ESG – WHAT IS IT?

May 18, 2023

2:00 p.m. – 3:40 p.m.

Jeffrey T. Larson, President
Larson Consulting Services, LLC.
jlarson@larsonconults.com 407.496.1597

LARSON
Consulting Services, LLC


WEBINAR OUTLINE

SECTION I TRADITIONAL CREDIT REVIEW & RATINGS CRITERIA

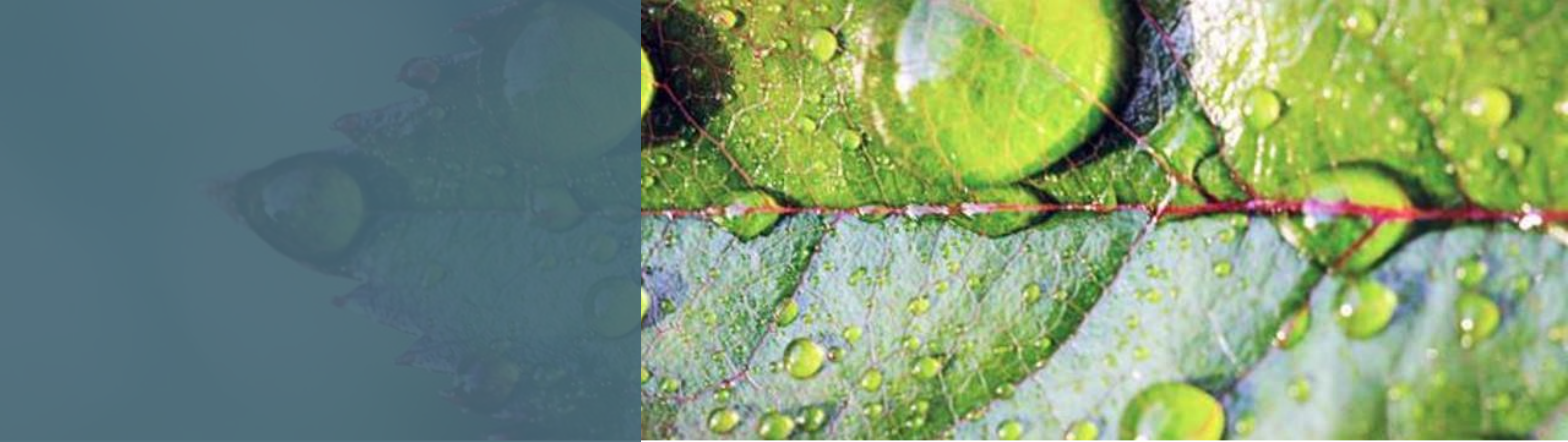
BOND INSURERS

- Traditionally, Bond Insurers review and approve insurance for "investment grade" issuers, and certain asset classes
- Bond Insurers focus on operating history, financial performance, key items including pledged revenues, leverage, operating policies, financial covenants, and debt service coverage

RATING AGENCIES

WHAT IS A RATING?

- Forward-looking independent assessment of credit quality
- Better representation of the likelihood of full and timely repayment over life of a specific financial obligation
- Based on Issuer’s ability and willingness to pay on time
- Ability to pay = quantitative
- Willingness to pay – quantitative, historical actions, policies



WHY DO RATINGS MATTER?

- Bridge between Issuer and Investor
- Increased Investor knowledge and acceptance
- Higher underlying ratings equal lower interest rates and lower annual debt service

FOUR TRADITIONAL KEYS TO CREDIT ANALYSIS

- Economy
- Debt and other long-term liabilities
- Financial Performance
- Management and Administration

SECTION II
WHAT IS ESG?

HISTORY

- According to Forbes, United Nations developed a plan, led by Al Gore, to enact environmental and social policies
- European Union was early proponent
- E = Environment
- S = Social
- G = Governance
- United Nations Climate Change Conference – November 2022

SECTION II
WHAT IS ESG?

ESG HISTORY CONTINUED

- In 2022, European Financial Reporting Agency Group (EFRAG), SEC, and newly formed International Sustainability Standards Board (ISSB) drafted various proposals for disclosure standards
- Certain large institutional funds and investors started focusing greater emphasis on ESG, following earlier investor interest in "green bonds"
- Rating Agencies quickly adopted ESG standards, procedures as follow-up to earlier "green bonds" ratings services

SECTION II
WHAT IS ESG?

ESG HISTORY CONTINUED

- GFOA website and GFOA Committees developed ESG Disclosure and ESG "Best Practices"
- ESG defined by GFOA refers to three factors that affect a government's credit profile, including an exposure to:
    - Climate risk and other environmental factors ("E")
    - Long-term social factors ("S")
    - Governance Issues ("G")

SECTION II
WHAT IS ESG?

ESG CONTINUED

- GFOA states "ESG factors affect the long-term sustainability of a community"
- Rating agencies and investors are increasingly looking at ESG factors
- Governments play an important role in that overall rating assessment by providing specifics about their ESG challenges, action plans, and transparency

SECTION II
WHAT IS ESG?

ESG CONTINUED

- Without transparency, belief that investors will form their own ESG conclusions
- If issuing municipal bonds, important to understand disclosures, relative to important ESG factors

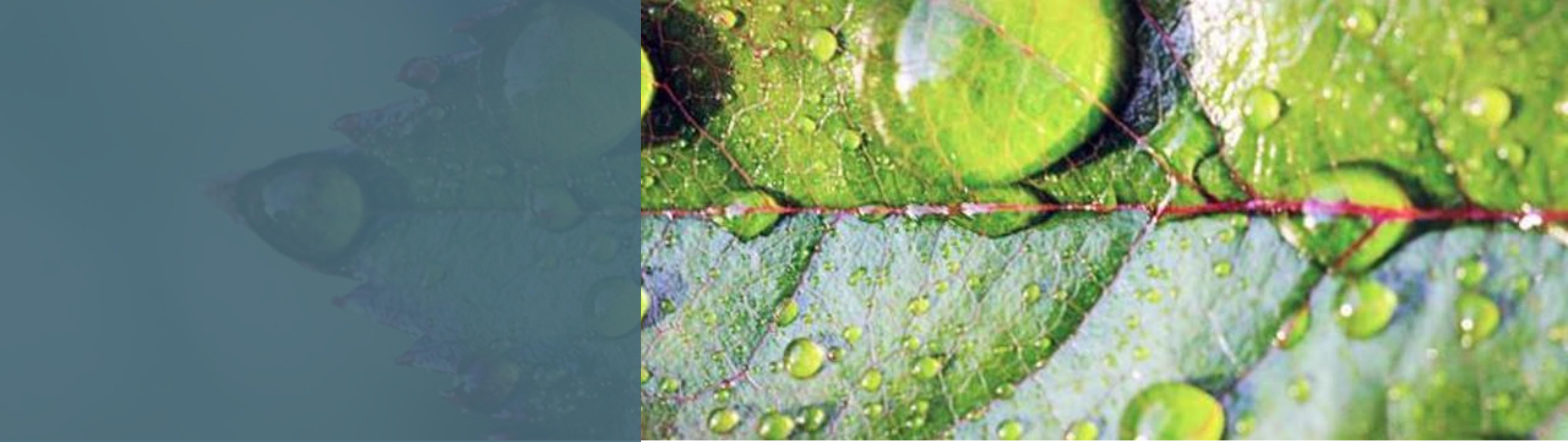
EXAMPLES OF ENVIRONMENTAL "E" FACTORS

- Inland flooding, tornados, drought, snow, ice storms, extreme weather events (hurricane risk)
- Climate change affects agriculture, infrastructure, local industries tax base
- Frequency and intensity of wildfires
- Sea level rise in coastal communities
- Water supply, both quality and quantity
- Diversity of power generation services and transition plans by providers

ENVIRONMENTAL CONTINUED

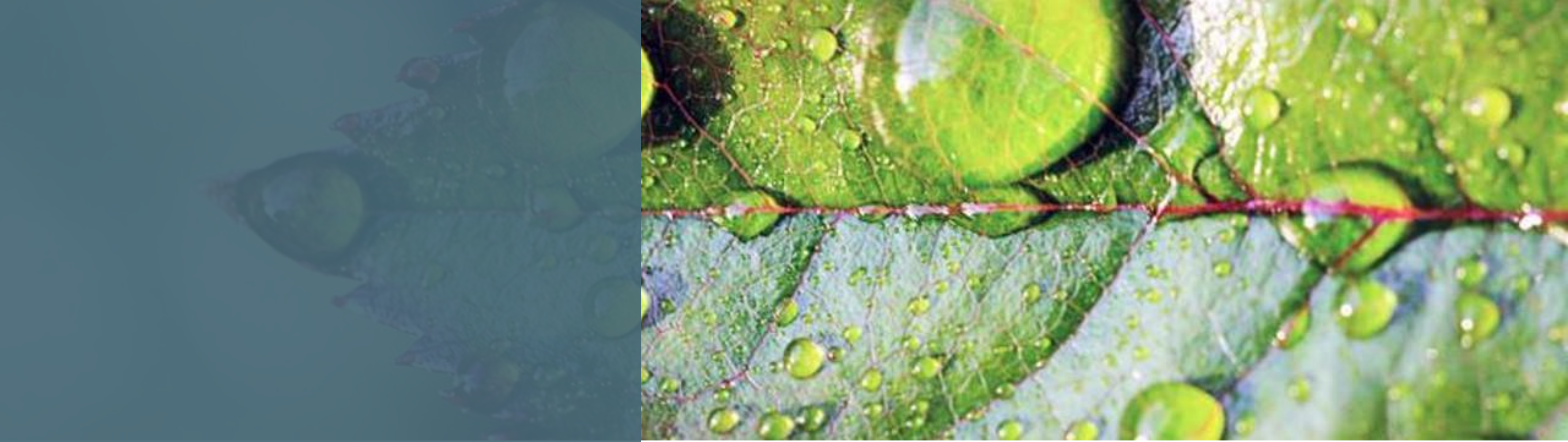
Best Practices Include:

- Identify leaders that have expertise
- Identify primary risks
- Review bond offering documents of peers
- Can “E” risks be quantified?
- Determine potential impact on operations
- Avenues to mitigate these risks
- Develop disclosure approach
- Develop policies



EXAMPLES OF SOCIAL “S” FACTORS

- Availability and affordability of housing for vulnerable populations
- Demographic changes and population trends affecting demand for services or tax base
- Income levels, wealth, and disparities
- Affordability of government services, tax rates, or sufficient tax base
- Labor union challenges/union contracts
- Availability, access, and quality community health services



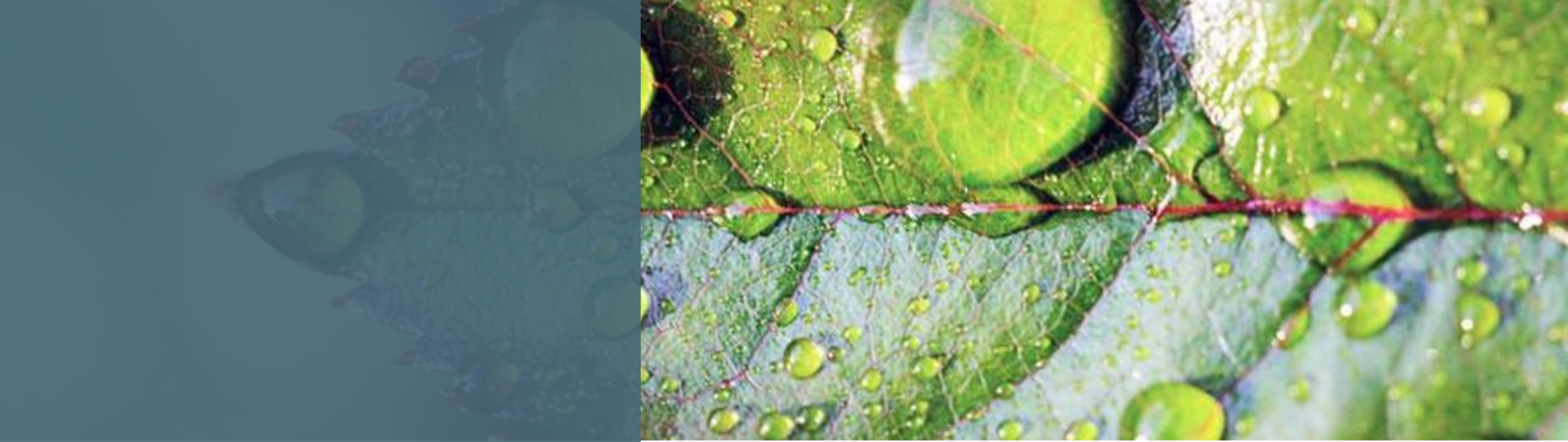
SOCIAL "S" FACTORS CONT.

- Quality of Public education and vocational training
- Labor force, employment/unemployment, job opportunities
- Internet access and affordability

SOCIAL FACTORS CONTINUED

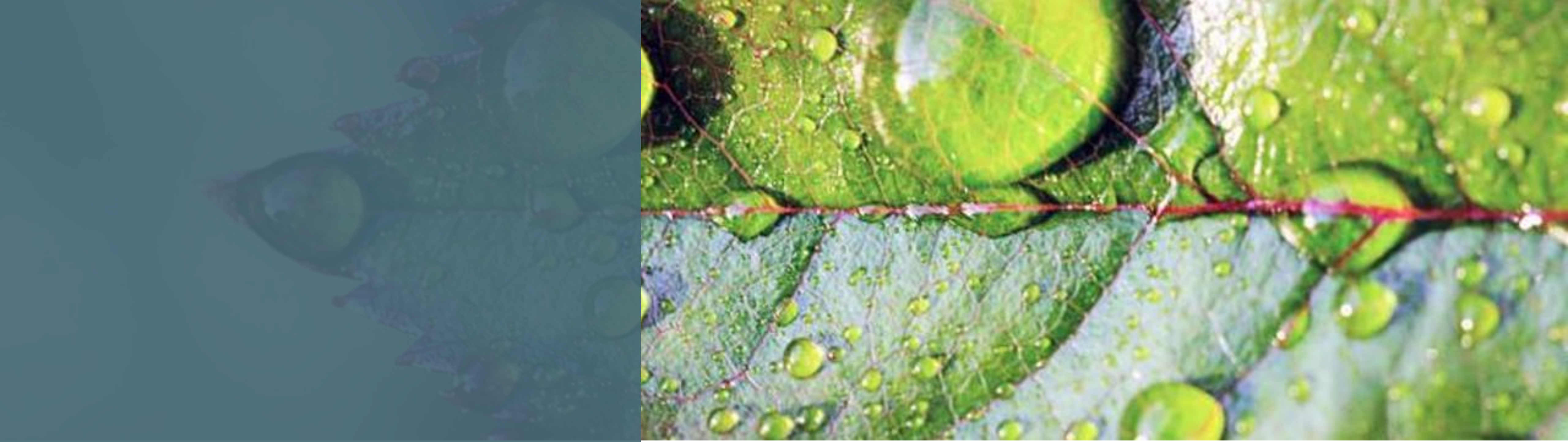
Best Practices can Include:

- Continue to provide information on population, personal income, employment, demographic trends in offering documents
- Disclose any particular issues, ie. civil unrest, crime, weather issues
- Look at trends affecting population growth, property values, employment opportunities
- Senior management and policy involvement since social factors can be complex, politically charged, amplified by media, sensitive to address



EXAMPLES OF GOVERNANCE “G” FACTORS

- Organizational structure
- Legal authority to issue debt
- Policy transparency
- Management and Policy framework
- Financial Reporting
- Federal and State framework



GOVERNANCE "G" FACTORS CONT.

- Risk culture mitigation – **Cyber security**
- Budget controls, revenue forecasting
- Relationship to federal and state funding
- Deferred maintenance, infrastructure management
- Smart growth and land-use planning
- Pension, OPEB, level of funding

GOVERNANCE FACTORS

Best Practices can Include:

- What is already being provided in bond offering documents, annual audit, CAFR?
- Continue primary and secondary (ongoing) disclosure
- Good governance, policies, policy making process, oversight
- Rigid Cyber Protection System

SECTION III CURRENT FEDERAL AND STATE ESG LEGISLATION

RECENT LEGISLATION INCLUDES:

- Federal Inflation Reduction Act
    - Passed August 2022 providing $739 Billion in funds for:
        - $309 Billion for Energy Security and Climate Change
        - $64 Billion for expansion of Affordable Care Act
        - $306 Billion for Deficit Reduction

$369 BILLION FOR ENERGY & CLIMATE CHANGE INCLUDED:

COVER CONSUMER ENERGY COSTS

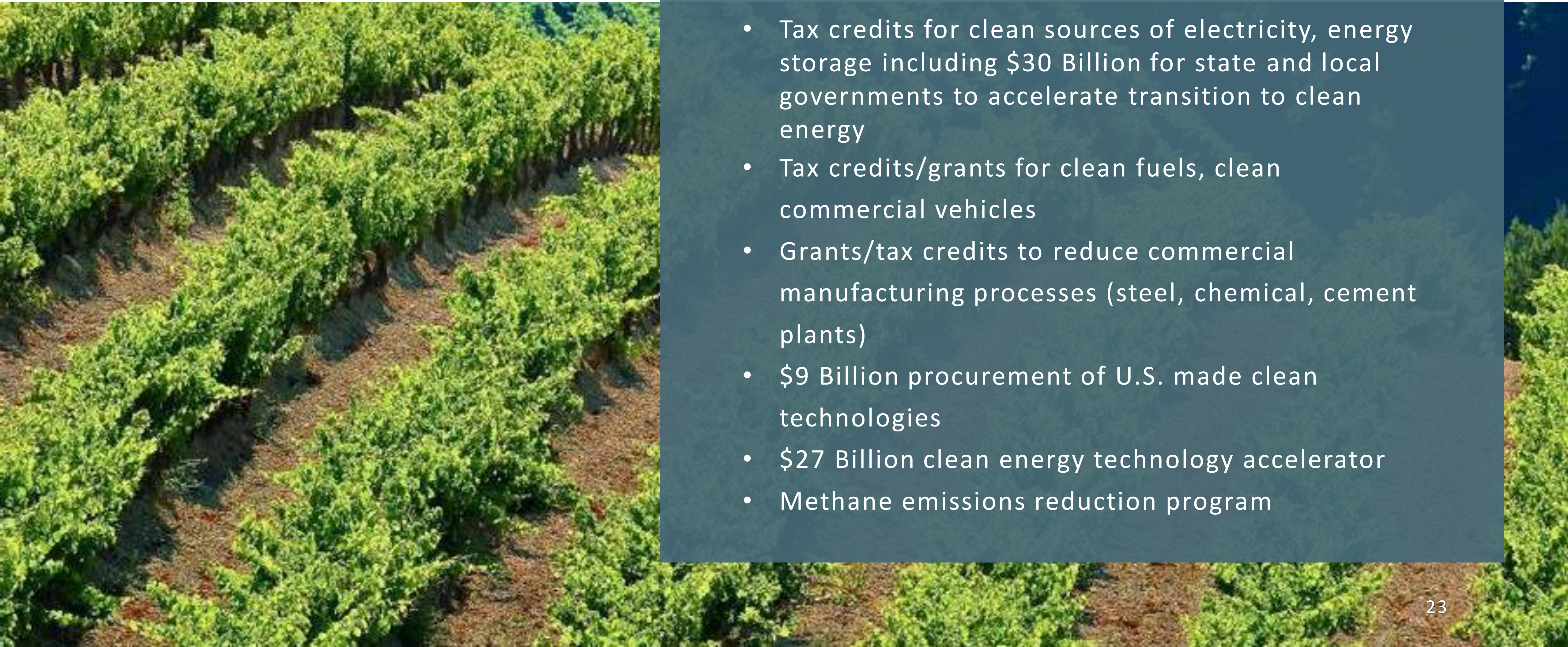
- $9 Billion consumer home energy rebate programs
- 10 years of consumer tax credits to make homes energy efficient, run on clean energy
- $4,000 consumer tax credit lower/middle income buy used EVs, $7,500 new EVs
- $1 Billion grant program to make affordable housing more energy efficient

$369 BILLION FOR ENERGY & CLIMATE CHANGE INCLUDED:

AMERICAN ENERGY SECURITY AND DOMESTIC MANUFACTURING

- Production tax credits to accelerate U.S. manufacturing of solar panels, wind turbines, batteries, critical minerals ($30 Billion)
- $10 Billion ITC build clean technology manufacturing facilities (EV's, wind turbines, solar panels)
- $500 Million for heat pumps, critical minerals processing
- $20 Billion loan for clean vehicle manufacturing facilities
- $2 Billion break through energy research

DECARBONIZE THE ECONOMY

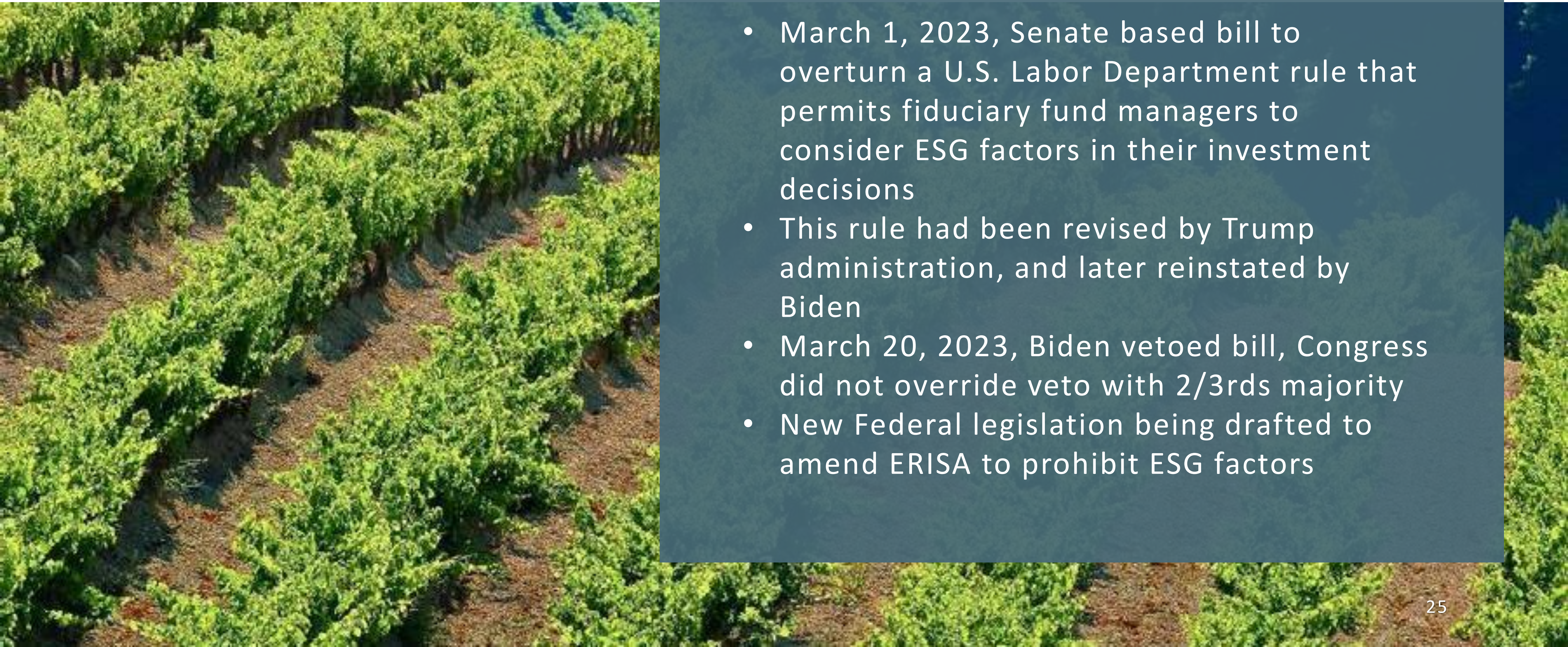


- Tax credits for clean sources of electricity, energy storage including $30 Billion for state and local governments to accelerate transition to clean energy
- Tax credits/grants for clean fuels, clean commercial vehicles
- Grants/tax credits to reduce commercial manufacturing processes (steel, chemical, cement plants)
- $9 Billion procurement of U.S. made clean technologies
- $27 Billion clean energy technology accelerator
- Methane emissions reduction program

OTHER PROGRAMS INCLUDE

- Block grants for community centers in disadvantaged areas
- Transportation grants
- $1 Billion clean energy heavy duty vehicles (school buses, garbage trucks)
- $20 Billion climate-smart agricultural practices
- Tax credit support domestic procedures biofuels
- $2.6 Billion grants to preserve and protect coastal habitats and communities

FEDERAL



- March 1, 2023, Senate based bill to overturn a U.S. Labor Department rule that permits fiduciary fund managers to consider ESG factors in their investment decisions
- This rule had been revised by Trump administration, and later reinstated by Biden
- March 20, 2023, Biden vetoed bill, Congress did not override veto with 2/3rds majority
- New Federal legislation being drafted to amend ERISA to prohibit ESG factors

RECENT FLORIDA ESG LEGISLATION

- May 2, 2023, Governor DeSantis signed legislation referred to as anti-ESG law, amending F.S. 280,516,560 and 655 targeted at any "financial institution"
- Financial institutions prohibited from:
  * making determinations about the provision or denial of services based on religious, political, or social beliefs
  * considering "social credit scores" in banking and lending practices
  * allowing banks that engage in corporate activism from holding QPD funds
  * using ESG in all investment decisions at the state and local level, ensuring that fund managers only consider financial factors

FLORIDA ESG LEGISLATION CONTINUED

- Prohibit all state and local entities, including DSO’s, from considering, giving preferences to, or requesting information about ESG as part of the procurement and contracting process
- Prohibits use of ESG factors by state and local governments when issuing bonds, including a contract prohibition on rating agencies whose ESG ratings negatively impact the issuer’s bond ratings
- Direct Attorney General and Commissioner of Financial Regulation to enforce (can include sanctions and penalties)

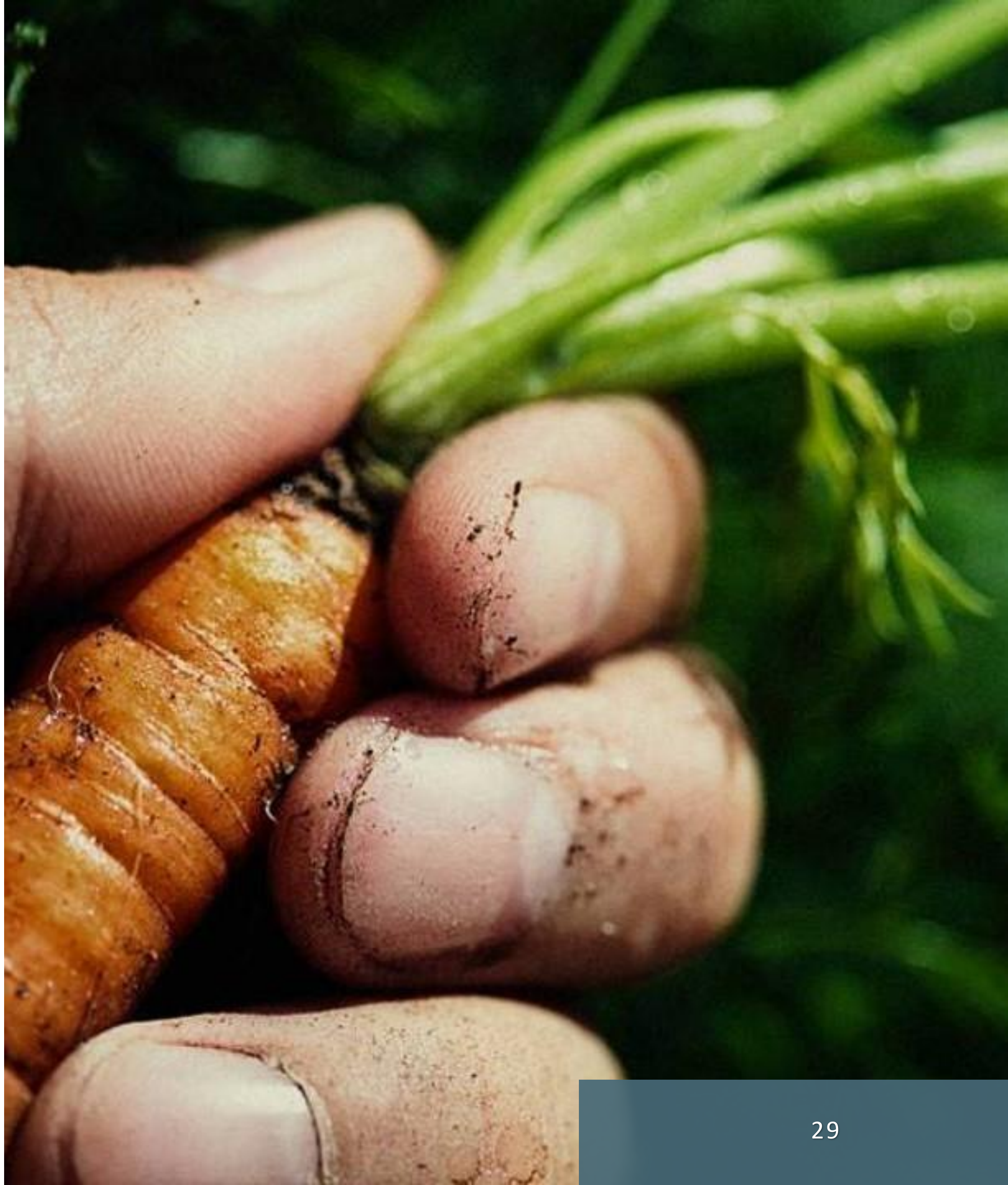
SECTION IV CONCLUDING COMMENTS

- Florida bill creates tensions regarding potential Federal Constitution’s protection of interstate commerce
- Florida bill creates potential conflict with Federal Reserve Board’s proposed safe and sound management exposures to climate related financial risks
- Other states forming an alliance with Florida to push back on Biden’s ESG Agenda
- New issues regarding QPD Bank status
- Changes approach on issuing bonds using ESG factors

RECOMMENDATIONS

Best practices for local governments issuing debt should continue to include:

- Full and fair disclosure of any material item
- Disregard “labels of ESG” until State/Federal conflicts are resolved
- Realization that many ESG factors were already being discussed, reviewed, and included in credit reviews, approvals, and ratings
- Discuss with your Financial Advisor and Legal Team



THANK YOU

Jeffrey T. Larson

407.496.1597

jlarson@larsonconsults.com

Larson Consulting Services

LARSON
Consulting Services, LLC

Jeffrey T. Larson

LARSON
Consulting Services, LLC

President, Larson Consulting Services
Tel: 407.496.1597
jlarson@larsonconsults.com

- Based in Orlando, and as President of Larson Consulting Services ("LCS"), an independent SEC and MSRB registered financial advisory firm, Jeff has successfully closed a wide range of municipal project finance and corporate financings totaling over $10 billion. Florida projects have ranged from negotiating and structuring a $2.7 Billion rapid rail project, higher education project financings, extensive water and wastewater capital expansions, investments support services, economic development and redevelopment initiatives, utility enterprise restructurings, refinancing and restructuring, downtown redevelopment, CRA TIF financings, debt and lease purchase private placements, public/private partnership project finance issues, and Charter School financings. In May of 2011, Jeff and FMAS was asked by the AAAm rated FL SAFE Local Government Investment Pool ("LGIP"), to serve as its Administrator and Executive Director. He has served many Florida governments since 1992 as an Investment Banker, Financial Consultant, Administrator, or Financial Advisor.
- Prior to establishing LCS and FMAS, Jeff managed D.A. Davidson's Southeast Regional Investment Banking Office. Prior to joining D.A. Davidson, Mr. Larson was the S.E. Regional Director Investment Banking and Consulting Services with Kirkpatrick Pettis, the investment banking arm of Mutual of Omaha, the Managing Director for Stifel Nicolaus/Hanifen Imhoff, and a Vice President, Investment Banking for SunTrust Capital Markets in Orlando, Florida. Recruited by these firms, he specialized since 1992 in Florida with the structuring and marketing of a variety of public finance and capital markets products. Prior to that, he spent ten years with C & S/Sovran in Atlanta and Barclays Bank PLC in Atlanta and San Francisco as a corporate finance, large corporate/Fortune 500, and Middle Market Banker.
- Mr. Larson received his MBA degree on an academic scholarship from Emory University, Atlanta, Georgia, in 1982. As part of his MBA graduate work, Mr. Larson worked, studied, and taught in Germany and Austria and was a Fulbright Scholar at the Johannes Kepler University in Linz, Austria. He received an A.B. in Business Administration with honors in 1980 from Franklin & Marshall College, Lancaster, PA. Mr. Larson's professional licenses with the SEC and MSRB include a Series 50 Municipal Advisor and Series 54 Municipal Advisor Principal.
- Jeff is a frequent speaker at industry conferences including the annual FGFOA, FCCMA, Florida Bond Buyer, FICPA, Florida Redevelopment Association (FRA), Florida Bar Association, Florida League of Cities, FL Tax Collector's Conference, FGFOA Webinars, Regional FGFOA Chapter meetings, FGFOA Career Seminars, Annual FGFOA Institute (School of Governmental Finance) and Special District conferences on topics ranging from "the Bond Issuance Process", "Best Practices in Debt Management", "Best Practices in Investment Management", "Planning and Capital Financing", to "Public-Private Partnership Financings." Jeff has also served as a member of the FGFOA Annual Conference Program Committee for over 20 years.

LARSON
Consulting Services, LLC

Larson Consulting's Team of Professionals provide financing solutions for many types of clients in Florida, the Southeast, and across the country. We specialize in a number of practices in which we have significant expertise. Our primary areas of focus include the following:

- Infrastructure Financings
- Special Districts and Land Development
- Higher Education
- Resort Communities
- Housing Agencies
- CRA & TIF Improvement Districts
- Tribal Finance
- Healthcare Finance
- Charter Schools
- Growth Management and Capital Planning
- Developer Project Negotiations
- Arbitrage Support
- Workforce Housing
- Project Financings
- Utility Financings
- Public Private Partnerships
- School Districts
- Project Consulting Services
- Lease-Purchase Financings
- Internet-Based Public Sales
- Alternative Energy
- Rural Water
- State Governments
- Utility Acquisition Analysis
- Refundings and Restructurings