



Desalination plant disappears into murky Off Balance Sheet Waters

December 2024

About KIT, KIFM and Keppel

KEPPEL INFRASTRUCTURE TRUST (KIT) is an infrastructure trust listed in Singapore. KIT is managed by Keppel Infrastructure Fund Management Pte Ltd (KIFM) and is sponsored by Keppel, a global asset manager and operator. KIFM is a wholly-owned subsidiary of Keppel.

The Trustee-Manager, KIFM, has dual responsibility of safeguarding the interests of KIT Unitholders, and managing the business conducted by KIT. The Trustee-Manager has general powers of management over the business and the assets of KIT and its main responsibility is to manage KIT's assets and liabilities for the benefit of Unitholders as a whole.

REPORT OBJECTIVE

KIT's proposed acquisition of 50% equity interest in Marina East Water Pte Ltd (MEW) from Keppel Infrastructure Holdings Pte Ltd (KIHPL), its sponsor, raises questions on Corporate Governance and deal structure. Will it truly be DPU accretive to KIT unitholders? Are there other factors driving this deal? Are the reasons for 5 out of 7 board members abstaining from recommending this transaction valid and fair? CML explores in this brief discussion.

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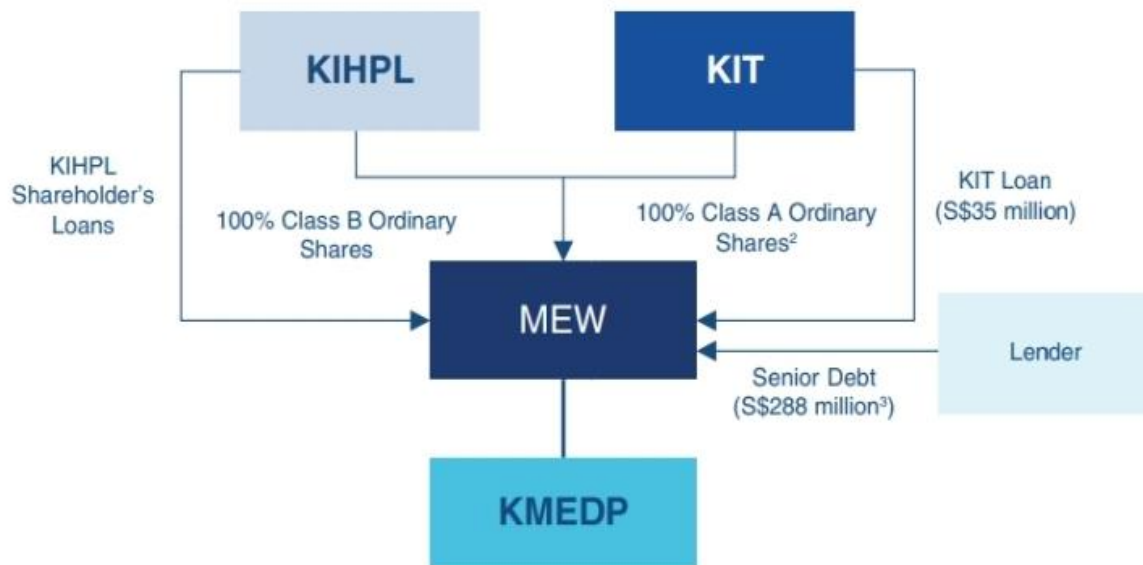
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Nov 2024: Keppel proposes to sell Singapore's 4th Desalination Plant to KIT

Transaction Overview

- Proposed acquisition of 50% equity interest in Marina East Water Pte. Ltd. ("MEW") which owns Keppel Marina East Desalination Plant ("KMEDP"). The enterprise value of MEW is approximately S\$323 million.
- Following completion, Keppel Infrastructure Holdings Pte. Ltd. ("KIHPL") and KIT will each hold a 50% joint-controlling equity interest in MEW, with KIT receiving the entire economic benefit from MEW.
- On 25 April 2022, MEW had drawn down S\$315.0 million on a term loan facility¹, which has since commenced amortisation. As at the Latest Practicable Date, S\$288.2 million remains outstanding on the facility. At completion, KIT will extend a non-interest bearing shareholder's loan of S\$35.0 million to MEW.

Overview of Post-Completion Transaction Structure



Salient features of the structure

- KIT and KIHPL will each hold 50% equity interest in MEW although KIT will be entitled to 100% of the economic benefits of MEW
- Per Circular, the joint controlling shareholder structure ensures that the interests and obligations of KIT and KIHPL regarding the operation of KMEDP are aligned, while ensuring KIT is entitled to the entire economic benefit from MEW.
- Other shareholder rights and board representation are generally similar for both classes of shares.
- On 25 April 2022, MEW had drawn down S\$315.0 million on a term loan facility, which has since commenced amortisation. As at the Latest Practicable Date, \$288.2M remains outstanding on the facility.
- KIT, in the response to shareholders' questions, confirmed that KIT will not consolidate the enterprise value of \$323M relating to the interest in MEW. As KIT and KIHPL have joint control of MEW, the investment will be equity-accounted.

A complex structure for a single asset purchase?

CML's Question to KIT:

Why would KIT not simply raise equity and debt to buy this asset? Why use a complicated transaction structure?

KIT's Reply:

The joint-controlling shareholder structure and the continued provision of O&M services by a wholly-owned subsidiary of KIHPL ensures that the interests of KIT and KIHPL regarding the operation of KMEDP are aligned, ensures the operational stability of KMEDP and allows MEW to benefit from the proven water services and diverse operating capabilities of KIT's sponsor KIHPL.

- 1. Since KIHPL will gain much more from providing O&M services to MEW than the \$2 investment, there is no alignment.**
- 2. If this is a 50:50 shareholding between KIT and KIHPL, why is KIT the only shareholder extending the shareholder loan of \$35M?**
- 3. With 50% shareholding interests and yet no economic interest, what is the commercial substance of this transaction for KIHPL?**
- 4. Is KIT not able to access debt independently, hence resorting to such deal structure to keep the \$288M loan?**



Off Balance Sheet effects of the transaction

- With this transaction structure, MEW will become an unconsolidated entity for both Keppel and KIT, with the important implication being its outstanding debt of \$288M will now be deconsolidated from Keppel's financial statements. CML noted that Keppel's gearing has been increasing in recent years.
- KIT will also similarly not reflect these debts on their financial statements. The proforma gearing of KIT increased only marginally even though the debt of MEW stands at \$288M. Without providing further analysis of KIT's ability to service the increased debt, this transaction could introduce undue financial risk to KIT.

**Has KIT become Keppel's off-balance sheet vehicle?
Is there real commercial substance to this proposed shareholding structure?**

Is this transaction truly DPU accretive to KIT unitholders?

- KIT is required to extend a non-interest bearing shareholders' loan of \$35M to MEW, which is unsecured and with no fixed terms of repayment. With no guarantee of recovering its upfront investment of \$35M, how is this beneficial to KIT's unitholders?
- Funds from Operation (FFO) from MEW is S\$10.5m for 2023. However, Distribution Income for KIT will only increase by \$0.6M (0.01 Singapore cents multiply by 6B Units). This means that substantial portion of the FFO is used for repayment of loan principal relating to MEW loan facility. If FFO from MEW were to decrease in certain years, will there be enough funds for servicing of MEW loan facility?
- Yearly Distribution Income from MEW of \$600k is highly uncertain as it can be easily wiped out in years when there is a drop in FFO. With 20 years remaining on the concession period, without significant increase in FFO in future years, total Distribution Income adds up to only \$12M. Compared against KIT's initial investment of \$35M, how can this transaction be considered DPU accretive to KIT shareholders?

CML calls on KIT to provide clear, sufficient and substantive information on how the Board and the Trustee-Manager are satisfied that this transaction is in the best interest of the unitholders and for the benefit of the beneficiaries of the trust and not to the detriment of unitholders of the business trust.

What is the ARC and Board recommending to Unit Holders?

At the date of the circular, Directors of Keppel Infrastructure Fund Management Pte Ltd, as trustee-manager of KIT, consists of the following:

- Daniel Cuthbert Ee Hock Huat, Board Chairman and ARC Member
- Mark Andrew Yeo Kah Chong, also ARC Chairman
- Chong Suk Shien
- Adrian Chan Pengee, also ARC Member
- Ng Kin Sze
- Khor Poh Hwa
- Christina Tan

Other than Christina Tan, all other directors (that is, 6 out of 7 Directors) were considered Independent Directors by KIT.

Despite having 6 Independent Directors, only 2 directors were involved in making the recommendation on the transaction to the Unit Holders. Majority of the Board Members are abstaining from making their recommendation to the Unit Holders. CML examines the reasons for directors abstaining from making their recommendations.

Only 1 out of 3 ARC members made the recommendation with 2 abstaining

6. STATEMENT OF THE AUDIT AND RISK COMMITTEE

The Audit and Risk Committee (with Mr Daniel Cuthbert Ee Hock Huat and Mr Adrian Chan Pengee abstaining as each of them is a director of certain subsidiaries of Temasek), having reviewed, among other things, the terms and rationale for the Proposed Acquisition, and after considering the advice of the IFA as set out in **Appendix A** to this Circular, concurs with the IFA and is of the opinion that the Proposed Acquisition is on normal commercial terms and is not prejudicial to the interests of KIT and its minority Unitholders.

11. DIRECTORS' RECOMMENDATION

Having considered the relevant factors, including the rationale for the Proposed Acquisition, the Directors (save for Mr Daniel Cuthbert Ee Hock Huat, Mr Adrian Chan Pengee, Mr Ng Kin Sze, Ms Christina Tan Hua Mui and Mr Khor Poh Hwa, all of whom are not making a recommendation in respect of the Proposed Acquisition for the reasons set out in **Section 10 of this Circular**) are of the opinion that the Proposed Acquisition is in the best interests of KIT. Accordingly, the Directors (save for Mr Daniel Cuthbert Ee Hock Huat, Mr Adrian

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See Section 10 on page 5 of this report

Only 2 out of 7 Board members made the recommendation with 5 abstaining

Chan Pengee, Mr Ng Kin Sze, Ms Christina Tan Hua Mui and Mr Khor Poh Hwa) recommend that Unitholders vote in favour of the Ordinary Resolution in respect of the Proposed Acquisition.



Are the reasons for abstention valid?

10. ABSTENTION FROM VOTING

By virtue of their interest in the Proposed Acquisition, each of KIHPL, Keppel, Temasek and the Temasek Entities will abstain and have undertaken to ensure that their respective Associates will abstain from voting on the Ordinary Resolution in respect of the Proposed Acquisition. Each of KIHPL, Keppel, Temasek and the Temasek Entities will also decline to accept appointment as proxy for any Unitholder to vote on the Ordinary Resolution in respect of the Proposed Acquisition unless that Unitholder concerned shall have given specific instructions in his Proxy Form as to the manner in which his votes are to be cast in respect of the Ordinary Resolution in respect of the Proposed Acquisition. Please refer to Section 8.2 of this Circular for the relevant Substantial Unitholders' direct or deemed interests in the Units.

Mr Daniel Cuthbert Ee Hock Huat is a director of a subsidiary of Temasek and an investment committee member of certain subsidiaries of KCH. Mr Adrian Chan Pengee is a director of certain subsidiaries of Temasek. Mr Ng Kin Sze is a private equity advisor to a subsidiary of Temasek and an investment committee member of certain subsidiaries of KCH. Ms Christina Tan Hua Mui is the Chief Executive Officer, Fund Management and Chief Investment Officer of Keppel, and a director of several other subsidiaries of Keppel. Mr Khor Poh Hwa is a non-executive director of two associated companies of Keppel.

Accordingly, each of Mr Daniel Cuthbert Ee Hock Huat, Mr Adrian Chan Pengee, Mr Ng Kin Sze, Ms Christina Tan Hua Mui, Mr Khor Poh Hwa and their respective Associates will abstain from voting on the Ordinary Resolution in respect of the Proposed Acquisition, and will also decline to accept appointment as proxy for any Unitholder to vote on the Ordinary Resolution in respect of the Proposed Acquisition unless that Unitholder concerned shall have given specific instructions in his Proxy Form as to the manner in which his votes are to be cast in respect of the Ordinary Resolution in respect of the Proposed Acquisition.

Save for the foregoing, the Trustee-Manager will disregard any votes cast at the EGM on the Ordinary Resolution in respect of the Proposed Acquisition by Mr Daniel Cuthbert Ee Hock Huat, Mr Adrian Chan Pengee, Mr Ng Kin Sze, Ms Christina Tan Hua Mui, Mr Khor Poh Hwa and their respective Associates. Please refer to Section 8.1 of this Circular for the relevant Directors' direct or deemed interests in the Units as at Latest Practicable Date.

Save as disclosed in this Circular, none of the Directors or Controlling Unitholders have any direct or indirect interest in the Proposed Acquisition.

CML Observations

- The directors abstained from recommending the acquisition primarily because of their roles as directors in other Temasek subsidiaries or subsidiaries/associated companies related to Keppel.
- Interestingly, since Keppel is the sponsor for KIT and often transfers its cash-generating assets into the Business Trust, wouldn't such MEW transactions be considered routine or normal? Given that Keppel is a Temasek-related company, if these directors abstain from making recommendations due to their appointments at Temasek subsidiaries, does this imply they would never evaluate any deals from Keppel? If so, does this fulfill their role as Directors of the Trustee-Manager?
- If these directors believe they should abstain from such deals, CML questions how they should consider themselves as independent directors of KIFM.
- CML evaluates the above observations against other REIT transactions with their Trustee Manager such as Mapletree Logistics Trust and Keppel REIT. None of the directors in these 2 trusts considered themselves conflicted in making a recommendation to their Unit Holders even though a number of their directors were also directors of other Temasek related entities.

Is the Board of the Trustee Manager constituted correctly when they are unable to recommend deals from Keppel? Are these directors truly independent then?

Comparison with MLT and Keppel REIT

Mapletree Logistics Trust - Proposed Acquisition of Logistics Assets from Mapletree; Circular Dated January 2022

11. RECOMMENDATION

11.1 The Proposed Acquisitions

Based on the opinion of the IFA (as set out in the IFA Letter in **Appendix E** of this Circular) and the rationale for and key benefits of the Acquisitions as set out in **Paragraph 4** of this Circular above, the Independent Directors and the Audit and Risk Committee believe that the Acquisitions (including the Income Support) are on normal commercial terms and are not prejudicial to the interests of MLT and its minority Unitholders.

Accordingly, the Independent Directors recommend that Unitholders vote at the EGM in favour of the resolution to approve the Acquisitions.

KEPPEL REIT - Proposed Acquisition of Keppel Bay Tower; Circular Dated 29 January 2021

9. RECOMMENDATION

Based on the opinion of the IFA (as set out in the IFA Letter in **Appendix D** of this Circular) and the rationale for and key benefits of the Acquisition as set out in Paragraph 3 above, the Independent Directors and the Audit and Risk Committee believe that the Acquisition is on normal commercial terms, and is not prejudicial to the interests of Keppel REIT and its minority Unitholders.

Accordingly, the Independent Directors and the Audit and Risk Committee recommend that Unitholders vote at the EGM in favour of the Resolution relating to the Acquisition.

No Abstention from Any Independent Directors and Audit and Risk Committee

Does KIT's Trustee Manager, KIFM, have a higher or lower bar for governance - a closer look at the Independent Chairman and the views of the Nominating Committee



DANIEL CUTHBERT EE HOCK HUAT, 71

Non-Executive Chairman and Independent Director

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Date of first appointment as a director:
18 May 2015

Length of service as a director (as at 31 December 2023):
8 years 7 months

Board Committee(s) served on:
Nominating and Remuneration Committee (Chairman);
Audit and Risk Committee (Member);
Investment Committee (Member)

Academic & Professional Qualification(s):
Bachelor of Science (Systems Engineering) (First Class Honours), University of Bath, UK;
Master of Science (Industrial Engineering), National University of Singapore

Present Directorships (as at 1 January 2024):
Listed entities
Keppel Infrastructure Fund Management Pte. Ltd. (the Trustee-Manager of Keppel Infrastructure Trust);
Olive Tree Estates Limited;
Capitaland Ascendas REIT Management Limited (the Manager of Capitaland Ascendas REIT)

Other principal directorships
Singapore Mediation Centre

Major Appointments (other than directorships):
Investment Committee Member,
Keppel Asia Infra Fund (GP) Pte. Ltd. and
Keppel Asia Infra Fund II (GP) Pte. Ltd.

Past Directorships held over the preceding 5 years (from 1 January 2019 to 31 December 2023):
Nil

Others:
Nil

Taking into account the views of the NRC, the Board has determined that:

- a. although Mr Daniel Cuthbert Ee Hock Huat is strictly not considered to be independent from Temasek and Keppel, a deemed substantial shareholder of the Trustee-Manager according to the BTR, nonetheless, the Board considers that Mr Ee is an independent Director. Mr Ee is a director of Capitaland Ascendas REIT Management Limited (Ascendas), a subsidiary of Temasek. In addition, Mr Ee is also an investment committee member of Keppel Asia Infra Fund (GP) Pte. Ltd. (KAIF) and Keppel Asia Infra Fund II (GP) Pte. Ltd., (KAIF II, and together with KAIF, the KAIF Entities), each of which is a wholly-owned indirect subsidiary of Keppel Capital. After review, the Board is satisfied that the above relationship will not interfere with Mr Ee's independent judgment and ability to act with regard to the interests of all the Unitholders as a whole. The Board reached

its conclusion on the basis that (i) Mr Ee is an independent non-executive director of Ascendas and his investment committee member roles on the KAIF Entities are independent non-executive roles, (ii) Mr Ee serves on the Board in his personal capacity, not as Temasek's and/or Keppel Capital's representative, (iii) Mr Ee is not an employee of Temasek and/or Keppel Capital and he has declared he does not act in accordance with the instructions of Temasek and/or Keppel Capital, and (iv) Mr Ee has declared that he does not derive any compensation from Ascendas, Temasek and/or Keppel Capital other than remuneration received for his service as a director of Ascendas and as an investment committee member of the KAIF Entities. Mr Ee has also consistently shown independent judgment in his deliberation of the interests of KIT. Mr Ee's participation in the Board will benefit KIT given his expertise. Mr Ee will however, abstain from the Board's decisions in relation to any matter which involves Temasek, Keppel Capital and its subsidiaries.

Similar playbook is seen in assessing the independence of Adrian Chan and Ng Kin Sze

A closer look at the Investment Committee which is tasked to evaluate investments, acquisitions and/or disposals:

Composition of Investment Committee

Ms Christina Tan – Non-independent Director
Mr Danial Cuthbert Ee Hock Huat, Independent Director
Ng Kin Sze, Independent Director

As this proposed acquisition with MEW involves Keppel, all 3 are conflicted and do not vote on the transaction. Would they have also recused themselves from any discussion relating to the transaction?

So, who is evaluating this transaction and recommending to the Board which in turn recommends to the Unit Holders?

Corporate governance of KIFM raises serious questions on the effective oversight of this transaction

In the corporate governance section of KIT's FY2023 annual report, 3 of the 5 independent directors (Daniel Ee, Ng Kin Sze and Adrian Chan) were not strictly considered independent of Keppel and/or Temasek, but the Board still considered each to be independent. Since then, Khor Poh Hwa has been appointed and he is a non-executive director of two associated companies of Keppel, and is therefore in the same situation as the 3 abovementioned independent directors.

Further, Daniel Ee and another independent director, Mark Andrew Yeo Kah Chong, who is also ARC Chairman, were independent Chairman and independent director respectively of Cityspring Infrastructure Trust (CIT) since 2010 or earlier. CIT was merged with KIT. Therefore, they have been independent directors of KIT and its predecessor entity for well over the tenure limit of 9 years for independent directors of business trusts.

The decision to deem the above directors as independent by relying on the flexibility accorded by the rules is disappointing, particularly as 6 out of the 7 directors on the board opining on the independence of the independent directors are either not classified as an independent director or have relationships or circumstances that raise concerns about their independence.

KIFM's Investment Committee in the board is chaired by Christina Tan, the sole non-executive non-independent director. The other two members are Daniel Ee and Ng Kin Sze, who are strictly not independent but only deemed to be independent by the board. The present transaction would be expected to have been recommended by the Investment Committee. How was this committee involved since none of the directors on this committee are recommending this transaction to unitholders?

CML VIEWS What should KIFM have done?

- **KIFM should set a high bar in determining the independence of the directors.**
- **Independent directors of KIFM should not have any other relationships with any other Keppel subsidiaries / associated companies**
- **For directors who may be directors of other Temasek related entities, they should not abstain from making recommendations so long as those entities have no conflict with the transaction in question.**

In our view, the corporate governance of KIFM raises serious questions on the effective oversight of this transaction. KIFM appears to have low bar in assessing the independence of the Board and a “high bar” in managing conflicts of interests where they choose to abstain when real work is needed, leaving UnitHolders on their own in evaluating such complex deals