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MSRB's ESG Request for Information Begins to Collect Submissions.

Responses to the Municipal Securities Rulemaking Board's request for information on environmental social and governance factors are beginning to show some indication of the challenges regulators face in responding to the growing interest in ESG investing.

Responses to the MSRB's December RFC so far have generally agreed that standardized ESG disclosures would add quite the workload for issuers, as was identified in the Government Finance Officers Associations best practices.

"When you mention ESG there's probably four different directions you can go with that and that's a challenge I think the market has," said Dave Erdman, capital finance director for the State of Wisconsin.

Many of these concerns were mentioned during GFOA's winter meeting, as many have remarked how broad ESG disclosures can be and how burdensome they may become should the MSRB or others decide they are necessary.

"It is not that issuers do not want to report ESG factors, but for many there are so many approaches which creates disorientation and questions about what is material or important," said Dan Aschenbach, principal consulting partner at AGVP Advisory in his submission.

Some issuers are already beginning to submit responses on what kind of disclosures make sense for them.

"Voluntary disclosures make the most sense for the municipal market," the City of Detroit said in its response, the only issuer to submit so far. "We agree with the GFOA guidance that standardized ESG disclosures would be overly burdensome, costly, and potentially inhibiting for municipal issuers who could decide not to use ESG designations they deserve to avoid the added cost and effort."

But the matter of disclosure becomes slightly more complicated as it relates to the issuance of social bonds.

The City of Detroit issued $175 million in 2021 in social bond designation "based on the intended use of the bonds for the financing of blight removal purposes," the submission said.

The City's Social Bonds Designation follows the "Social Bond Principles," as promulgated by the International Capital Market Association, updated most recently in June 2020.

"The proceeds of the bonds are funding projects consistent with a number of these categories, including affordable housing, employment generation and socioeconomic advancement and improvement, which is expected to benefit certain of the target population included by the ICMA in the Social Bond Principles," the city said.

The City of Detroit decided to use ICMA standards saying they were “clear, easy to follow and fit our purpose.” The issuer also did not consider using a third-party vendor to certify the bonds as they “did not feel doing so would add any value or be a good use of money.”

Detroit also intends to disclose annually with EMMA on the spending of those bonds with the Social Bond designation, despite it not being required by the City. They also indicated the potential disparities that may arise from a dependence on ESG data vendors.

“Vendors that certify ESG Municipal Securities could cause a disparity in markets because small issuers may not be able to afford their services,” the submission said. “Such certification essentially price out issuers who would otherwise sell ESG bonds.”

The MSRB is also being asked to consider the matter of “greenwashing,” which the Securities and Exchange Commission is expected to address this year. Greenwashing refers to a misleading labeling of something as environmentally sound.

“Self-certification or examination in the private sector resulted in ‘greenwashing’ and now there are calls for disclosure regulation on what gets published,” AGVP?s Aschenbach said in his submission.

“The question remains in the private sector on what is material and relevant,” he added. “The municipal bond sector should recognize the potential for ‘municipal greenwashing’ and with limited municipal staff, understand the strain on ESG self-reporting.”

In the City of Detroit?s view, ESG considerations are very different in the corporate and public sectors and further guidance should reflect that.

“ESG considerations in the corporate sector are very different than in the public sector, and the type and frequency of disclosures should not be the same,” the City of Detroit submission said. “The vast majority of municipal bonds clearly serve an ESG purpose; whereas the vast majority of corporate bonds do not.”

“Corporate issuers who seek to use an ESG designation should be required to meet certain disclosure requirements, which are unnecessary for municipal issuers given the fundamental public purpose that municipal bonds serve by definition,” the City of Detroit said.

Other submissions seek to address how one might seek to address historic ills in the financial system with the use of ESG designated bonds.

“An investor seeking to identify bonds that explicitly created racial and social equity, how would she do so?” said Joyce Coffee, president and founder of Climate Resilience Consulting in her submission. “The S in ESG frequently identifies projects that improve health, education or workforce outcomes,” she added. “However, these outcomes could be ascribed to any demographic.”

The MSRB is collecting responses until March 8.

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