



ESG: Responsible Infrastructure Investing

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WHAT IS ESG?

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Generally, it is an emphasis on environmental, social, and governance (ESG) factors in addition to financial returns by both companies, investors and donors



Many investors believe focus on ESG, including climate risk, will enhance financial returns while donors believe that investments – instead of grants – can bolster impact

E

S

G

ESG – Material to Operations

INFRASTRUCTURE SECTOR

E

GHG Emission, Air Quality, Energy Management, Water & Waste Water Management, Waste & Hazardous Materials Management and Ecological Impacts

S

Access & Affordability and Product Quality & Safety

G

Business Ethics, Critical Incident Risk Management and Systemic Risk Management

CONVENTIONAL ENERGY

E

GHG Emissions, Air Quality, Waste & Hazardous Materials Management and Ecological Impacts

S

Human Rights & Community Relations

G

Business Ethics, Management of the Legal & Regulatory Environment and Critical Incident Risk Management

RENEWABLE RESOURCES & ALTERNATIVE ENERGY

E

GHG Emissions, Air Quality and Energy Management

S

Human Rights & Community Relations

G

Management of Legal and Regulatory Environment and Critical Incident Risk Management

Source: SASB website, [materiality](#)

ESG – Climate Risk

- PHYSICAL risks from the increased frequency and severity of climate- and weather-related events that damage physical assets, resources and can disrupt trade.
- TECHNOLOGICAL risks from cost reductions and technological improvements.
- POLICY risks that include carbon taxes, subsidies for low-carbon energy and new regulations.
- LIABILITY risks stemming from parties who have suffered loss from the effects of climate change seeking compensation from those they hold responsible.
- TRANSITION risks that can arise through a sudden and disorderly adjustment to a low carbon economy.

Source: BoE Governor Mark Carney's speech "Breaking the tragedy of the horizon – climate change and financial stability" (2015), CTI analysis



ESG + ENERGY/INFRASTRUCTURE

ESG + ENERGY/INFRASTRUCTURE



OVERVIEW

- The need for renewable energy and infrastructure investment coincides with the rapid increase of impact investment, or investments made with the intent to generate financial returns as well as social and environmental returns.
- In 2019, Global Impact Investment Network study found \$239 billion impact investments under management.
- Energy remained a small but growing portion of those assets – 25% in 2019 compared to 16% under management in 2017.
- Infrastructure investments are also growing – 4% in 2019 compared to only 1% of assets under management in 2017.

ESG + ENERGY/INFRASTRUCTURE



- For investors who want to strive for market returns in renewable energy, infrastructure, and efficiency, the ability to monitor, measure, and report on the positive environmental impact of an investment could prove to be critical to securing the investment opportunity itself, co-investment partners, and government support.
- It also makes for better investment decisions and returns.

ESG + ENERGY/INFRASTRUCTURE



EXAMPLE 1: ENERGY COST EFFICIENCY

- Climate change regulations and growing energy demand will be contributing to rising prices for conventional electricity sources.
- Energy companies that need to focus on ESG to improve returns, including by
 - Managing their overall energy efficiency;
 - Diversifying energy sources to mitigate the risks and maintain a reliable energy supply (which could be particularly relevant in emerging markets); and
 - Minimizing energy costs through effective energy management to gain competitive advantages through operational efficiencies and pricing.

ESG + ENERGY/INFRASTRUCTURE



EXAMPLE 2: COSTS OF ENVIRONMENTAL IMPACTS

- Being proactive in cost-effectively reducing GHG emissions can create a competitive advantage for companies and mitigate unanticipated regulatory compliance costs.
- Failure to properly estimate capital-expenditure needs and permitting costs could result in significant negative impacts on returns in the future in the form of asset write-downs, costs of obtaining carbon credits, or unexpected increases in operating and capital expenditures.
- Regulatory emphasis on this issue will likely only increase over the coming decades.



TOOLS FOR ESG FOCUS

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FUND STRUCTURES

- **Traditional LPs and LLCs with impact features**
 - Return priorities – Return first; Return + impact; Impact first
 - Longer term to promote investments requiring longer runway to profitability
 - Linking compensation to impact performance
 - Protective provisions
 - Distribution structures – Impact investors first; Traditional investors first; Percentage to charity
- **“Evergreen” fund with various redemption options**
- **Permanent capital vehicles**
- **“Stacked deck” funds**
- **Side car impact funds**

TOOLS FOR ESG FOCUS



CORPORATE STRUCTURE

- **Traditional corporate forms**
 - Can include mission focus in charter, contract, and/or license
- **Hybrids or tandem structures**
 - Marrying non-profits with for-profits for impact and commercial purposes
 - Joint ventures between NGOs and for-profits
 - “Not your grandmother’s foundation” – 1% to charity approach is outdated and disconnected from operations
- **New corporate forms**
 - Public Benefic Corporation (DE)/Social Purpose Corporation (CA)
 - Other Benefit Corporations
 - Low-profit Limited Liability Company

TOOLS FOR ESG FOCUS



INVESTMENT TERMS

- **Convertible Debt:** Can be used to ensure impact by including specific covenants regarding mission and by defining violation of mission as an “event of default.”
- **Preferred Equity:** Strategies to anchor mission can be established by the social enterprise’s founders at time of formation or required by investors in later stages of investment.
- **Green Bonds:** New form of socially responsible investment. Generally are debt securities with proceeds ear-marked for uses that advance environmentally friendly objectives.
- **Social Impact Bonds:** Multi-party, pay-for-performance contract that pays investors financial returns based on social impact created by a nonprofit organization.

TOOLS FOR ESG FOCUS



METRICS, MEASUREMENTS, and BENCHMARKING

- Existing public companies already show considerable disclosure on ESG factors
 - **Required:** 10-K, 10-Q (particularly risk factors, MD&A)
 - **SEC required disclosure on climate change**
 - **Voluntary:** CSR or similar reports using Global Reporting Initiative (GRI) standard
- Integrated disclosure
 - **TCFD:** Task Force for Climate-Related Financial Disclosure
 - **SASB (US):** Sustainable Accounting Standards Board
 - **IIRC (International):** International Integrated Reporting Council
 - **Carbon Tracking/Risk:** Carbon Disclosure Project and Carbon Tracker Initiative
 - **Sustainable Stock Exchanges Initiative**

Q&A AND ADDITIONAL RESOURCES

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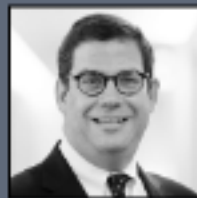
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ADDITIONAL MOFO RESOURCES



MOFO IMPACT RESOURCE CENTER

<http://www.mofo.com/impact>

MOFO IMPACT BLOG

<http://impact.mofo.com>