financial crisis. Following the debate, 100% of attendees believed that responsible investment remained relevant. The debate was recorded and a webcast of the event was made available to all staff globally via the company intranet and highlights were shown at CFSGAM's all staff briefing to raise awareness and understanding of the issues.

2. Education forums

Responsible investment sessions are part of an education and awareness-raising program which helps to provide staff with a better understanding of the opportunities and challenges presented by responsible investment.

These sessions equip staff with the knowledge to engage on ESG issues with clients and the wider funds management industry. The following table summarises some of the guest speakers who were invited to present at the investment sessions during 2009 and the topics they covered.

Presenter	Topic
Charles Berger Director of Strategic Ideas Australian Conservation Foundation	While carbon and climate change issues are potentially the most material near-term investment issues, Mr Berger spoke of other pertinent environmental issues for investors, such as: – the transition to sustainable economies and green industries – increasing consumer interest in sustainability – the challenges of unsustainable patterns of consumption – emerging changes in how we assess economic growth and development, and – water scarcity, biodiversity and other environmental issues.
Elaine Prior Industry Thematics and SRI Analyst Citi Investment Research	In support of the pioneering research work Ms Prior has undertaken in this area, Ms Prior spoke about water challenges for listed companies and how they will adapt to increasing water-related risks, including: – security of supply – exposure to water pricing – how companies use water, and – how companies are adapting to growing water challenges.
Julie Hudson Managing Director UBS	To effectively integrate ESG considerations into the investment process, ESG data needs to be expressed in a way that allows key issues to be incorporated into stock analysis and company valuations. Ms Hudson outlined her views on how to more effectively integrate ESG considerations into equity valuations and spoke of the research on ESG issues that UBS had undertaken globally.
Ann Byrne CEO Australian Council of Superannuation Investors (ACSI)	Ms Byrne outlined a number of important ESG issues as they relate to the superannuation industry, including: – the outcomes of the second round of research that ACSI has done on the reporting practices of ASX companies – general observations that ACSI makes on companies' approach to ESG, and – the outcomes of the joint research done with Investment and Financial Services Association on how Australian fund managers are addressing ESG issues.
Terence Jeyaretnam Managing Director Net Balance	Net Balance is one of largest providers of sustainability advice, assurance and research in Australia. Mr Jeyaretnam shared his insights with staff about: – Net Balance's corporate governance research report on reporting practices of the ASX top 50 companies – 'the good, the bad and the ugly'; general company sustainability reporting practices, and – Net Balance's insights and experiences from working with companies on sustainability practices, and performance reporting.

3. Responsible investment library

A library is maintained on the CFSGAM intranet, where all staff can gain access to research papers, reports, presentations and articles relating to a range of current ESG topics.

The responsible investment library includes items that have been prepared by external companies and organisations as well as material that has been prepared internally.

The purpose of the library is to stimulate interest amongst employees and enable them to keep abreast of the latest ESG thinking and developments. The library seeks to educate employees about the scope of ESG issues and provide a deeper understanding of how these issues may affect our investments.

4. Third-party research providers

As part of our commitment to fully integrate ESG risk assessment into our investment processes, we engage third-party research providers for industry analysis and high-quality ESG research, to help CFSGAM understand factors which may place business value at risk.

The enlisting of third-party research providers underscores our commitment to sustainability and governance issues, and helps to ensure that we continue to offer our clients outstanding products and services. In addition to third-party research, we engage with companies directly and encourage brokers to produce quality ESG research.

Stock analysis – six key criteria

1. Management	2. Industry/company position	3. Valuation
Relevant experience	Industry structure/changes	Triangulation
Ability to execute	Pricing power/margins	Relevance to sector and peers
Shareholder focus	Competitive advantage	Consistency
4. Market factors	**5. Financials**	**6. Sustainability**
Index movements	Balance sheet	Social policies
Market themes	Cash flow generation	Environmental policies
Corporate activity	Earnings transparency	Management commitment and disclosure

Examples of our approach

Each investment team in CFSGAM takes its own, autonomous approach to considering ESG issues in its investment process. Given the differing nature of asset classes and investment strategies, we believe this is the most effective way to realise the value of ESG analysis. Examples of how we approach Principle 1 across our business are outlined below.

5. Australian Equities, Core team

The Australian Equities, Core team is committed to incorporating ESG issues into its investment philosophy and process. 'Sustainability' has recently been made explicit in the investment process and specified as one of the six criteria which the team uses to analyse companies listed on the Australian Securities Exchange.

Stock analysis – six key criteria

Analysts' assessment of listed companies now includes criteria related to practice, commitment and disclosure of social and environmental issues by management and performance relative to peers. For example, social assessment incorporates measures of employee and stakeholder policies, environment considers issues of climate change, company efficiency and practices relative to industry and acceptable standards, and management commitment is measured in terms of disclosure policies and practices and the integration of sustainability into employee key performance indicators. This is in addition to our analysis of companies' corporate governance policies, which are assessed under the Management criteria.

The Australian Equities, Core team has a commitment to engage with companies on sustainability issues as part of the day-to-day investment practice and also actively encourages brokers to incorporate ESG issues in their coverage and analysis of listed companies.

A good example of our commitment to engagement on ESG issues in the Australian investment community was in our dialogue over the past year with AGL Energy. The Australian Equities, Core team has a long history as a shareholder and has an established relationship with company management.

At a meeting with AGL Energy senior management in mid-2009, two members of the Australian Equities, Core team felt that while the company was effective in highlighting its renewable energy projects, its communication around safety issues could be improved.

As a result, the Head of Australian Equities, Core challenged AGL Energy to reconsider the way the company reports ESG issues in order to satisfy the demands of institutional shareholders, including CFSGAM. This piece of engagement encouraged AGL Energy to review the way its approach to sustainability is reported to the investor community.

AGL Energy has since effectively communicated how the company has incorporated and embedded an awareness of ESG and sustainability issues throughout its business. During subsequent presentations by the company, a full range of ESG considerations have been thoroughly covered, suggesting a genuine commitment to ESG issues exists within the company. Indeed, we believe the company is committed to promoting best practice regarding ESG and sustainability issues within the Utilities sector.

Following our initial dialogue with the company, a Senior Portfolio Manager in the Australian Equities, Core team was asked to present to a leadership forum at AGL Energy to present on a range of issues including the way CFSGAM considers ESG issues in its company analysis and why we believe a consideration of ESG factors is important for Australian companies in the 21st century.

This type of ongoing engagement with company management demonstrates how active investors can help change corporate behaviour by encouraging companies to focus on areas and improve on key issues.

As well as improving the company's commitment to sustainability issues, the process has undoubtedly strengthened the existing relationship between senior executives of AGL Energy and CFSGAM. This is important, as we believe forging and maintaining strong relationships with the companies in which we invest will benefit all our investors over the long term.

6. Direct property

ESG is incorporated into every aspect of managing the buildings within CFSGAM's direct property asset class, in accordance with the CFSGAM Property's sustainability policy. The investment process for property can be explained through the following three steps as it relates to ESG.

Step 1 – Acquisition

ESG considerations are incorporated in the due diligence process when acquiring new buildings through a standard checklist and sign-off process. This process investigates the environmental and physical impacts relating to the property and the land with regard to its construction and ongoing use and operation.

Social aspects are investigated with regard to the community and how the building interacts with its local environment. Regarding governance, the asset is reviewed for compliance with regulatory controls and economic performance. These ESG aspects are an integral part of our due diligence process.

Step 2 – Performance

The day-to-day management of buildings is closely guided by responsible investment principles, through our operational performance strategy. This strategy is focused on setting performance targets for the operation of the building based on an appropriate benchmark for the class of the building.

Monitoring, managing, analysing and reporting on the achievement of these targets allows for continual improvement. These factors are not taken into account alone, however, as the occupant use of the building is an integral part in achieving set targets. The improvement process involves physical and mechanical intervention and recommissioning of plant and equipment in the building.

Step 3 – Valuation

The valuation of buildings takes into account the income from the occupants and the costs incurred in running and maintaining the building, and ESG factors are integral to both of these aspects.

In regard to the income from occupants, we have green lease clauses in place for certain buildings and are developing these as a standard. Green leases assist in managing the occupant use of the building to help achieve sustainability, water efficiency, energy, resources and indoor environment quality goals.

With regard to the costs incurred in running and maintaining the building, life cycle costing of plant and equipment is used and takes into account ESG factors. Other aspects of valuation consider the amenity that the building provides and is reflective of the building's ability to attract and retain tenants to secure a reliable income stream.

7. Direct infrastructure

A consideration of sustainability issues is embedded in the life cycle of the direct infrastructure investment process. ESG issues are considered at the following four steps.

Step 1

During initial due diligence, prior to an investment being made in an asset, reference on the key issues for the different infrastructure sectors will be made to:

- existing legislation
- the IFC Performance Standards and the Equator Principles, and
- applicable industry-specific environmental, health and safety guidelines.

Step 2

We undertake ongoing active asset management post-acquisition as part of a continuous improvement process to value-add to asset performance and effectively manage risk. This is done through our active asset management strategy.

Step 3

Appropriate management of ESG considerations is undertaken as part of the ongoing valuations of assets and is a consideration in decisions whether to divest an investment.

Step 4

Thematic ESG issues are considered as part of our overall investment strategy. Through participation in industry dialogue we ensure we are across emerging sustainability issues for different infrastructure asset classes.

Direct infrastructure corporate engagement guidelines

CFSGAM has introduced new guidelines for corporate engagement to ensure that an adequate management framework is in place that identifies ESG issues within each asset under management.

The guidelines were developed to identify potential and existing risks for infrastructure assets and to set benchmark performance objectives that focus on key principles associated with ESG issues.

The guidelines were developed in close consultation with CFSGAM's Responsible Investment team and have been noted by the Responsible Entity and Trustee boards for the relevant CFSGAM infrastructure funds.

These guidelines help ensure that the long-term value of CFSGAM's infrastructure assets is enhanced and the reputation of CFSGAM's clients is protected.

8. Credit investments

ESG risks that have been proven to apply to equity performance are not necessarily relevant to credit. To provide value to credit investors, the consideration of ESG risk must add material value to the investment process rather than simply be a box to be ticked. The relevance of ESG risk to credit products, therefore, must first be established and then be effectively integrated into the investment process.

A major hurdle to integrating ESG into any investment process is the quality of research that is available. Current research on ESG factors is already severely limited compared to more traditional financial measures, and generally only covers listed companies. This presents a challenge for credit products, where listed companies may comprise only half the assets in a typical credit portfolio.

There is also a disparity in investment fundamentals. The main consideration for a credit product is simply a company's ability to repay its debt at the end of the term. The risk is not falling investment returns or a declining share price.

Furthermore, credit products have only potential downside: that is, that a company defaults on its loan. With zero upside potential, can ESG considerations enhance long-established and proven investment processes?

While there are challenges to integrating ESG into credit products, many ESG considerations are already entrenched in the credit investment process, with governance being the main focus. Governance is a key area of interest given its potential to contribute to default risk. Corporate collapses can seriously impact a credit manager's performance and often they occur as a result of poor governance. If environmental and social factors can provide pointers to effective governance, then ESG considerations are vital.

There is no assigned weight for any of the credit research parameters, including ESG. It is the analyst's role to consider all the different factors that could impact credit worthiness. Examples of an analyst's approach are given below.

- In a review of Fortis, a European bank and insurance company, the Innovest rating was incorporated into the overall rating. The company is not a leader in terms of ESG initiatives, and although the social welfare sponsorship aspects of the bank were fairly good, they were not outstanding. As a result, Fortis was given an overall internal rating of 'a', not 'a+', which might have been the case if the company's Innovest rating, and its demonstration of ESG initiatives, had been higher.
- A decision was made to not purchase bonds issued by a mining and refining company operating in India and Australia, despite strong financial performance, due to serious governance and management concerns. In our due diligence, it was discovered that the company's hydrant system in its aluminium business was not reliable or adequately equipped. The company also has large potential contingent liabilities for asbestos and environment claims due to its acquisition of a troubled copper producer in the US.

  The company is also facing court proceedings by the Stock Exchange of India (SEI) over one of its key operating subsidiaries. The SEI has alleged that the company violated regulations prohibiting fraudulent and unfair trading practices and passed an order prohibiting the subsidiary from accessing the capital markets for two years. This ruling was eventually overruled by the Securities Appellate Tribunal but the SEI has appealed to the High Court of Bombay. In addition to the issues mentioned above, the company still faces a number of further litigation matters, both civil and criminal, with civil financial claims totalling US$240 million.

The credit team has access to ESG research on over 2,500 companies, provided by Innovest, Glass Lewis and RiskMetrics, to help us understand and consider ESG issues that have the potential to contribute to default risk. Innovest ratings and research are captured in our proprietary credit research analytical system, 'Cred.net'. We also work closely with the internal Sustainability and Responsible Investment team to ensure we understand what ESG issues could impact our investments and there is a process in place to ensure continuous improvement.

There is still work to be done before ESG considerations in credit are on a par with equities. However, as happened with equities, there is increasing awareness that ESG can be effectively integrated to add real value to the investment process. As the integration of ESG risks in the investment process develops over time and becomes more refined, it will become an increasingly valuable consideration in credit investment decisions.

Cross business collaboration

9. Incorporating ESG issues into investment analysis and decision-making processes

As highlighted in our Responsible Investment Report 2008, the lack of comparable ESG reporting by companies presents challenges when trying to effectively incorporate ESG issues into investment analysis and decision-making processes.

This is particularly true for fixed interest and credit investments as there are very few ESG research providers who cover debt products as highlighted under 8 Credit investments.

To address these challenges, we developed a number of sector-specific tools which enable us to more easily and effectively integrate ESG considerations into the investment process. These tools were then rolled out across the investment teams at CFSGAM to help investment teams identify the material ESG issues for each asset class and capture metrics which best quantify these issues. Key issues are also captured for investment teams to address when we engage with companies.

Sector research tools were built for the following sectors:

- materials and industrials
- consumer discretionary and consumer staples, and
- Real Estate Investment Trusts.

These sectors were selected as ESG risks are particularly material and they coincide with the concentration of corporate names that are currently covered by the Fixed Interest and Credit team, but are unlisted and therefore have no existing ESG research. Although the sector research tools cannot provide coverage for unlisted issuers, they can supplement the coverage of corporate issuers who are not covered by third-party research providers.

Metrics used to assess companies on their environmental performance include:

- potential carbon liability and impact on net profit
- water intensity and potential risks to future security of water supply, and
- ownership of environmental issues.

Metrics used to assess companies' social performance include:

- employee safety performance over time and management oversight into contractor safety
- human capital management, including employee turnover and productivity, and
- staff accountability and alignment with shareholder interests.

Key governance metrics include:

- board structure and independence
- presence of substantial shareholders and protection of minority interests
- independence of auditors
- CEO remuneration and entrenchment within the company, and
- exposure to political risk and political donations made by a company.

To help populate these metrics, data was obtained from Trucost and RiskMetrics. Trucost is an external data provider of company carbon emissions and environmental footprint analyses. Where companies do not currently measure or publicly disclose their carbon emissions, Trucost uses a proprietary model to estimate a company's carbon footprint. The Trucost data was used by analysts to assess companies' potential carbon liabilities and associated regulatory risks. The Global Emerging Markets team have since subscribed to the Trucost data for emerging markets companies where reporting on ESG is particularly low.

RiskMetrics Group is the recognised standard-setter in financial risk management. Its view of financial risk includes consideration of corporate governance, compliance, accounting, legal, transactional and sustainability risks.

These sector research tools and frameworks, together with ESG data from external research providers, allows us to more effectively integrate ESG issues into investment processes and decisions, particularly where there is a lack of readily available information.

Challenges to implementation

As highlighted in our Responsible Investment Report 2008, the lack of comparable ESG reporting by companies presents challenges when trying to effectively incorporate ESG issues into investment analysis and decision-making processes. This is particularly true for fixed interest and credit investments as there are very few ESG research providers who cover debt products. Also, nearly half of the issuers under our Fixed Interest and Credit team's coverage are unlisted, including private companies, sovereigns, trusts, special purpose vehicles and government agencies. These entities make up a material proportion of funds under management where no ESG data or research is produced. This lack of quality research, combined with a lack of comparable reporting by companies, was the biggest obstacle we encountered when implementing Principle 1.

We like to be challenged in our views and provided with rigorous detailed analysis that can be used to supplement our own in-house thinking on ESG issues. For the mainstream research market to deliver the research we require they need to get consistent signals from their investment manager and superannuation fund clients. Collaboration with our asset owner clients, within the investment management industry and with the broker community to facilitate the development of quality ESG research, will assist us to fulfil our commitments under Principle 1.

Principle 2

“We will be active owners and incorporate ESG issues into our ownership policies”

With more than A$70 billion invested in Australian and global equities, CFSGAM is a significant shareholder on behalf of investors in many listed companies around the world. Our size and standing in the industry puts our investment managers in a strong position to engage with individual companies on ESG issues.

PRI action points	Reference
Exercise voting rights or monitor compliance with voting policy (if outsourced)	10
File shareholder resolutions consistent with long-term ESG considerations	10
Develop an engagement capability (either directly or through outsourcing)	11
Engage with companies on ESG issues	12
Participate in collaborative engagement initiatives	12
Participate in the development of policy, regulation, and standard setting	13
Ask investment managers to undertake and report on ESG-related engagement	N/A

Active ownership and engagement are amongst our top priorities as a fiduciary, because we firmly believe that there is a correlation between companies with good governance practices and strong, sustainable shareholder returns. Through our discussions, we seek to raise issues for potential improvement and encourage disclosure on ESG issues. Consequently, we seek to positively influence companies towards ESG best practice to ultimately benefit our investors.

Given the varying nature of the different asset classes we manage in relation to engagement, we take a different approach given the level of influence we have. For example, in engagement with listed equities where we do not have management control, we will use our influence as shareholders to encourage best practice ESG issue management.

Due to the autonomy of our funds, one investment team may have ESG concerns about a particular stock that is a major position in a different fund. Over the past 12 months we have looked to improve collaboration between investment teams on engagement on controversial issues.

Engagement with unlisted investments takes a slightly different approach. For direct infrastructure we engage through the board seats that we hold. During 2009, we formalised our commitment to engagement through the development of a detailed ESG policy for infrastructure. This ESG policy outlines how we engage the assets, and also how those assets should engage relevant stakeholders such as surrounding communities.

For direct property investments we are typically the manager of the assets, so engagement with the tenants of the property is the main area of focus. We also seek to develop and implement sustainability policies and ensure that reporting against these policies takes place. For more information on our approach to ESG considerations in direct property investments, please refer to 6 Direct property under Principle 1.

Listed investments

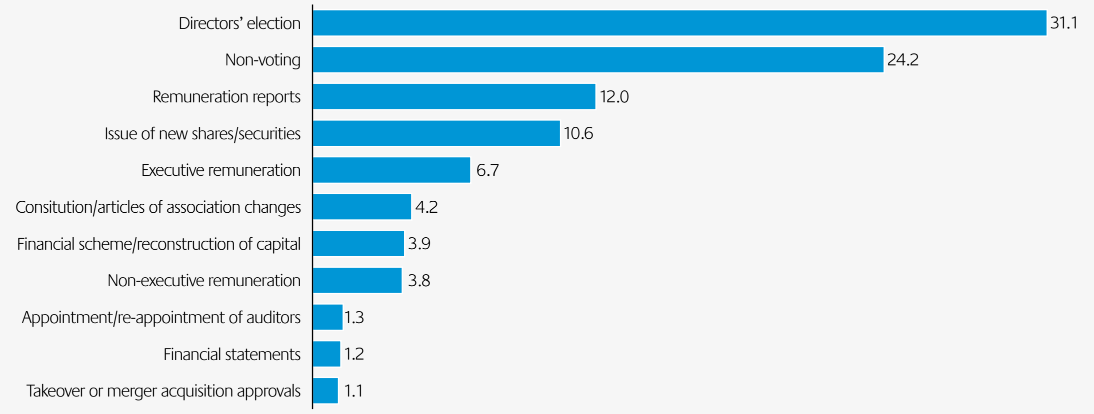
CFSGAM is an active manager and we undertake proxy voting and direct company engagement for our listed investments. As the active representative of major shareholders in many listed companies in Australia and overseas, we use our influence to encourage best practice management of ESG issues in the companies in which we invest.

During 2009, we undertook private collaborative engagement, primarily on corporate governance, and we supported engagement undertaken as part of the corporate governance research process by RiskMetrics for Australian companies.

Principle 2
continued

The chart below shows the proportion of resolutions that we voted on during the recent proxy voting season. There has been a focus on executive remuneration and board composition in recent times to ensure that they are appropriate and in the best interests of the company and its shareholders.

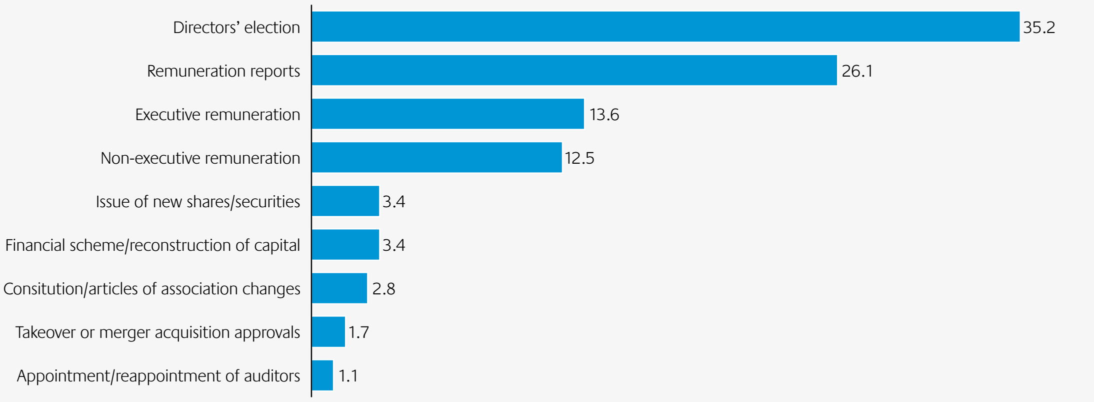
Categories of voting resolutions 2009 (%)



Source: CFSGAM.

The chart below shows a category breakdown of where we voted against resolutions. A significant number of 'against' votes were recorded during 2009, with election/re-election of directors and remuneration being the main areas of contention.

Breakdown of CFSGAM 'against' votes 2009 (%)



Source: CFSGAM.

10. Proxy voting

Proxy voting rights are an important component of shareholder responsibility, and so we vote on all possible resolutions at company meetings. The relevant investment manager and company equity analyst carefully consider each resolution, with guidance provided by our **Guidelines and principles for corporate engagement on governance, environment and social issues** and recommendations from a selection of independent corporate governance research houses.

We believe that voting against resolutions is not the only way to encourage change. By voting in favour of appropriate, well-structured appropriate resolutions we send a clear signal to the company and the broader market about practices we will support.

11. General engagement

CFSGAM actively engages with company management and directors on a range of ESG issues. CFSGAM's scale and reputation in the investment management industry provides our investment managers with the valuable opportunity to engage in dialogue with individual companies. We seek to highlight areas for potential improvement, encourage disclosure on ESG issues and recognise companies that are making progress in addressing ESG considerations.

At CFSGAM we engage with companies in which we invest on a variety of ESG issues. The following list does not necessarily apply to all asset classes or investment management processes, but examples of the type of ESG issues we engaged in included:

- activities in conflict zones
- benefits and compensation
- bribery and corruption
- climate change
- distribution of fair trade products
- human rights
- labour issues
- management quality
- occupational health and safety, and
- social licences to operate.

We believe that engagement with companies is key to achieving ESG improvements and we have collaborative initiatives with third-party engagement providers to help gather necessary information to help us get maximum value from engagement.

12. Engagement examples

Stockland

Stockland invited CFSGAM to provide feedback on its sustainability report from an investor perspective. We believe it is a positive step by Stockland to seek direct feedback on its ESG management and a CFSGAM analyst was pleased to provide the following key points where it was felt there could be improvements in the Stockland sustainability report.

- The report effectively captures ESG initiatives that Stockland has undertaken during the year to address sustainability issues; however, the outcomes of these initiatives could be provided in more detail.
- Summary data at the beginning of the report and a downloadable spreadsheet of metrics would be useful for investors.
- More transparency is needed on quantifying the cost of raising properties' National Australian Built Environment Rating System (NABERS) energy ratings, and the cost savings that would be realised by improving asset efficiency. Stockland will seek to provide discussions and case studies on these points in future reports.
- It would be useful for Green Star ratings to be disclosed for new properties and developments.

We also provided feedback to Boral and James Hardie during the period on their sustainability reporting. This dialogue should help companies understand what CFSGAM, as an investor, would like to see in ESG reporting. Over time, this will enhance the transparency and usefulness of ESG reporting more broadly so investors can better consider companies' ESG credentials when making an investment decision.

Esprit

The consumer analyst in CFSGAM's Global Equities team met with Esprit's Chief Operating Officer and Investor Relations Manager at its offices in Germany. During the course of the meeting, the analyst noted that the business was predominantly European but that the company maintained its Hong Kong listing. The analyst observed that Esprit shares had higher relative volatility compared to its closest peers, H&M and Inditex. The analyst noted that a consequence of this higher volatility was a higher cost of equity and therefore a potentially lower share price. The analyst urged Esprit management to consider this issue of share volatility as it was hampering a more positive view on the stock.

At a follow-up meeting, CFSGAM analysts presented data showing Esprit's higher beta compared to that of H&M and Inditex, which Esprit management found interesting. Our analysts suggested that more frequent communication with the market might help reduce some of the volatility, as Esprit reports results only semi-annually whilst some peers report quarterly earnings and monthly sales. Esprit management expressed its desire to improve the overall level of communication with market participants and the idea of more frequent sales disclosure was well received. Esprit is now considering providing these results on a quarterly basis.

Platinum production company

A small platinum producing company with its assets located in South Africa was raising money to repay a US$40 million facility that had very high interest costs from a local South African bank. CFSGAM's Global Resources team liked the quality of the resource, the projects and operational management.

The team had reservations, however, with the company's corporate governance and treatment of minority shareholders. The controlling shareholder was a private equity firm that owned 52% of the company and had two seats on the board. This company has additional interests in a number of tenements that could potentially be sold into the company at a later date. Whilst this should be beneficial for the long-term valuation, we were concerned that the terms of these future deals might not be deemed fair for minority shareholders.

The Global Resources team held several discussions with various levels of management, including the Chairman and Managing Director, who pointed out that they are also minority shareholders, each with a significant holding in their own right. Consequently, it transpired that their interests are completely aligned with our own.

They advised us that any future transactions between their company and associated companies of the major shareholder will be done at arm's length, based upon independent valuations and using industry standard metrics such as $/oz per category of resources. All such transactions will be put to the board for approval and related parties will not be eligible to vote. Although corporate governance risks remain, we now have more comfort and the stock's position in the Global Resources portfolios reflects this risk/reward balance.

Vedanta Resources

CFSGAM received correspondence from Amnesty International in relation to concerns about Vedanta's approach to ESG issues. While we only have very minor holdings in Vedanta and subsidiaries, we contacted the company and requested clarity on the concerns that had been raised.

The Global Equities Team also attended a workshop sponsored by BankTrust and Amnesty International in London. Various stakeholders attended, including around 14 non-government organisations and several representatives of financial institutions that are either investors or have provided financial advice or loans to Vedanta. The sector specialist attended along with an external consultant. Although Vedanta was apparently invited to attend too, they were only aware of the workshop when we mentioned it to them. In response to the Global Equity team's query and those of other investors, Vedanta drafted a response to some of the claims and allegations of the non-government organisation community. We have had several interactions with Vedanta's investor relations personnel on these claims and their responses. We continue to monitor the company and its approach to ESG issues.

Kingboard Chemical

The Global Emerging Markets team undertook a lengthy engagement process with Kingboard Chemical. This company is not held within our Global Emerging Markets Sustainability Fund, although it is held in other CFSGAM funds. The company manufactures printed circuit boards, a key component of computers. Following the publication of a Greenpeace report which accused the company of polluting the Pearl River, our team in China embarked on a lengthy set of meetings with the Chairman, CEO, CFO, key independent directors and Greenpeace.

It transpired that Greenpeace did not contact the company ahead of publishing its contested report, which led to a more confrontational and less productive relationship between Greenpeace and Kingboard Chemical than we would have liked. Nonetheless, we are optimistic that Kingboard Chemical will be focusing on sustainability over the coming months and years and we will continue to monitor the company accordingly.

Spotless Group

Engagement often takes a different form in the credit and fixed interest asset class than it does in listed equities. An example of engagement undertaken by our Fixed Interest and Credit team is when we were invited to participate in a structured deal by ABN AMRO and the service provider in the transaction was Spotless Group. Due to public concerns about governance issues at Spotless Group, we asked ABN AMRO to provide more information. We did not proceed with the investment for several reasons, one was the ongoing governance issue at Spotless, and the pricing appeared slim given the rating.

Unlisted investments

Principle 2 is also relevant to unlisted asset classes. However, the implementation of this Principle is somewhat different from listed investments, given the different nature of the shareholding and ownership relationship.

The relative lack of liquidity in unlisted investments makes ESG issues potentially more material if not managed proactively. As investors in unlisted assets, we are generally able to take a longer-term view than may be the case with publicly traded equities.

Our investment process for unlisted investments seeks to:

- price ESG risk as part of the consideration during the initial transaction process
- incorporate ESG considerations into the due diligence process
- incorporate ESG management through the governance process, primarily through Board representation, and
- continually monitor all aspects of the investments, including consideration of ESG risks.

For our unlisted infrastructure investments, CFSGAM generally seeks representation at the board level or equivalent. We are active on ESG issues via this representation or through company engagement. We also seek to ensure that there are adequate sustainability policies in place and reporting against these policies takes place.

Case study: direct infrastructure engagement

13. Electricity North West Corporate Social Responsibility Policy

CFSGAM, through its infrastructure funds and mandates, owns 50% of Electricity North West (ENW). CFSGAM is an active owner in ENW and holds three board positions.

ENW owns and, through United Utilities, operates and maintains the electricity distribution network throughout north-west England. This incorporates 58,000km of cables, 96 bulk supply substations, 363 primary substations and 33,000 transforming points, delivering over 24 terawatt hours of electricity annually to some 2.3 million domestic and industrial customers.

CFSGAM worked closely with the ENW corporate team to develop the ENW Corporate Social Responsibility (CSR) Policy. Since the introduction of the policy in September 2009, ENW has had dedicated resources working on the implementation of CSR initiatives.

The implementation of the ENW CSR Policy is a critical step to ensure that an appropriate management culture is established in the ENW management team to fully assess and address ESG risks and opportunities in the business.

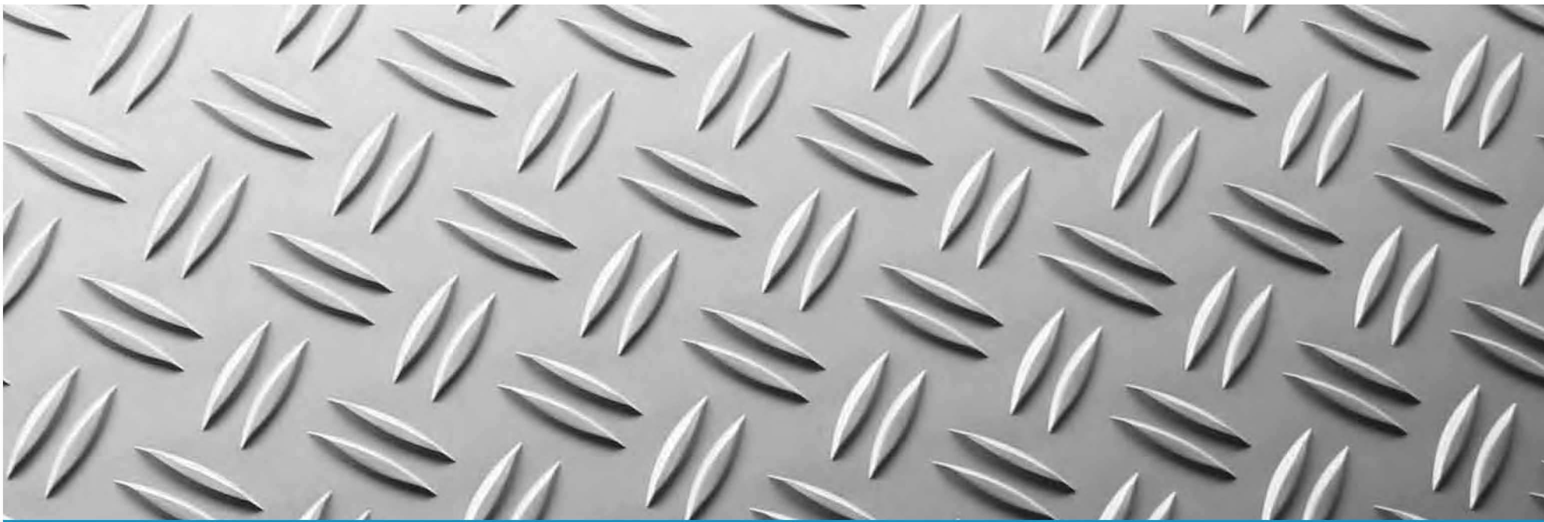
The policy provides a framework to establish:

- appropriate business ethics and operational values
- a strong workplace culture relating to employment practices, employee behaviour, company approach to business and community commitment
- appropriate health and safety policies in the business
- a commitment to the company sustainable development policy, and
- a series of key performance indicators to ensure the policy is being implemented effectively.

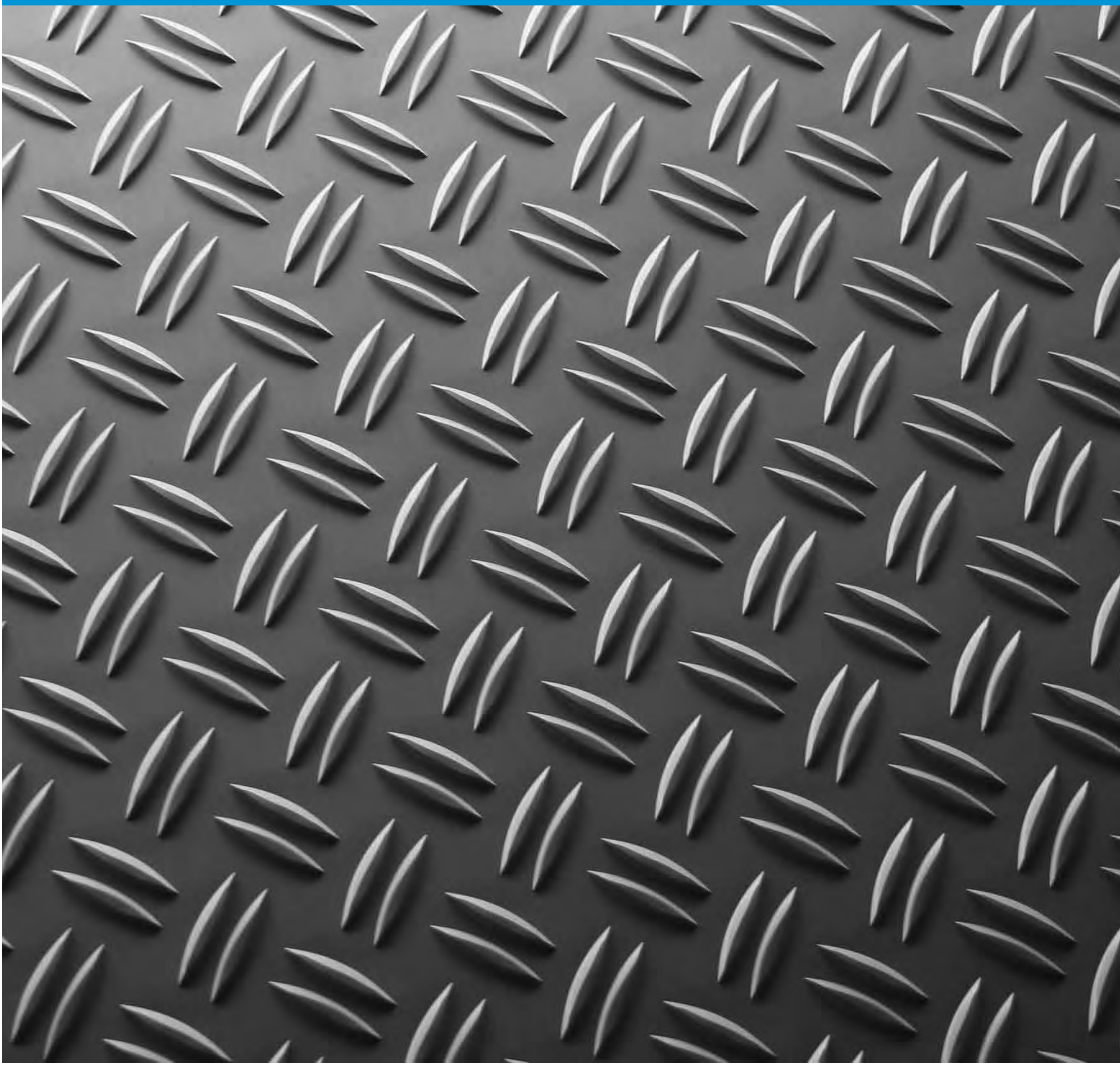
As an active investor, we will continue to support initiatives that deliver sustainable investment returns for the ultimate benefit of our funds and clients. Through influencing the quality of the company's policy, we can have better oversight at the board level and be more confident in the effective management of long-term ESG issues.

Challenges to implementation

As we reported last year, the large scale, complex structure and global reach of our business continues to provide challenges when looking to monitor and report our activities under Principle 2. Given the autonomy of the investment teams and the different investment styles, it is difficult to effectively capture the engagement that occurs. As a result, tracking our success is challenging. This, combined with the fact that the actual outcomes of engagement are difficult to measure, means it is difficult to accurately quantify our achievements.



Principle 3



"We will seek appropriate disclosure on ESG issues by the entities in which we invest"

PRI action points	Reference
Ask for ESG disclosure to be integrated within annual financial reports	14
Ask for information from companies regarding adoption of/adherence to relevant norms, standards, codes of conduct or international initiatives	14
Support shareholder initiatives and resolutions promoting ESG disclosure	15, 16, 17
Ask for standardised reporting on ESG issues	18

It is important for us to seek adequate and appropriate disclosure on the entities in which we invest in order to provide our investment analysts with practical information that they can effectively incorporate into their investment decision-making processes. To encourage companies to provide useful information, a common industry view needs to be formed on the impact that ESG issues could have on listed companies. It is still a challenge that most investment managers are not asking for the necessary information as there needs to be a critical mass of investors to drive companies to produce the information we require.

We undertook a number of initiatives during the year to encourage transparency and disclosure on ESG issues from companies, examples of which are outlined below.

14. Company reporting

Company reporting on sustainability and responsible investment and their participation in ESG initiatives was a key feature of engagement during 2009. We participated in the following collaboration initiatives to encourage better reporting by companies on ESG issues during 2009.

15. Carbon Disclosure Project

CFSGAM is a signatory to the Carbon Disclosure Project (CDP) which was launched in 2000 to collect and distribute high quality information that motivates investors, corporations and governments to take action to prevent climate change. The CDP harnesses the collective power of corporations, investors and political leaders to accelerate unified action on climate change.

More than 2,500 organisations in 60 countries now measure and disclose their greenhouse gas emissions and climate change strategies through CDP, in order that they can set reduction targets and make performance improvements. CFSGAM's listed property trusts, CFS Retail Property Trust and the Commonwealth Property Office Fund, disclose to the CDP.

16. Forest Footprint Disclosure Project

The Forest Footprint Disclosure Project (FFDP) is a new UK Government-supported initiative, created to help investors such as CFSGAM identify how an organisation's activities and supply chains contribute to deforestation, and link this forest footprint to their value. Modelled on the Carbon Disclosure Project, it aims to create transparency and shed light on a key challenge within investor portfolios, where currently there is little quality information.

By engaging with the financial and corporate communities, the FFDP aims to reduce the size of the global forest footprint and ensure that forest footprint evaluation is embedded into the working practices of the target sectors. CFSGAM became a signatory to the FFDP in early 2009.

17. Extractive Industries Transparency Initiative

The Extractive Industries Transparency Initiative (EITI) was established in 2003 to support improved governance in resource-rich countries through the full publication and verification of company payments and government revenues from oil, gas, and mining. The EITI arose following public concerns about how much companies are paying, and what countries are doing with the funds. About 30 countries are currently participating to help protect their social licence to operate, including Yemen, Peru, Albania and Nigeria. The EITI helps companies improve stakeholder and community relations, mitigates reputation risk and helps provide transparency to investors.

CFSGAM supports the EITI because it contributes towards improvements in governance and transparency in emerging markets. Country reporting is expected to provide a better understanding of sovereign and political risk which may be particularly useful for our Credit and Fixed Interest investment team.

18. Direct infrastructure ESG reporting

CFSGAM's active investment management typically involves taking a seat on the board of directors of the company, participating in the planning and budgeting process, selecting management and maintaining ESG and reporting standards. By taking active roles on the boards of our invested companies, we ensure that we are fully informed of the current asset condition and applicable risks.

Through regular and ad hoc reporting we ensure that investors are kept appraised of policies and procedures that are implemented to mitigate and manage ESG risks and which help to protect the assets' social licence to operate. Following are examples of ESG reporting undertaken by our direct infrastructure investments.

Airports

The direct infrastructure team has investments and/or board representation at Brisbane Airport, Sydney Airport, Adelaide Airport, Perth Airport and Bankstown Airport.

CFSGAM takes an active, hands-on approach to sustainability and ESG considerations in its airport investments and works to support and protect the social licence to operate for these environmentally and socially sensitive pieces of infrastructure.

The airports in which CFSGAM invests undertake a range of ESG reporting. This includes producing a Master Plan, which is developed under the Commonwealth Government's planning regime. The airports' master plans are designed to provide a comprehensive overview of the future developments, direction and growth of our airports. The airports also produce environmental reports, strategy papers and annual reports.

Bankstown Airport also publishes an Operational Environmental Management Plan which identifies the environmental risks and legal obligations associated with the day-to-day operations of a tenant business. It specifies the management measures the tenant will implement in order to prevent or minimise the environmental impacts associated with these operations.

Utilities

Loy Yang Power (International Power)

Privatised in May 1997, Loy Yang Power owns and operates the 2,200 megawatt Loy Yang power station and the adjacent Loy Yang coal mine. The company supplies approximately one third of the state of Victoria's power requirements. The Loy Yang power station is the largest in Victoria and the open cut is the largest producing brown coal mine in the southern hemisphere.

In 2009, Loy Yang Power released ESG reporting which included:

- a report to the community
- an externally verified sustainability report, and
- an annual report.

Hazelwood Power Station (International Power)

Hazelwood Power Station, situated in Victoria, is a brown coal fuelled power station. The power station is of 1,600 megawatt capacity, and supplies up to 25% of Victoria's base load electricity. Hazelwood Power released a 2009 annual report which covered in detail the environmental and governance issues associated with the operating activities of the Hazelwood Power Station and the associated coal mine. It also released:

- an annual environmental performance report
- an annual environment and resource efficiency plan, and
- quarterly environmental reports to our Environmental Review Committee.

Electricity North West

During the period, Electricity North West (ENW) released a number of ESG communications including a **Strategic Direction Statement** which covers at high level the main developments ENW foresees for its business, network, and the services it provides to customers.

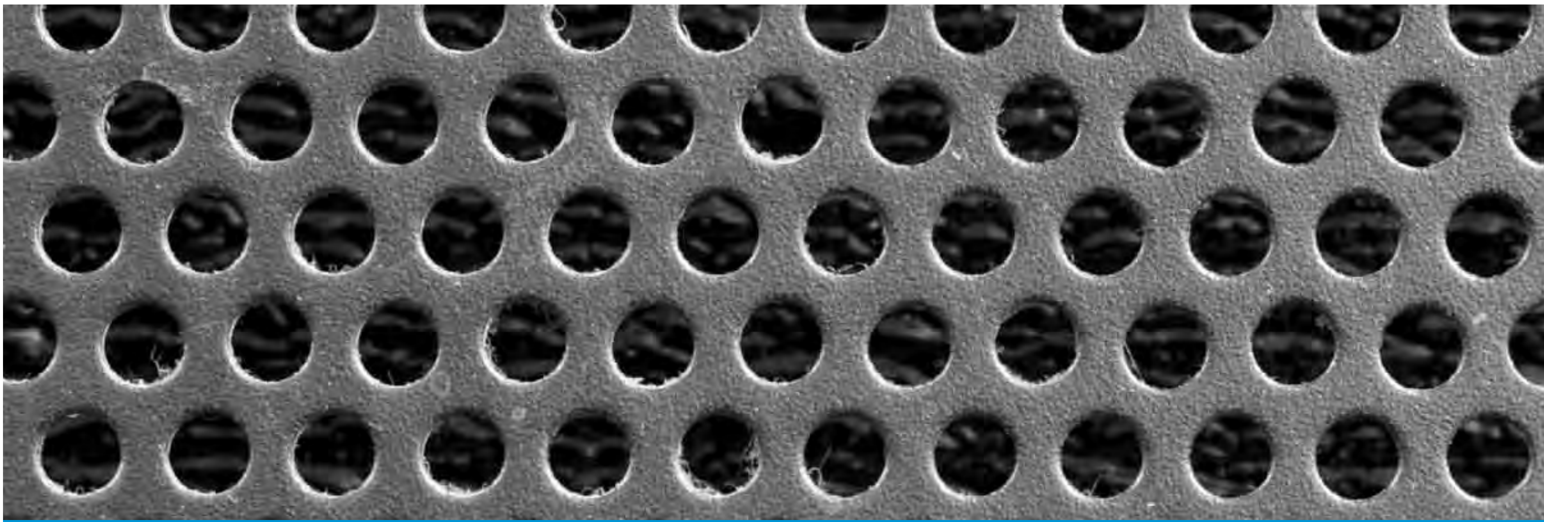
ENW also commissioned an independent **Low Carbon Energy Market** survey to understand how the low carbon energy market may develop in north-west England, and how ENW can assist in its development.

Challenges to implementation

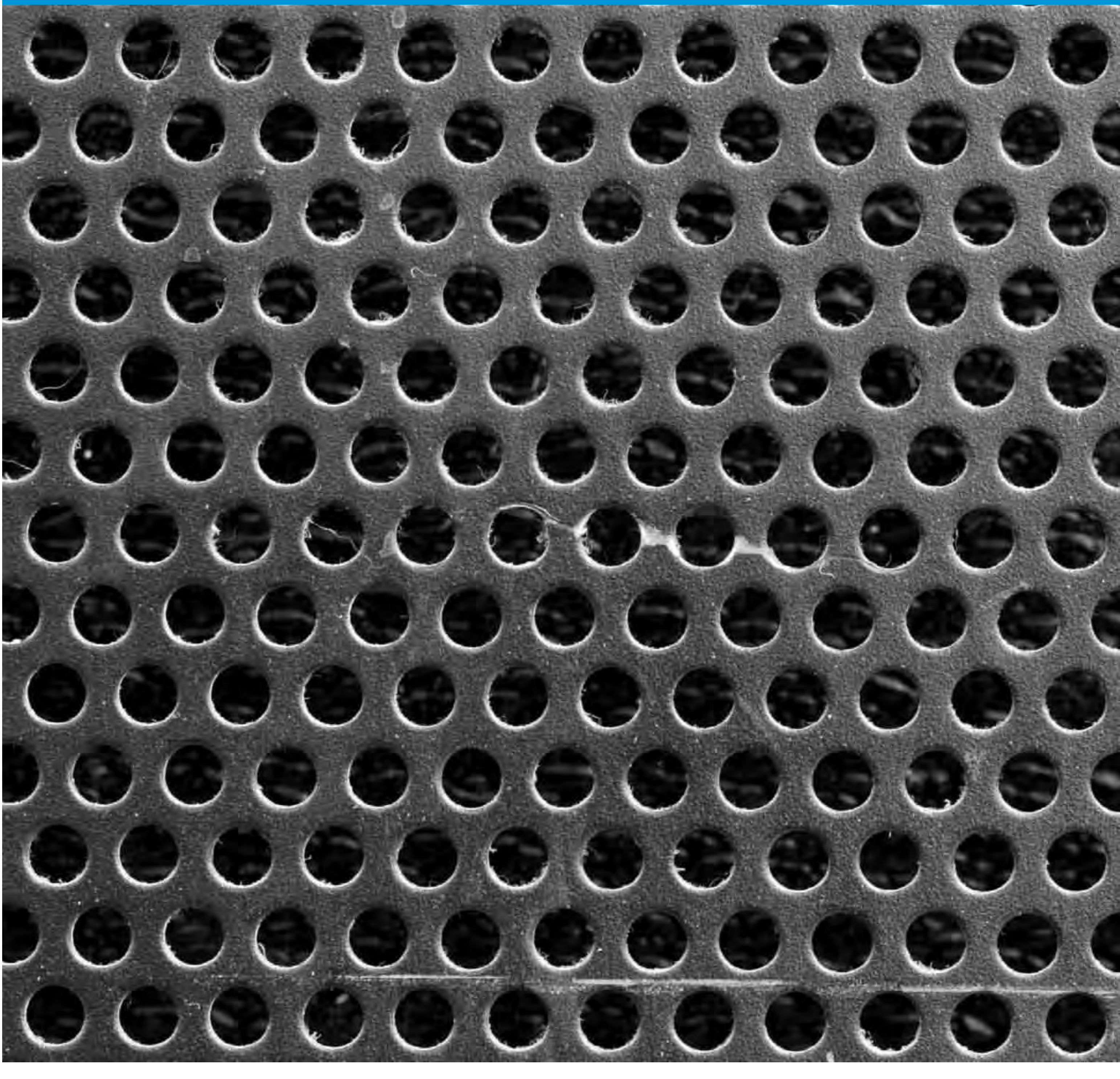
The limited engagement with companies on ESG reporting from the investment community means that the information companies provide is still not written in a form and style consistent with what we need to integrate the information into our investment processes. Furthermore, what companies are currently reporting is still not always the most material information.

In 2009, we saw an improvement in the coordination of the investment industry's approach to providing ESG information, with Bloomberg increasing coordination in the ESG information it now provides. Given the number of analysts that use Bloomberg for standard market data, we believe this is an important step in the right direction. We raised Bloomberg's ESG information in a number of company meetings and encouraged companies to review the fields and make sure they are providing as many data points as possible. Similarly, Thompson Reuters is another leading market data provider. Its acquisition of Asset4 should also lead to a greater 'mainstreaming' of ESG.

Image on next page is courtesy of Electricity North West (ENW).



Principle 4



"We will promote acceptance and implementation of the Principles within the investment industry"

PRI action points	Reference
Support the development of tools for benchmarking ESG integration	19
Include Principles-related requirements in requests for proposals	20
Communicate ESG expectations to investment service providers	20, 24
Support regulatory or policy developments that enable implementation of the Principles	21, 22
Revisit relationships with service providers that fail to meet ESG expectations	23
Align investment mandates, monitoring procedures, performance indicators and incentive structures accordingly	25

CFSGAM actively engaged in dialogue, lobbying and initiatives pertaining to government policy and industry regulations, primarily through the Investor Group on Climate Change, the Investment and Financial Services Association, the Property Council of Australia and the Green Building Council of Australia.

We consider ESG issues when selecting proxy voting specialists, investment research and internal operations. Service providers, clients and peer organisations are encouraged to become PRI signatories and we encourage the wider asset management industry to consider ESG issues. CFSGAM participated in a number of engagement initiatives to promote acceptance of the Principles within the investment industry during the year, most notably the participation in ESG Research Australia.

Specific examples of our activities under Principle 4 include:

19. Direct property: the Property Council of Australia and the Green Building Council of Australia

CFSGAM is an active member of the Property Council of Australia (PCA), with both the Head of Sustainability (Property), and the Sustainability Manager (Property), being members of the National Sustainability Roundtable and the Sustainable Development Committee. CFSGAM actively promotes and encourages other investment organisations to implement ESG principles in their ownership models.

Through the National Sustainability Roundtable and the Sustainable Development Committee we have actively lobbied government on proposed policy formation and on practical aspects of policies. Such policies and regulations include the Carbon Pollution Reduction Scheme (CPRS), the National Greenhouse Energy Reporting (NGERS) Act as well as mandatory disclosure of energy efficiency in office buildings.

Members of these committees, representing direct property asset owners, published an industry guide to disclosure under the NGERS Act. This is available on the PCA website, and assists property owners satisfy their ESG legislative obligations through reporting of emissions.

CFSGAM is also an active member of the Green Building Council of Australia through its representation on the board and as a member of the board sub-committee on Advocacy.

20. Direct infrastructure: working with suppliers

When appointing our panel of independent valuers for our direct infrastructure assets, we requested information and data on their capabilities of taking into account ESG considerations relating to valuations. This information was used in the short-listing process for our valuation panel. Similarly, in the appointment and review of all service providers for our direct infrastructure investments, ESG capabilities are an important consideration.

21. ESG Research Australia: engaging service providers

There is a need to send a clear signal to the research community regarding the lack of quality ESG research and CFSGAM has been an active participant in the discussions leading to the formation of the ESG Research Australia Initiative.

To encourage brokers to provide ESG research, superannuation funds HESTA, UniSuper and VicSuper established ESG Research Australia in 2009. A number of superannuation funds and fund managers have subsequently joined ESG Research Australia to work towards the common objective of increasing the quantity, quality and scope of ESG research produced on Australian companies. CFSGAM has representation on the board of ESG Research Australia and chairs the Research Evaluation Committee.

ESG Research Australia's objective is to increase the quality and quantity of research by Australian brokers that includes longer term environmental, social and governance factors. Further information about ESG Research Australia can be found on its website.

When ESG Research Australia was founded in early 2009 there were only two researchers consistently producing high quality ESG research in Australia. Now, despite the challenges presented by the global financial crisis, most of the major Australian brokers have established some form of capacity in this area. While the key topics covered by these brokers remain largely focused on carbon trading and environmental issues, we expect the market will deepen its understanding of social and governance issues over time. Topics we would like to see covered in more depth include:

- consumer and public health
- supply chain stewardship issues
- related party transactions and the independence of the board
- consumer debts for the financial services and retail sector
- executive remuneration
- board quality, and
- geo-political and security risk.

Although ESG Research Australia is focused on research on Australian companies, it represents part of an international effort to improve investment practices by taking into account ESG factors.

ESG Research Australia's progress is consistent with the high uptake of the PRI in Australia, and supports the view that fund managers and superannuation funds in Australia are cognisant of the investment implications of long-term ESG factors.

22. Government engagement

The impact of an emissions trading scheme is clearly one of the environmental issues most likely to affect investments across a range of asset classes. It is therefore in investors' best interests to ensure there is a scheme that is fiscally responsible and environmentally credible. Only then can investors accurately price potential risks and opportunities presented by the schemes.

While most of our policy engagement on emissions trading and broader climate change issues is done through the Investor Group on Climate Change, in 2009 CFSGAM engaged directly in the policy process. This involved presenting to the Senate Economics Committee inquiry into the draft of the legislation to implement the Carbon Pollution Reduction Scheme in March 2009. The transcript of the presentation and the resulting report is available on the Australian Government's website.

On global policy, we were pleased to support the '2009 Investor Statement on the Urgent Need for a Global Agreement on Climate Change' that was signed by our Chief Executive Officer.

In 2009, Senator Nick Sherry, Minister for Superannuation, announced that he had written to the Australian Prudential Regulation Authority (APRA) to request it 'review its investment guidance with the aim of clarifying the fiduciary responsibility of trustees in regard to balancing short and long-term investment goals and to make it clear that trustees can incorporate ESG issues in the formulation of their investment and other operational strategies'.

We strongly supported this guidance and we wrote to APRA in encouragement. We also emphasised the importance of distinguishing between socially responsible or ethical investing and the 'mainstreaming' of ESG in any guidance that is provided.

Contribution to policy that supports responsible investment is also made through our membership of various initiatives, including the:

- Asian Corporate Governance Association
- Australian Green Infrastructure Council
- Green Building Council of Australia
- Investor Group on Climate Change, and
- Property Council of Australia.

23. Emerging markets

The standard of disclosure in emerging markets can present a challenge when integrating ESG. To encourage improved disclosure we emphasised the importance of guidance to companies on ESG reporting when we met with the exchanges in various emerging market jurisdictions.

We also looked to provide input to the discussion arising from the publication of the Walker Report on corporate governance of UK banks and financial institutions in the UK. David Gait, Senior Portfolio Manager from our emerging markets business, wrote the opinion piece at the end of this section that was published in various media outlets. The article emphasises the importance of improved stewardship in Asia and examines the unique challenges for establishing and encouraging the rights and responsibilities that go with owning part of a business in Asia.

24. External presentations

Employees from across CFSGAM have presented at a number of key industry forums on various aspects of ESG integration, examples of which are given below.

Green Cities 09 Australasian Conference

The Head of Sustainability and Responsible Investment spoke at the Green Cities conference in March 2009. This was a joint initiative of the Property Council and the Green Building Council of Australia and sought to deliver leading edge thinking on sustainability.

Australian Super Investment Conference 2009

Representatives from CFSGAM participated in a discussion about protecting shareholder value through active engagement with companies. The discussion explored the potential benefits from engaging companies on their approach to safety performance and getting them to improve and be more transparent in their approach.

2009 International Corporate Governance Network Annual Conference

CFSGAM's representative was the Moderator in a joint IGCN and PRI conference session titled 'Sustainability: Managing in a world of extra financial risk'. This session examined the potential impacts of climate change for long-term investors and looked at the biggest challenges to achieving long-term sustainability. CFSGAM's Co-head of Infrastructure also presented on ESG issues in direct infrastructure investing.

Clean Energy Expo Asia 2009

Clean Energy Expo Asia is a trading and knowledge-sharing platform which brings together leaders in the Technology, Services, Finance and Government sector to address key issues in the areas of renewable energy, energy efficiency and sustainable development in the Asia Pacific region. CFSGAM participated in a conference session titled 'Clean Energy – Energy Efficiency Panel Discussion on Energy Efficiency as a Clean Energy Resource'.

Professional development on climate change

This program, titled 'Learning to Adapt: The Climate of the Future' looked to heighten the awareness of business and environmental leaders dealing with climate change by identifying gaps in understanding and providing tools and techniques to help business adapt to the climate of the future. A CFSGAM representative participated in an expert panel discussion on the need for climate change adaptation.

25. Sustainability rating tools

The Australian Green Infrastructure Council (AGIC) was established in 2007 to develop and implement a sustainability rating tool within the infrastructure industry. CFSGAM joined AGIC in August 2009 and was appointed to the board at that time. CFSGAM has been very active via its government contacts in canvassing Federal and State governments for funding for AGIC.

AGIC's sustainability rating tool will help to deliver more sustainable infrastructure in Australia and we consider it to be an important value protection mechanism. The tool will also be used for benchmarking industry performance where comparable data is available in the unlisted investment space.

AGIC has been working with both Federal and State governments to secure necessary funding to complete the development of the sustainability rating tool and the board believes this funding will be secured in the first half of 2010, with the development of the tool finalised by the end of 2010.

A senior CFSGAM representative from Infrastructure Investments gave a presentation to the annual AGIC conference on the benefits of the AGIC rating scheme to infrastructure asset owners and managers. The presentation focused on the need for the development of ESG key performance indicators within the infrastructure sector to allow performance benchmarking to be undertaken on a sector-by-sector basis.

Challenges to implementation

There remains a persistent misunderstanding by the broader market that ESG issues are socially responsible or ethical issues that are only of interest to a niche group of investors that want to invest in accordance with their moral or ethical beliefs. These investors believe that their investments may be compromised through a reduction in their investment universe or a preference towards environmentally friendly companies, rather than ones that will provide the best possible investment outcome. This isn't the case for the mainstream investment managers that have signed the PRI, yet the scope of ESG considerations is still not yet fully understood by the market.

Encouraging company stewardship in Asia

by David Gait, Senior Analyst, Global Emerging Markets

An offer document of 450 pages recently landed on the desk of Asian investors from an Asian company hoping to list. A cursory glance revealed a number of worrying corporate governance issues. The owners had previously been banned by the regulator from accessing the stock market for two years because of stock price manipulation. The company had 172 outstanding litigation cases covering 31 pages. There were significant conflicts of interest. There had been three different auditors in the past three years and, to cap it all, there were several serious environmental issues outstanding. In terms of corporate governance, it would have been hard to give it more than one out of ten. Yet far from scaring off investors, the issue was oversubscribed 39 times. For now at least, corporate governance is firmly off the radar screen of many Asian investors.

The contrast between East and West is noticeable. In the UK, the debate over corporate governance, the ownerless corporation and engagement has recently reached a crescendo. All institutional investors are to be subject to a ‘Stewardship Code’, which aims to improve the quality of engagement between shareholders and the companies they own. Unlike their Western counterparts, Asian markets are not dominated by ownerless corporations. Nonetheless, better stewardship is desperately needed in Asia too.

Good stewardship requires three simple guidelines. Most importantly, investors need to open their eyes. Too many still hide behind the excuse that information on governance, environmental or social performance is not available. This is not true. The information is there, albeit not always in the places one might expect to find it. As a useful rule of thumb, the greater the number of pictures of smiling children in the sustainability report, the greater the problems lurking beneath. Yet by far the best source remains the companies themselves. The ability of management teams to articulate convincingly their approach to corporate governance or environmental management is very revealing. They can also be a rich source of both positive and negative information on their peers. Reputation checks on owners, independent directors and auditors are usually easily done, while local NGOs provide invaluable insights. Elsewhere, there are often plenty of clues in the notes to the accounts, while flotation documents offer a once-in-a-corporate-lifetime glimpse at what are usually well-hidden skeletons.

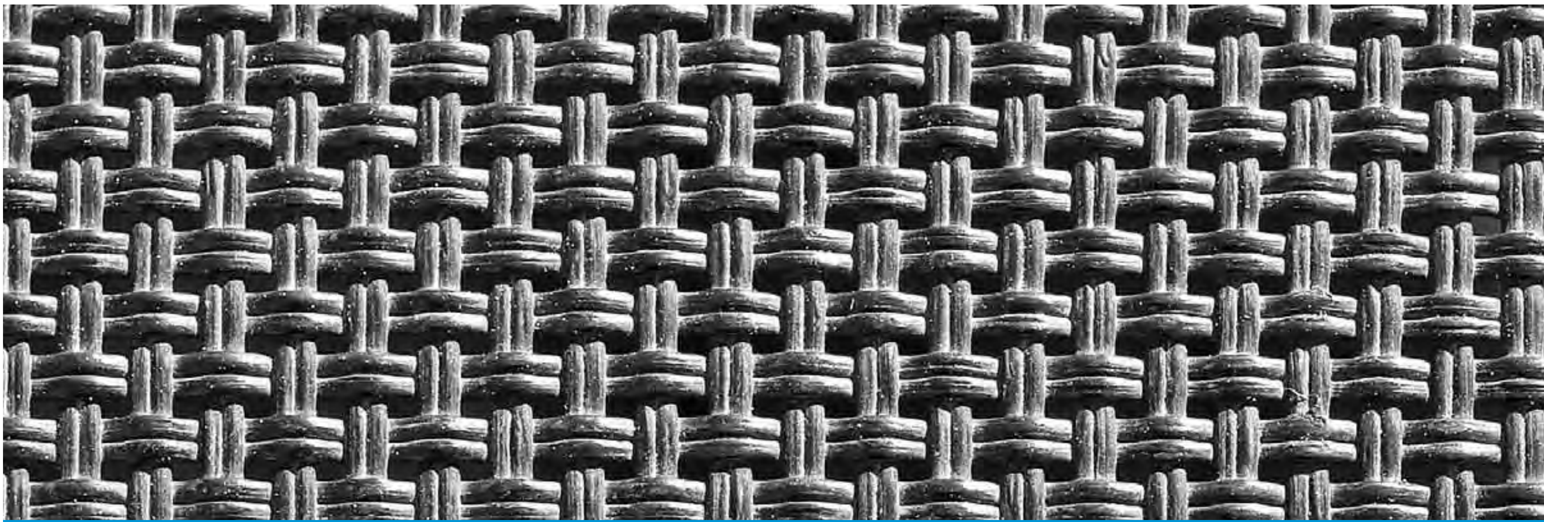
A second useful guideline is to recognise that there is no such thing as the perfect company. Having started to look, it is easy to get overwhelmed by the number of issues that appear, particularly where companies have multiple business divisions. India’s largest solar panel company still depends for most of its profits on coal-fired power generation. It also happens to manufacture the Pinaka multi-barrel rocket launcher system and the Akash medium range surface to air missile launcher.

Another Indian company recently released an annual report that stretched to over 1,200 pages. The company employs 75,000 people across 98 different business divisions. Even the CEO could be forgiven for not being able to name them all. In such cases, investors will never know the environmental performance of each division. They can, however, make a decent stab at assessing the corporate culture and senior management’s willingness and ability to address the most important sustainability challenges across the group. Stewardship comes in shades of grey. There needs to be tangible evidence of an improving trend, even if it is of the ‘two steps forward, one step back’ variety. Corporate culture matters. Management teams must be willing to admit their weaknesses and mistakes, and learn from them. Incentivisation schemes need to encourage a long-term mindset and focus on risks as well as rewards. Above all, when investors come across issues, they must engage with management.

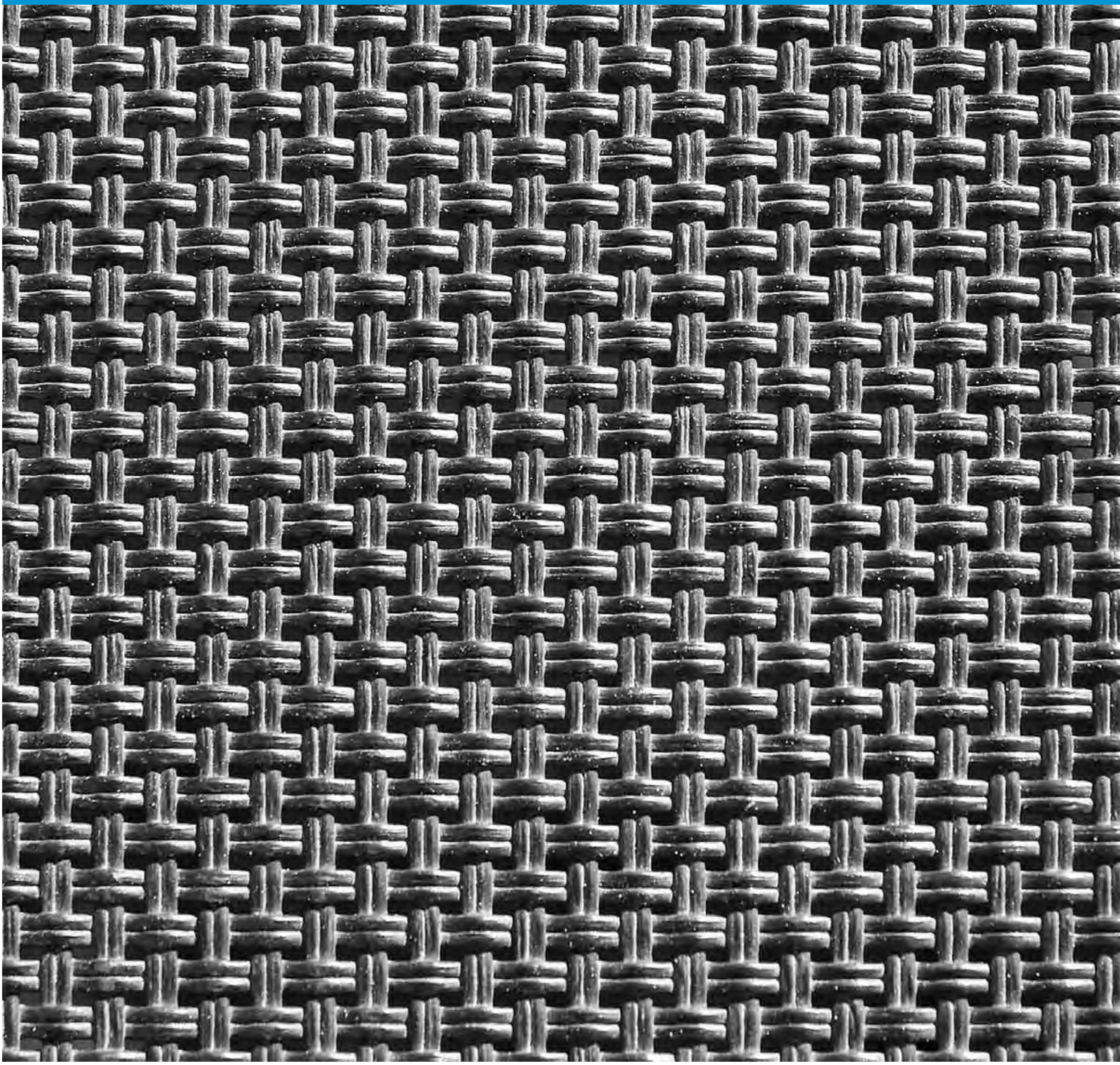
The third important guideline is to ensure this engagement is constructive, not destructive. Aggressive letters rarely, if ever, work. Nor do demands or ultimatums. Fortunately, Asian companies are remarkably open to suggestions. In the past month, the CEOs of two different Asian banks have approached investors directly for suggestions on how corporate governance can be improved. Work hard to build rapport. This can be as simple as writing thank you letters after meetings. The longer the time spent on the shareholder register the more productive the engagement becomes. Investors need to lean much more on independent directors for support. If confidence is lost in management’s ability to address the problem, agitate behind the scenes for a change in personnel. This is usually much more effective than waiting for a confrontational showdown at the next AGM.

Would an Asian stewardship code encourage investors to follow these simple guidelines? It seems unlikely. Over the past few years, investors have been asked to sign up to a proliferation of stewardship initiatives and their accompanying acronyms; ACGA, ASRIA, CDP, EITI, EMDP, FDI, ICGA, IGCA, WDP, UNPRI and so on. Their impact has been limited to date. Signing up is usually a fairly painless process and requires little follow through. For example, the Carbon Disclosure Project has 475 investors as signatories representing a combined $55 trillion of assets. Yet many responding Asian companies complain that they have yet to receive one question from investors on their carbon positioning.

Some investors have wondered if the introduction of policies such as delayed dividends, deferred voting rights and short-term capital gains taxes might not be more effective? A financial version of the Hippocratic Oath has even been suggested. Above all, good stewardship requires the right mindset. Buying a share means buying not only a piece of paper or electronic ticker, but part of a real business with all the rights and responsibilities that go with this. Get this right and everything else follows. Get this wrong and investment becomes little more than an elaborate game of speculation. And speculation and stewardship are not natural bedfellows.



Principle 5



"We will work together to enhance our effectiveness in implementing the Principles"

PRI action points	Reference
Support/participate in networks and information platforms to share tools, pool resources, and make use of investor reporting as a source of learning	26, 27, 28, 29, 30, 31
Collectively address relevant emerging issues	33
Develop or support appropriate collaborative initiatives	32, 34

In our approach to Principle 5 during 2009 we focused on communicating the business case for the PRI and promoted a deeper understanding of ESG issues through education in the industry. To this end, we participated in a number of engagement initiatives and associations during the period and contributed to the development of education programs to enhance the industry's effectiveness in implementing the PRI.

CFSGAM held several client briefings and worked closely with educational institutions to develop education materials and course content. We also participated in global collaborations, most notably through being a member of the Award Panel for the PRI Academic Network Research Awards. We believe this project was particularly important given the need to see rigorous academic research produced to support the investment industry in its approach towards responsible investment.

In 2009, our parent company, the Commonwealth Bank of Australia, joined the United Nations Environment Program Finance Initiative. This allowed us to become more involved in the relevant working groups and also gave us the opportunity to take a leadership role in Asia Pacific.

26. Asia outreach

Responsible investment in Asia was a focus for CFSGAM during the period. While we have been a member of the Asian Corporate Governance Association (ASGA) for some time, more investment professionals are now across the work of ASGA.

We worked closely with Responsible Research, based in Singapore, and jointly hosted a roundtable in Singapore in late 2009 on ESG integration. Speakers from RiskMetrics, Trucost, RepRisk, Responsible Research and Asia Sustainability Rating discussed options for integrating ESG screening and research into portfolio management. A representative from the PRI also discussed the PRI's plans to expand its reach into Asia.

We were also pleased to work with the PRI in some of the PRI briefings held across Asia in January 2009.

27. PRI Academic Network

During 2009, we participated as a member of the PRI Academic Network Steering Committee. The PRI Academic Network provides a link between responsible investment practitioners and the academic community. It aims to stimulate responsible investment research and provide multiple avenues for greater interaction between academia and practitioners. We participated in this initiative because we believe it is critical that the academic community contribute to the discussion and evolution of responsible investment. We are particularly interested in the finance faculty's role in facilitating the development of rigorous frameworks for the inclusion of ESG into modern portfolio theory and other financial frameworks.

28. The National Australian Built Environment Rating System

The National Australian Built Environment Rating System (NABERS) tool was developed by the NSW Government Department of Energy, Climate Change and Water (DECCW). CFSGAM has trialled and piloted the new tools developed by DECCW for Indoor Environment and Waste. In the case of NABERS Indoor Environment, we were able to assist in providing feedback and examples which helped DECCW to improve the tool for the property industry to adopt.

The NABERS Indoor Environment (IE) tool provides building managers, owners and occupants with a tangible understanding of the indoor environment quality of their office buildings in an operational sense, while providing the impetus and platform for improvements to be made.

As a leading asset manager that puts sustainability at the core of its practice, and with NABERS integral to the ongoing strategy for its properties, CFSGAM played a key role in the development of the NABERS IE tool from a grassroots level.

Our involvement with the new tool was a natural fit, with sustainability a critical component of our asset management strategy. Already, NABERS Energy and Water tools are used to monitor operational performance and set targets that ensure our entire portfolio minimises its operational impact on the environment. The group is also preparing to adopt the NABERS Shopping Centre tool.

NABERS IE is the only method by which CFSGAM can effectively measure its indoor environment performance, and its involvement in its development ensures the tool is relevant to the needs of building and portfolio owners. CFSGAM has already achieved three impressive ratings using NABERS IE.

In regard to the NABERS Waste tool, we have provided direct feedback and assistance from our consultants to DECCW to assist it in its understanding of the practical complications of the current tool and have offered further assistance to change the protocol to be a more practical and easily adopted tool for the property industry.

29. Every drop counts

CFSGAM participates in 'Every drop counts', which is a Sydney Water initiative to help businesses understand where and how water is used in their businesses, assess the true costs of water, improve their management of water and implement practical projects to save water. The program involves water management diagnostics, implementation of improvement plans, water efficiency audits and regular reviews to ensure ongoing improvement.

30. 1200 Buildings Partnership

The 1200 Buildings Partnership is a City of Melbourne initiative to achieve carbon neutrality by 2020 through the implementation of the Zero Net Emissions by 2020 strategy. The goal of the 1200 Buildings Partnership is to realise this vision by encouraging building owners to take part in environmental retrofits, as the commercial building sector is currently responsible for the majority of greenhouse gas emissions in the municipality, accounting for nearly half of total greenhouse gas emissions across the city of Melbourne. CFSGAM's buildings at 385 Bourke Street and 367 Collins Street are participating in the 1200 Buildings Partnership.

31. Sustainable Sydney 2030

'Sustainable Sydney 2030' is the City of Sydney's vision for the sustainable development of Sydney for the next 20 years and beyond. This sustainable development is not just about the physical environment, but also about the economy, society and cultures, and how addressing each will result in better outcomes now and for future communities.

As a major land and building owner in Sydney, CFSGAM has assisted in the development and implementation of the Sustainable Sydney 2030 plan. CFSGAM has been involved in discussions on green transformers and distributed renewable energy concepts.

32. 385 Bourke Street sustainability upgrade

The Commonwealth Property Office Fund's (CPA's) landmark building at 385 Bourke Street, Melbourne is undergoing a life cycle transformation to strategically future-proof the building through a comprehensive sustainability upgrade. The first stage of the upgrade in 2009 focused on a tune-up of maintenance and operational systems through the reduction of energy use, heating and cooling loads and water savings.

CPA has developed a memorandum of understanding with Sustainability Victoria and collaborated closely with the environmentally sustainable design consultant to produce a detailed scope and process for improving the sustainability of the building. The project team identified a number of works that would deliver improved efficiency and were able to utilise their financial, property management and technical skills to define a roadmap which could be utilised as a benchmark for the future redevelopment of other existing towers.

33. 2009 Investor Statement on the Urgent Need for a Global Agreement on Climate Change

CFSGAM supported the 2009 Investor Statement on the Urgent Need for a Global Agreement on Climate Change along with 190 other investment institutions, who together represent assets of more than $15 trillion.

The document sets out the perspective of institutional investors on climate change and the key elements of a global agreement that will drive the financial flows necessary to address climate change.

The Statement was produced by the Institutional Investors Group on Climate Change (IIGCC), the Investor Network on Climate Risk (INCR), the Investor Group on Climate Change/Australia and New Zealand (IGCC Australia/New Zealand) and the UNEP Finance Initiative (UNEP FI).

34. Collaborative initiatives

To support our implementation of the PRI, we participated in a number of collaborative initiatives. This collaboration helps us to stay abreast of developments in the sustainability and responsible investment arena more broadly, and also helps us to work with like-minded investors to facilitate ongoing improvements in the industry's approach to sustainability and responsible investment.

CFSGAM's Sustainability and Responsible Investment team members are well-regarded and active participants in their field and contribute their expertise to a number of third-party organisations, including:

ESG Research Australia
Board member

Chair of Evaluation Committee

Green Building Council of Australia
Board member

Investor Group on Climate Change
Management Committee Member, Deputy Chair, Member of the Property Working Group and Acting Chair

Property Council of Australia
Member of the National Sustainability Roundtable and Sustainable Development Committee Member

United Nations Environment Programme Finance Initiative
Co-Chair, Property Working Group

Chair, Asia Pacific Taskforce

Member of the Investment Commission

Board member

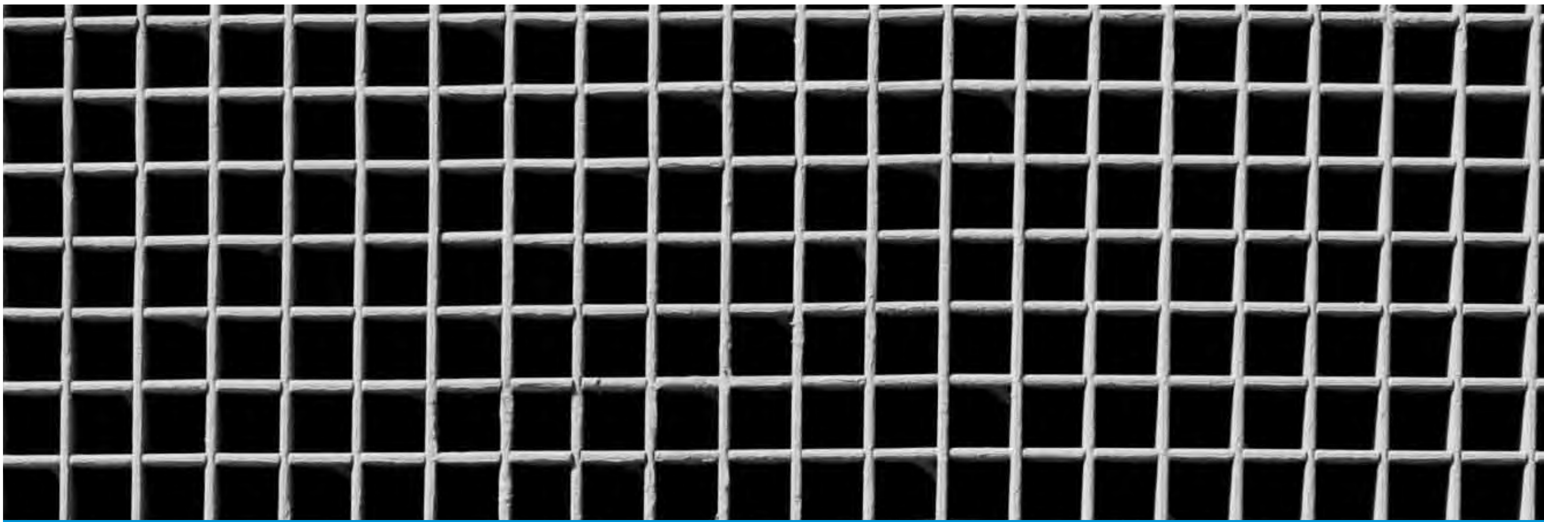
Member of the Asset Management Working Group

Other collaborative initiatives CFSGAM participated in include:

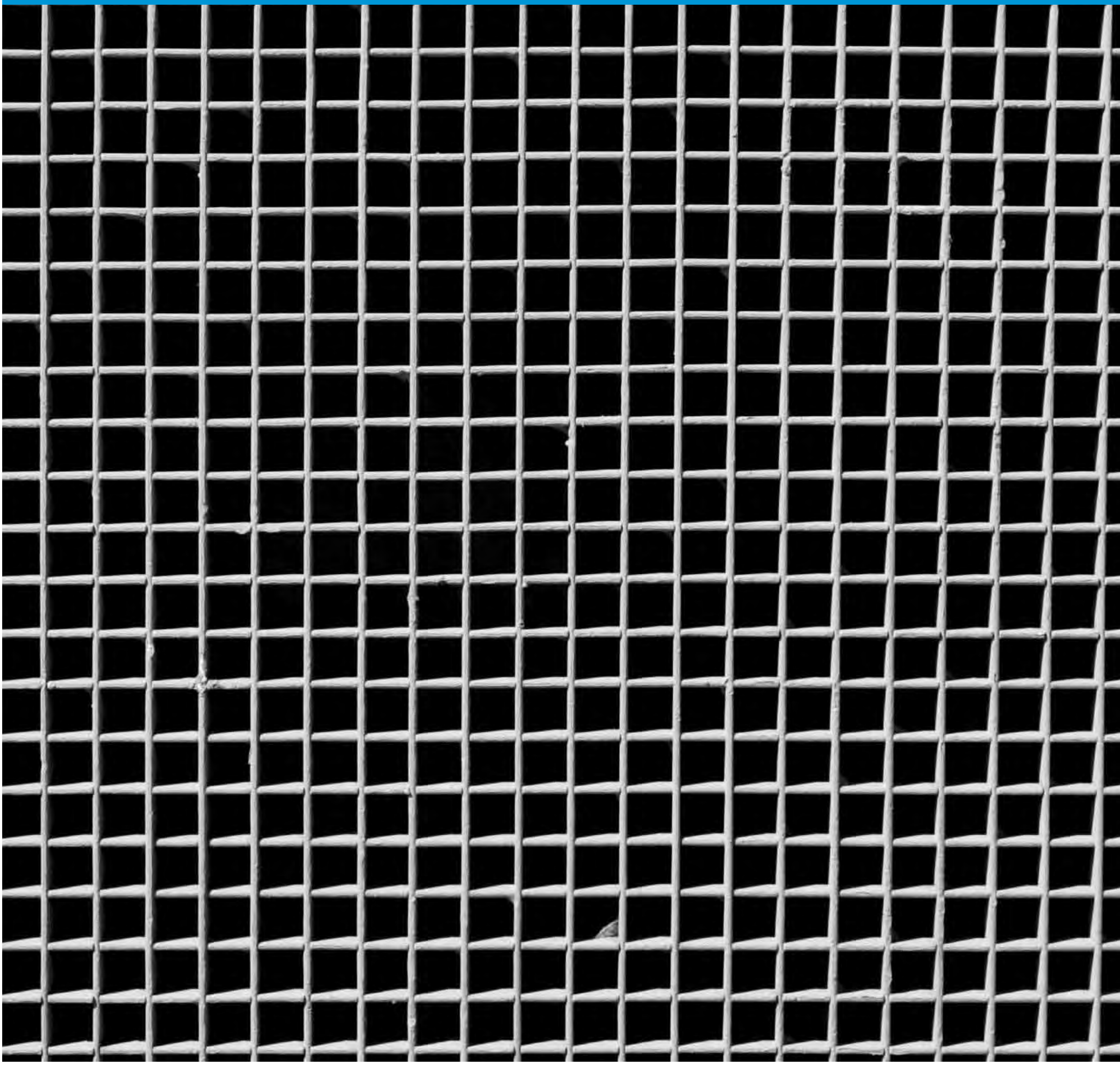
- Asian Corporate Governance Association
- Association for Sustainable & Responsible Investment in Asia
- Australian Council of Superannuation Investors
- Carbon Disclosure Project
- Extractive Industries Transparency Initiative International Corporate Governance Network
- Investment and Financial Services Association Carbon Markets and Climate Change Committee
- Regional social investment organisation – Association for Sustainable and Responsible Investment in Asia
- The Sydney Conference Advisory Committee of the International Corporate Governance Network, and
- UN Global Compact's 'Who Cares Wins' initiative.

Challenges to implementation

Definitional issues around the difference between mainstreaming ESG and ethical investing continue to make collaboration difficult at times because of the potential for misunderstanding or misalignment of desired outcomes. We actively emphasise the importance of distinguishing between socially responsible, or ethical, investing and the 'mainstreaming' of ESG considerations in our engagement and communications with stakeholders.



Principle 6



“We will each report on our activities and progress towards implementing the Principles”

PRI action points	Reference
Seek to determine the impact of the Principles	Governance, policy and strategy
Make use of reporting to raise awareness among a broader group of stakeholders	35
Disclose what is required of service providers in relation to the Principles	35
Report on progress and/or achievements relating to the Principles using a ‘Comply or Explain’ approach	35, 36, 37, 38
Disclose active share ownership policy	39
Communicate with beneficiaries about ESG issues and the Principles	40
Disclose how ESG issues are integrated within investment practices	41

We seek to be fully transparent in our approach to implementing the PRI. It is important to keep our stakeholders informed on our progress and we have undertaken a number of steps to raise awareness of our ESG initiatives. All current policies and reports are publicly available on our website, and mainstream communications now feature our approach to sustainability and responsible investments.

35. Responsible investment report

In 2009, we were pleased to announce the release of our second responsible investment report for the calendar year 1 January to 31 December 2008. In 2007 and 2008, CFSGAM was the only Australian fund manager to release a comprehensive PRI implementation report. We produce this report to encourage discussion with our stakeholders, increase awareness of challenges and opportunities and to provide transparency on our processes towards implementing the PRI.

36. Property sustainability reports

The Commonwealth Property Office Fund (CPA) and CFS Retail Property Trust (CFX) annual reports cover the sustainability initiatives taking place across CPA’s and CFX’s property portfolio. Both CPA and CFX report on how they have performed and the benefits to investors in undertaking sustainability and environmental initiatives.

The reports outline how the funds’ daily operations and approach to business help drive long-term sustainable value. The key philosophies underpinning the engagement in sustainability practices are consistent with CFSGAM’s membership of the PRI. The sustainability component of the report demonstrates how the funds have upheld the PRI and monitored its impacts on the environment and developed relationships with stakeholders.

In keeping with the move towards integrating ESG disclosure within annual financial reports, for the first time in 2009 CPA and CFX incorporated their ESG reporting into the annual report, rather than producing a standalone sustainability report. This is an important step towards the mainstreaming of ESG issues as they should not be viewed by investors in isolation from more traditional financial measures and reporting.

37. Direct Property Investment Fund sustainability report

The Direct Property Investment Fund (DPIF) released its second sustainability report to investors on the sustainability initiatives undertaken in the 2008-09 financial year and its plans for the future.

While this is only the second official report to investors on these activities, DPIF has been actively focused on managing ESG issues for many years.

DPIF is committed to promoting change within the industry and to facilitating further advances in sustainability initiatives not just within the fund’s portfolio, but by the broader property industry and its stakeholders. DPIF will continue to drive operating efficiencies within its properties, while increasing the focus on improving tenant engagement and fostering improved tenant/landlord partnerships.

38. Other property reporting

CFS Retail Property Trust (CFX) is a retail sector Australian Real Estate Investment Trust (A-REIT) which invests in high quality regional and sub-regional shopping centres across Australia. The trust listed on the Australian Securities Exchange in April 1994.

Commonwealth Property Office Fund (CPA) is an A-REIT which invests in prime quality office property located in central business districts and major suburban markets across Australia. The fund listed on the Australian Securities Exchange in April 1999.

Both CFX and CPA respond to the following initiatives.

Australian SAM Sustainability Index

Australian SAM Sustainability Index (AuSSI) tracks the performance of Australian companies that lead their industry in terms of corporate sustainability. Based on a thorough assessment of economic, environmental and social criteria, the AuSSI comprises the top sustainability driven companies from each of 21 industry clusters covering the entire Australian economy. CPA was recognised as the leader for the Real Estate Investment Trusts Cluster by AuSSI. CPA and CFX are both listed on the AuSSI.

Carbon Disclosure Project (CDP)

In 2009, CPA was recognised as a 'Climate Leader' by the CDP.

Dow Jones Sustainability Index

The Dow Jones Sustainability Index (DJSI) tracks the financial performance of the leading sustainability-driven companies worldwide. Currently, 70 DJSI licences are held by asset managers in 16 countries to manage a variety of financial products including active and passive funds, certificates and segregated accounts. CPA and CFX are listed on the DJSI.

Environmental Real Estate Index

CPA and CFX are listed on the Environmental Real Estate Index (EREI). This index measures the environmental performance of the commercial real estate sector globally. The EREI produced its inaugural report in 2009.

FTSE4Good Index

The FTSE4Good Index measures the performance of companies that meet globally recognised corporate responsibility standards and facilitates investment in those companies. Both CPA and CFX are listed on the FTSE4Good Index.

39. Corporate governance reporting updates

As one of Australia's largest asset managers, CFSGAM is an active representative of major shareholders in many Australian listed companies. We use our influence to encourage best practice corporate governance in the companies in which we invest and produce a regular report to provide an update on our corporate governance practices and activity. The corporate governance update outlines how we voted on key issues such as director elections/re-elections, executive remuneration and non-executive remuneration and provides case studies of engagement.

40. Investor communications

In 2009, there was a marked increase in focus on ESG issues and considerations in investor communications which reflects the importance that funds and investors now place on sustainability and responsible investment. A number of Requests for Information were completed specifically in relation to ESG practices and the PRI survey.

41. Responsible investment website

CFSGAM's responsible investment website includes information on our commitment to sustainability, links to all current policies and reports, latest news and research on sustainability and responsible investment in the business and profiles of the responsible investment team. CFSGAM's responsible investment website can be accessed at www.cfsgam.com.au/RI.aspx.

Looking ahead

We are committed to integrating ESG issues into our investment and asset management processes and have a long-term vision to be regarded as the leader in responsible investment and sustainability.

Priorities for 2010

Increase the level of sophistication with which the investment teams integrate ESG issues into research and portfolio construction.

During the past three years, there has been much progress in the quality of information produced for investors on ESG issues. In light of this, during 2009 we undertook a global review of the ESG research providers in the market and subsequently appointed Asset4, Responsible Research (Asian equities), RepRisk and Trucost (for emerging markets only). All these ESG research providers will help our investment teams further develop their ESG integration in a way that suits their investment process.

We will also continue to educate our investment teams about ESG issues. The most significant investment will be training all our investment teams how to effectively use Asset4. We will also undertake training of the Direct Infrastructure team in the application of the International Finance Corporation Environment, Health and Safety Guidelines along with broader ESG training. The Direct Infrastructure team have undertaken significant work over the last two years to ensure ESG issues are an integral part of their investment process and the training of the team will help deepen their understanding of these issues.

Increase the level of engagement with companies that represent a 'house view' on ESG issues, especially for the more controversial issues.

We are pleased to have appointed Nicholas Edgerton to the role of Manager ESG Research and Engagement. Nicholas will help our investment teams enhance their approach to engagement with listed companies.

We are also looking to increase the amount of collaborative engagement between our investment teams and better utilise our capacity as major shareholders to positively influence companies in their approach to ESG considerations.

To date our investment teams have each taken an autonomous approach to company engagement and this will continue to be the primary form of engagement. However, in future we will seek to be more collaborative in our approach to some of the more controversial issues across our markets and engage with companies accordingly.

Encourage service providers to produce more integrated ESG research that helps to demonstrate the materiality of ESG issues.

We will continue to work with our sell-side research providers to support them in their objective to increase the quality and usability of ESG research for our teams. We have experienced a positive response from the Australian sell-side brokers with the development of ESG Research Australia; however, we believe these efforts need to be sustained to achieve the best outcomes. Emerging markets is an area where we would like to see more ESG research and would particularly like to see the sell-side scrutinise ESG risks and opportunities of companies coming to market.

We also believe our approach to the PRI is supported by the pension fund industry. We were particularly pleased to see a greater level of detailed questions from pension funds on our approach to ESG and a greater level of support from this industry. While there is the ongoing challenge around the definitional issues of responsible investment, we believe the pension funds are getting more sophisticated in their support of mainstreaming a consideration of ESG issues into the investment process.

Glossary of terms and references

Association of Superannuation Funds of Australia (ASFA)
Australasian Investor Relations Association (AIRA)
Australian Council of Superannuation Investors (ACSI)
Australian Institute of Superannuation Trustees (AIST)
Australian Real Estate Investment Trust (A-REIT)
Australian SAM Sustainability Index (AuSSI)
Carbon Disclosure Project (CDP)
Carbon Pollution Reduction Scheme (CPRS)
CFS Retail Property Trust (CFX)
Commonwealth Property Office Fund (CPA)
Direct Property Investment Fund (DPIF)
Dow Jones Sustainability Index (DJSI)
Environmental, social and governance (ESG)
Financial Services Institute of Australasia (FINSIA)
FTSE4Good Index Series (FTSE4Good)
Global Reporting Initiative (GRI)
Green Building Council of Australia (GBCA)
Investment and Financial Services Association (IFSA)
Investor Group on Climate Change (IGCC)
National Australian Built Environment Rating System (NABERS)
Responsible Investment Association (RIA)
United Nations Principles for Responsible Investment (PRI)

Carbon Disclosure Project
cdproject.net

CFSGAM responsible investment website
cfsgam.com.au/RI.aspx

Investor Group on Climate Change
igcc.org.au

UNEP Finance Initiative
http://www.unepfi.org/

UN Principles for Responsible Investment
www.unpri.org

Further information

For further information about CFSGAM's commitment to the PRI and ESG activities, please visit cfsgam.com.au/RI .aspx or contact one of the regional representatives below.

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