Bond Case Briefs

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Why Buy Municipal Bonds if the World Is Ending?

States and cities seem much less sure about climate change in their disclosures than in their lawsuits against energy companies.

From electric vehicle initial public offerings to environmental, social and governance funds, opportunities in climate-related investments appear endless. Yet a troubling trend is emerging involving state and local governments' general-obligation bonds and their judicial climate activism. The same jurisdictions that are suing energy companies for alleged climate-change damages are also stating in their own bond disclosures that they can't attest to the effects of climate change.

New Jersey became the latest plaintiff with a new lawsuit on Oct. 18. But New Jersey's most recent GO bond offering indicates the state can't account for climate risk having a material effect. According to its bond disclosure, the state warrants that it "cannot predict the impact that these climate events may have on its financial condition."

New Jersey reverses its position with specific language in its legal complaint. Among many allegations, the state claims that "oceans are acidifying at an alarming rate because of fossil-fuel burning, endangering New Jersey's coastal ecosystems and economy." An especially shrill line reads, "As a result of the fossil fuel industry's lies and deceit, the State has paid billions of dollars to clean up climate change-induced disasters like Superstorm Sandy."

The disclosure for the city and county of Honolulu GO Bond Series 2022A states: "No assurances can be given as to the frequency or severity of any future natural disasters, nor what impact, individually or in the aggregate, such disasters may have on the State, the City and County, their residents or their overall financial condition." But Honolulu and its Board of Water Supply filed a state court case in 2020 with allegations that specifically contradict this uncertainty. According to the lawsuit, the "defendants' individual and collective conduct is a substantial factor in causing global warming and consequent sea level rise and attendant flooding, erosion, and beach loss in the City."

San Francisco, one of the earliest plaintiffs to file suit, asserted on issuing its GO Refunding Bonds Series 2022-R1: "The scientific understanding of climate change and its effects continues to evolve. Accordingly, the City is unable to forecast when . . . adverse effects of climate change . . . will occur. In particular, the City cannot predict the timing or precise magnitude of adverse economic effects . . . during the term of the Bonds," which mature after 12 years.

That's contrary to what San Francisco stated in court in 2017. The case asks the court to order energy companies to pay for sea walls and other infrastructure because the city faced "imminent risk of catastrophic storm surge flooding." In addition, the city claimed, the defendants' "production will intensify future warming and San Francisco's injuries from sea level rise."

Baltimore's GO bond disclosure asserts that the city adopted a Disaster Preparedness and Planning Project. The city admits that "due to the uncertainty of climate conditions, and thus of relative sea level rise projections, it can be difficult to assign quantitative probabilities to projections of sea level increases." If it is difficult to assign probabilities to such sea level increases, then on what grounds did the city file a 2018 lawsuit against 26 energy companies with differing claims? Baltimore's complaint specifically alleges "the City has already incurred, and will foreseeably continue to incur, injuries, and damages due to anthropogenic global warming, including sea level rise."

In neighboring Annapolis, the city's disclosure doesn't highlight any dire reports of past climate-related injuries or threats. The bond offering's only reference to climate notes "city management is also developing a plan to make Annapolis resilient against the effects of climate change and other factors by joining Anne Arundel County's efforts to establish a Resiliency Authority." So why sue 26 energy companies in February 2021 for the costs and consequence of past climate damages? The lawsuit alleges that "as actual and proximate results of Defendants' conduct, which caused . . . environmental changes"—tidal flooding in Annapolis—"the City has suffered and will continue to suffer severe harms and losses."

Even a novice investor can see that the information contained in these bond disclosures directly contradicts the premise of the issuers' legal claims. In light of the above contradictions, these lawsuits are unfounded. At the same time, officials issuing these bonds should be transparent in acknowledging such discrepancies. They'd be well served by not only distancing themselves from the cases, but also urging their withdrawal. This flawed legal strategy doesn't help the climate. It's a disservice to muni investors and the residents of these states and cities.

The Wall Street Journal

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Nov. 2, 2022

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