



March 7, 2022

Mr. Ronald Smith, Corporate Secretary
Municipal Securities Rulemaking Board (MSRB)
1300 I Street NW, Suite 1000
Washington, DC 20005

Re: MSRB Notice 2021-17: Request for Information on Environmental, Social and Governance (ESG) Practices in the Municipal Securities Market

Dear Mr. Smith,

pfm

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PFM Financial Advisors, LLC (“PFM”) welcomes the opportunity to submit comments in response to the Request for Information on Environmental, Social and Governance (ESG) Practices in the Municipal Securities Market (the “Request for Information”) issued by the Municipal Security Rulemaking Board (the MSRB). In 2021, PFM was the nation’s leading independent municipal advisor, having advised on 935 bond transactions with a total par amount over \$67 billion, according to Ipreo. Our municipal market presence gives us a broad, national perspective on the municipal market on behalf of our municipal advisory activities and the municipal entities and obligated persons we serve. We have a long-standing commitment to working in the public interest, as well as promoting environmental sustainability, and we are actively engaging in ESG considerations with our clients and other market participants.

While PFM understands and appreciates the MSRB’s desire for marketplace clarity and uniformity, PFM does not believe that action is required of the MSRB at this time for ESG-labeled bonds nor ESG-related disclosure considerations. PFM believes that a variety of market-based initiatives (e.g., voluntary standards, rating agencies, private vendor ESG certification services, GFOA) are appropriately guiding and directing the evolution of this market. In our observation, issuers are by-and-large responding, as appropriate, to these initiatives. And, PFM observes no widespread and material distinction in investor interest in bonds (or the pricing of bonds) due to ESG-related disclosure considerations. Municipal issuers already have a clear, existing obligation to disclose complete and accurate material information, including ESG factors, related to the security of any given series of bonds, and that obligation is being fulfilled.

For ESG-labeled bonds, internationally accepted standards (e.g. ICMA’s Green Bond Principles, Social Bond Principles, and Sustainability Bonds Guidelines and CBI’s Climate Bonds Standards) do exist and are increasingly used by municipal issuers. Municipal issuers are also increasingly using private vendor ESG certification services, with over \$17B of municipal issuance in 2021 receiving this verification.¹ Furthermore, we note an August 2021 report from S&P Global Ratings found that the fear of greenwashing may be greater than reality: “While there are increasing concerns that these potentially misleading practices [i.e., greenwashing, sustainability washing] are taking place, there seems to be little evidence that they have become widespread in reality.”²

¹Source: IHIS Markit.

² S&P Global Ratings “The Fear of Greenwashing May Be Greater Than the Reality Across the Global Financial Markets,” August 23, 2021.



For ESG-related disclosure, broadly recognized leaders in municipal finance (e.g., DC Water, the City and County of San Francisco, the Sacramento Municipal Utility District, and the New York Metropolitan Transportation Authority) are setting the stage with solid examples of voluntarily addressing ESG risks and reporting key metrics through primary market disclosure and through additional reporting.³ For some issuers, disclosure counsel has recommended including any voluntary ESG reporting information as part of the Continuing Disclosure Undertaking as a means to ensure that the issuer has a formal reporting framework.⁴ The rating agencies have also made significant efforts to increase the transparency of their assessment of ESG-related risks, as evidenced by new ESG scores and enhanced descriptions of ESG risks in their credit reports.⁵ It is important to note that these efforts have resulted in very limited rating changes. Finally, as a historical example of market-based initiatives guiding additional transparency and disclosure in the municipal market, please consider pension risk. In the past decade, pension risk was considered a top concern among municipal investors. The MSRB's website points to industry guidance on pension disclosure (i.e., GFOA, NASACT, NFMA, NABL, SEC)⁶ without imposing separate regulations. Accounting standards (e.g., GASB 67 and 68) also contributed to disclosure on pension risks⁷. Correspondingly, accounting organizations worldwide (e.g., SASB, International Sustainability Standards Board) are beginning to develop accounting standards for ESG risks⁸.

In addition to the rapidly developing market-based solutions, PFM fears that the potential for regulation of ESG-labeled bonds and/or ESG-related disclosure will result in the imposition of additional direct and indirect costs on issuers. We believe this cost would be unduly burdensome to issuers with no clear benefit to offset any regulation, particularly given the market-driven initiatives guiding additional transparency and disclosure currently underway. To date, we have observed no easily discernable or consistent pricing distinction, if any, for ESG-labeled bonds. Nor, as already mentioned, have we observed any widespread and material distinction in investor interest for bonds (or the pricing of bonds) due to ESG-related disclosure considerations.

³ See dcwater.com/investor-relations; sfcontroller.org/primary-market-disclosurefinal-official-statements-upcoming-sales; smud.org/en/Corporate/About-us/Company-Information/Investor-Relations; new.mta.info/investor-info

⁴ City of Gainesville, Florida Utilities System Revenue Bonds, 2021 Series A Official Statement; Appendix H: Form of Green Bonds Annual Impact Report.

⁵ S&P Global Ratings "S&P Global Ratings' ESG Roadmap and Reminders About Our Approach," October 5, 2021. Moody's Investors Service "ESG considerations have neutral to low credit impact on most large US counties," November 16, 2021. Moody's Investors Service "ESG considerations have neutral to low credit impact on most large US cities," November 16, 2021. Fitch Ratings "Public Finance & Global Infrastructure Interactive ESG Relevance Heatmap-3Q21," October 8, 2021.

⁶ <https://www.msrb.org/educationcenter/issuers/disclosing/preparing/resources-for-developing-disclosure.aspx>

⁷ Moody's Investors Service "State and Local Governments – US FAQ: Improved GASB Pension Disclosure Does Not Eliminate Need for Adjustments," April 18, 2016

⁸ sasb.org/about; ifrs.org/groups/international-sustainability-standards-board/



PFM is also concerned that any regulatory definition of ESG would not address the multiple perspectives that exist on this topic and, thus, would inadvertently create other ambiguities. Consider, as an example, a project that is designed to reduce sewer overflows into public bodies of water. While the project would clearly result in environmental benefits regarding cleaner public bodies of water, it would not reduce greenhouse gas emissions, which is one common measure of environmental risk. Comparably, for any disclosure of climate risk, we note that climate modeling is predicated upon a multitude of assumptions and inputs, with dedicated climate risk professionals differing in their assumption choices. Furthermore, as stated by Moody's Investors Service, "The definition of ESG issues is also dynamic because what society classifies as acceptable evolves over time, resulting from new information (e.g., the impact of carbon dioxide emissions) or changing perceptions (e.g., what constitutes privacy)."⁹ It is anticipated that as investors develop more concrete policies about what they invest in (i.e., "no coal"), this could drive the market toward more ESG reporting and standardization of the reporting. By being transparent and voluntary, the market-based initiatives that are becoming commonplace in the municipal securities market (for both ESG-labeled bonds and ESG-related disclosure) accommodate multiple perspectives on the definition of ESG.

While certain investors are outspoken with requests to regulate and increase standardization of ESG-labeled bonds, based on our observations, investors as a whole have not up to this point reflected that sentiment with any clear and consistent pricing distinction for municipal ESG-labeled bonds. If and when a pricing benefit materializes, we believe issuers will adjust their issuance approach, where applicable, to meet the market demand. Furthermore, we note that investors protect their own purchasing decisions by limiting clear and transparent reporting on their municipal investment decisions, including ESG-related decisions. Even when municipal issuers sell ESG-labeled bonds, it is difficult to discern which orders were placed as a direct result of such label.

Similarly, certain investors are requesting regulation and increased standardization of ESG-related disclosure. We understand that materiality is key to all municipal disclosure requirements and that the materiality of ESG risks varies significantly from credit to credit. We have observed that for a variety of municipal issuers that have expanded their ESG-related disclosure, there was limited feedback or questions from investors and other key stakeholders. As such, it is extremely challenging to discern any clear and consistent benefit of this disclosure that would be broadly applicable across all municipal issuers.

Below, we address a number of the questions set forth in the MSRB's Request for Information.

Questions for Municipal Advisors:

Does the formulation and delivery of advice regarding ESG-Labeled Bonds raise any novel compliance issues for firms, such as challenges related to recommendations, pricing, suitability or other related legal obligations?

⁹ Moody's Investors Service "General Principles for Assessing Environmental, Social and Governance Risks Methodology," October 19, 2021.



No. From PFM's perspective, ESG-labeled bonds raise no broad novel compliance issues under the current regulatory construct. Our approach to and documentation of advice on ESG-labeled bonds is the same approach and documentation we use to advise on a range of other topics. Given the existing, voluntary market standards for ESG-labeled bonds and the observable pricing of ESG-labeled bonds, we have sufficient information to discuss the advantages, disadvantages, nuances and complexities of ESG-labeled bonds with our clients.

Furthermore, we strongly believe that the MSRB should not require municipal advisors to distinctly address ESG-labeled bonds within its Written Supervisory Procedures (WSPs) but should, as intended under the current regulatory framework, require instead that a municipal advisor's WSPs be reasonably designed to ensure compliance with applicable SEC and MSRB rules and other applicable securities laws and regulations. Accordingly, municipal advisor's WSP's, as established, need to consider the particular facts or circumstances and the principles of fiduciary duty and suitability, including reasonable care, inquiry, and diligence. To require a municipal advisor's WSP's to specifically address ESG-labeled bonds would distinguish one specific aspect of a specific type of municipal bonds without the same treatment for others (types or attributes). For example, the MSRB does not require WSPs to specifically address unrated or low-rated bonds or pension obligation bonds, which arguably could carry greater risks than ESG-labeled bonds.

Does the formulation and delivery of advice regarding ESG-Related Disclosures raise any novel compliance issues for firms, such as challenges related to recommendations, pricing, suitability or other related legal obligations?

No. As a municipal advisor, our role in the development of ESG-related disclosures, if any at all, is typically educational in nature. For example, we assist issuers in understanding investor preferences and help issuers understand ways to effectively communicate their ESG narrative. As part of the education process, we also point to industry guidance such as GFOA's Best Practices on ESG Disclosure.¹⁰

As noted above in the previous question, we believe that the MSRB should not require municipal advisors to distinctly address ESG-related disclosure within our WSPs as the current regulatory framework sufficiently addresses an MA's responsibilities related to recommendations, pricing, suitability or other related legal obligations.

Questions for all Municipal Market Participants

Are there any ESG-related factors that could pose a systemic risk to the municipal securities market? If so, how might the MSRB approach such systemic risks from a regulatory perspective? Are there non-regulatory approaches the MSRB could take that would advance issuer protection, investor protection, and the overall fairness and efficiency of the market?

¹⁰ GFOA " 'ESG' Best Practice - 'E' Environmental," March 8, 2021. GFOA " 'ESG' Best Practice - 'S' Social," October 1, 2021. GFOA " 'ESG' Best Practice - 'G' Governance," October 1, 2021.



While there are ESG-related factors that may pose systemic risks to the municipal market (e.g., social risks, governance risks, climate risks), they are rooted outside of the realm and control of municipal finance. Furthermore, while there is currently a heightened focus on these risks, they are long-standing risks – not new ones. We believe regulation of ESG-related factors is neither needed nor appropriate at this time. PFM is concerned that any regulation would result in additional costs placed upon issuers, with no clear benefit to them. We suggest that the MSRB allow industry-led initiatives to continue to drive the evolution of market participant response to these risks.

As noted later in our response, we believe MSRB can leverage the strength of its EMMA platform to make several technical adjustments to EMMA that would facilitate greater transparency and data-sharing on ESG-related risks.

There are a number of organizations establishing voluntary standards for the issuance of ESG-Labeled Bonds, such as the ICMA and CBI. Does the availability of these voluntary, market-based standards provide adequate guidance for issuers and transparency for investors in the municipal securities market? If not, what additional guidance or transparency do you believe are warranted with respect to ESG-Labeled Bonds?

PFM believes that voluntary, market-based standards provide sufficient guidance for the market with respect to ESG-labeled bonds. The existing standards provide multiple quantitative and qualitative views of ESG risks, offering the market diverse perspectives. This diversity of perspectives, and optionality in their use, is critical in navigating what is a complex topic. When issuers choose to follow these standards, investors can understand the paradigm and definitions used to substantiate the ESG label.

We understand that certain market participants would like a singular, universal ESG language to guide the municipal market. We note that the two voluntary standards cited by the MSRB in this question (i.e., ICMA and CBI), along with the United Nations Sustainable Development Goals (UN SDGs), are increasingly followed by municipal issuers, broadly accessible to the market, transparent, and broadly understood.

There are a number of industry-led initiatives underway intended to improve the quality of ESG-related information available in the municipal securities market. Does the availability of these voluntary, market-based initiatives enhance the ability of investors and other market participants to make informed decisions in the municipal securities market?

We believe that market-based initiatives are naturally guiding and improving ESG-related disclosure in the municipal market.

In terms of disclosure, we note that reporting is one of the four core tenets of the ICMA Principles (i.e., Green Bond Principles, Social Bond Principles, and Sustainability Bond Guidelines), which in our observation has been the most widely adopted ESG framework globally. As such, we have observed that issuers have responded with increased reporting and disclosure on ESG specific considerations. In the municipal



market, many issuers closely follow the GFOA. GFOA's recently published best practices regarding ESG disclosure provide additional guidance to issuers on this subject.¹¹ We believe the GFOA guidance is flexible and can be adjusted to each issuer's distinct geographic location and unique demographics, while also providing concrete examples and suggestions.

Beyond ESG related disclosure that issuers are voluntarily providing, other market participants are offering increased transparency and communication in this area. For example, the rating agencies are focused on increasing transparency of ESG risk assessments, as evidenced by new ESG scores and disclosure in credit reports.¹² Additionally, for ESG-labeled bonds, private vendors offering ESG certification services provide additional insights and clarity through the information they attach to the bonds.

We anticipate that the adoption of current market-based initiatives will continue to grow and that new industry-led developments will emerge, all contributing to a natural and voluntary evolution of enhanced transparency in the municipal market.

There are numerous vendors providing ESG data for the municipal securities market. Does unequal access to ESG data result in disparate impacts to investors and other market participants? Does competing ESG data create investor confusion? How could the MSRB use the EMMA website to reduce information asymmetry or investor confusion?

PFM observes there is current inequity between issuers and investors in accessing quantitative ESG risk assessment data. In recent years, investors and rating agencies have purchased multiple data services (e.g., RisQ, Four Twenty Seven, Video Eiris)¹³ that focus on assessing certain environmental and social risks. We understand that this data is used to assign differential risks scores at the geographic, obligor, or even the CUSIP level. We observe that the firms producing this data are primarily focused on selling this data to investors and rating agencies, and justifiably so, as those parties are driven by comparative analysis across credits. As stated previously, we do not believe issuers have a clear and consistent cost benefit related to ESG-labeled bonds or ESG disclosure and as such, would be challenged to justify the cost of purchasing this type of ESG risk assessment data for their own credit(s). Issuers' access to this same or similar data could help them provide more informed and targeted disclosure, potentially addressing any areas of elevated risk or concern.

¹¹ GFOA " 'ESG' Best Practice - 'E' Environmental," March 8, 2021. GFOA " 'ESG' Best Practice - 'S' Social," October 1, 2021. GFOA " 'ESG' Best Practice - 'G' Governance," October 1, 2021.

¹² Moody's Investors Service "General Principles for Assessing Environmental, Social and Governance Risks Methodology," April 26, 2021. S&P Global Ratings "S&P Global Ratings to Enhance Transparency in U.S. Public Finance Credit Analysis with ESG Credit Indicators," February 16, 2022. Fitch Ratings "2021 ESG in Credit White Paper," July 2021.

¹³Any third-party's tradenames, product and service names used throughout are the intellectual property of their respective owners.



The MSRB recently incorporated an ESG indicator from an independent data vendor, IHS Markit, into the New Issue Calendar shown on the EMMA website.¹⁸ This ESG indicator denotes when an issuer has self-labeled a bond issue as green, social, or sustainable, or if the issuer includes an independent ESG certification as part of the offering document. Does making this ESG indicator available on the EMMA website enhance market transparency regarding ESG-Labeled Bonds? Specifically, is it valuable to investors, municipal issuers or other market participants?

PFM commends the MSRB for this recent enhancement to EMMA which increases market transparency. We believe this feature could be increasingly beneficial if the ability to search for historical ESG-labeled bonds is expanded beyond just “recently sold” to include as much historical information as possible. This would provide an opportunity for all market participants to better understand the market for ESG-labeled bonds (e.g., who is issuing, how much is being issued, ESG label types) without the burden of paying for this data through other services.

What improvements could the MSRB make to the EMMA website regarding ESG-Related Disclosures, ESG-Labeled Bonds and other ESG-related information? Which improvements to the EMMA website would most enhance access for investors and other market participants to ESG-related information? Which improvements to the EMMA website would most enhance the fairness and efficiency of the municipal market?

PFM suggests the MSRB consider creating a dedicated tab / section for “ESG Disclosures,” similar to current “Financial Disclosures” and “Event-Based Disclosures.” Alternatively, MSRB might consider creating a way for issuers to flag voluntary disclosure as ESG-related. This enhancement could facilitate a clearer path of voluntary communication on this topic between issuers and other market participants.



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PFM greatly appreciates the continued outreach the MSRB provides for the opportunity to share our input with the Board and staff. As always, we would welcome the opportunity to discuss these comments further.

Respectfully submitted,

PFM FINANCIAL ADVISORS LLC

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By: 
Daniel Hartman
Chief Executive Officer

cc: Patrick Brett, Chair, MSRB
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