Transcript

Code 53

How Attention to ESG is Impacting Sustainability

Eric Tilden:
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Alison Johnson:
Welcome back to Code 53, The Apartment Podcast. I'm Alison Johnson with NMHC. On this show, we bring you into conversation with apartment industry executives, leading experts in the multifamily sector, and a diverse group of practitioners, all to help you learn everything it takes to create communities, from business strategy to design, to finance and leadership. Today on Code 53, we're exploring what sustainability looks like at the property level in 2023. From waste and material recycling, water use and energy efficiency to renewable energy and greenhouse gas emissions, the scope of how a property is designed and operated is more critical to the bottom line than ever before.

Coming up in a minute, we'll speak with Elme Communities senior director of ESG, Eric Tilden. We'll get specifics on how multifamily developers and management firms are reducing their environmental footprints and conserving resources, and we'll get his professional perspective on the ways these challenges present unique opportunities and risks in the multifamily space.

Announcer:
The Code 53 Podcast is brought to you by NMHC, the National Multifamily Housing Council, the place where the leaders of the apartment industry come together to guide their future success. From owners to managers and developers, NMHC's members create thriving communities by providing apartment homes for 40 million people, contributing $3.4 trillion annually to our nation's economy.

Alison Johnson:
Our guest today has helped to build a best in class ESG program focused on environmental impact, social equity, and positive governance for the publicly traded multifamily REIT Elme Communities, previously known as WashREIT. Eric Tilden is a civil engineer by trade with parchment from the University of Florida and his career has included stints as a civil project engineer, sustainability consultant, and senior managing director of US and energy sustainability services at Cushman & Wakefield. Today, he leads Elme Communities' ESG program and joins us from Washington, DC. Eric, thank you for joining Code 53.

Eric Tilden:
Thanks, Allison. Really glad to be here speaking with you today.

Alison Johnson:
Eric, let's start with the big picture, right? A long time ago, actually not so long ago, environmental aspects of a building would've been deemed secondary to other kind of building characteristics. But a lot has changed, particularly with the growth and influence of ESG or

environmental and social governance issues and reporting. How would you describe your work with both Wall Street and Main Street?

Eric Tilden:
Yeah, good question. I mean, ESG seems to be the acronym of the 2020s. Definitely you see it everywhere from all the major Wall Street firms and investors all the way down to the building level. Really what it entails is obviously environmental, social, and governance, that's literally what ESG stands for, but really it means how does an organization interact with and safeguard the environment through their operations? How does it impact communities both internally and externally? That includes managing relationships with employees, suppliers, vendors, and society in general.

And then G for governance is how are we ensuring accountability, transparency, and ethical behavior across all levels of the company, all the way up to leadership in the board of directors, if you have one? The intent of ESG is it's another way to analyze a company for an investor alongside other markers and metrics like returns. For companies, an ESG strategy should really tie into the financial decision-making of the organization and it should focus on short-term and long-term value creation while addressing material risks. That's one of the big differentiators between the Main Street and Wall Street definition of ESG or the unique way those two parties look at it.

When I go home and I talk to family and they ask me what I do for a living and I say ESG, they have really no idea what that really means. But when it comes to Main Street, it's really like how does an organization or company operate in a way that has positive effects and impacts on society and the environment? It's a really short, quick way in which my grandmother will understand. When it comes to Wall Street, they're really looking at how does an organization operate in a way that reduces risk and reduces potential loss, while at the same time creating and increasing value through those positive impacts, through environmental and social and governance related policies and practices.

A really good example with the Wall Street is if you're operating in a way that is focused on ethics, you might possibly reduce the chances of a litigation or a lawsuit. If you're operating in a way that's more energy efficient or more efficient for water consumption, you can potentially reduce the costs of running that property or that organization. You can also reduce the cost for possible transitional risks as the world sets its sites to a lower carbon economy, which we can talk about a little bit.

On the social side, if you're focused on labor standards and human rights, you have policies and practices, you have less exposure in your supply chain or in your direct organization to potential, again, litigation involving those areas. Really poor governance structures and oversight have led to some major failures of companies. I mean, think decades past like Enron, for example. Ensuring that you have these practices and policies that align with an ESG strategy is one way in which an investor and an analyst can look at an organization and say, "Ah, they have a potentially lower risk than other organizations."

Again, ESG should be seen as just one of many metrics that you look at in an organization when it comes to your decision to invest.

Alison Johnson:
I really appreciate how you defined it differently for the two audiences and why it's important to each of those. If I could summarize in my own way, would you say it's a way of making an executive or a leadership their strategic market management of their business practice more transparent?

Eric Tilden:
Yeah. I mean, you could say one aspect of ESG is obviously transparency. I mean, there's a lot of more corporate reporting when it comes to ESG across all different industry types. Now you have more organizations that rate your group such as MSEI, Moody's, S&P, Sustainalytics, ISS. Essentially, these organizations are taking publicly available information about your company and assessing your ESG programs to make reports that inform investors around your progress or your status compared to your peer group relevant to your industry. Transparency is a really big part of ESG.

I think one of the things which if you read The Economist, some of the op-ed pieces obviously that have come out recently around ESG is it's really broad. It's almost too broad. The way I always like to think of ESG is I don't necessarily disagree. ESG encompasses a lot of different aspects. It includes transparency around a lot of different items. But I always think of that as a big pizza pie. Each pie is a specialty. You have greenhouse gas emissions reporting. You have water use. You have diversity, equity, inclusion, and accessibility. You have human rights. You have ethical behavior. You have all these really important pie pieces which incorporate an entire organization.

For instance, in our organization, we have a diversity, equity, inclusion, and accessibility consultant that we have to support our company in developing programs and goals around DEI, to incorporate it into our culture. While I am the head of ESG, I'm by no means a DEI expert. What you want to do as an organization is you do want to have a robust ESG program. You also want to look at the experts and specialists within the respective pie pieces to support you in growing it so that you don't necessarily say, "Oh, it's just too broad. It's too much to encompass."

Well, it should involve everybody from accounting to HR, to marketing, to building operators, to maintenance teams, to vendors, all the way up to your CEO and your board of directors. Everybody should be included within a successful ESG program.

Alison Johnson:
I love the pizza pie analogy. If I can try to figure out how to make that work a little further, let's focus in on the pie and the toppings that you do focus on and that is environmental and resilient and those factors. Earlier at the top of the broadcast I said we were going to talk about property level sustainability. You had mentioned energy efficiency and water flow. Aside from low flow toilets, what does sustainability at the property level look like?

Eric Tilden:
When it comes to sustainability, what we're doing at Elme Communities is looking at greenhouse gas emissions and ways in which we can mitigate and reduce those emissions through various strategies. That includes deploying onsite renewable power where it makes sense for our organization, for our investors. We are a publicly traded REIT, so we look at

everything through a lens of return on investment and fiduciary responsibility to our investors. For example, in the City of DC where we have a few of our multifamily communities, we just finalized construction on two large solar arrays on top of those buildings.

What that will do is reduce our use of grid energy in the area. It will reduce our greenhouse gas impact. Those solar arrays are tied directly into the building. We're looking at more opportunities to deploy onsite renewables as legislation or the Inflation Reduction Act comes out, which may be able to help support REITs like ourselves take advantage of tax credits, which were previously not really accessible to us before. We're looking at energy efficiency opportunities to take advantage of local programs. Another good example from 2022 is we installed a new boiler system in one of our major apartment buildings in the DC area, and we actually took advantage of a utility rebate program for that boiler project.

Through that program, they paid about 40% of the entire boiler project by the local utility. That was great. I mean, the money is out there. It was a cash rebate. It proved the energy efficiency of our project, but we did it in tandem with a local utility program and we're able to win-win all around by reducing our initial capital costs. Across our properties, we're looking at waste obviously to reduce water beyond WaterSense fixtures and fittings, which we already have common practice in our units. We're looking at more and more zeroscaping. That means landscaping that doesn't require any permanent irrigation.

How are we installing native plants that can just live on their own, which is actually a win-win for us because not only does it reduce our water use, which reduces our common area water bills, but it also reduces the cost of irrigation, which is notoriously a money drain for a lot of communities similar to ours. Pipes leak, meters go bad, lawnmower hits the head of a sprayer, like everything can go bad with irrigation. If we can remove it completely and install native plants that live on their own, that's the way to go. And then continuously, we're looking at ways we can increase recycling and diversion rates at our properties, but waste is almost the gorilla in the room when it comes to sustainability.

One of the big things about it is it's hard to track. It's hard to consistently measure. Waste haulers typically don't have the capacity or the interest to track the weights of each individual can that leaves your facility and it's generally mixed in with other ones. We're always looking for ways to promote recycling, to promote proper sorting at the resident level, while at the same time always consistently trying to find ways in which we can track better the waste and recycling that leaves our facilities. It's a big task where we're continuously trying to find ways to improve.

Alison Johnson:
Those are a lot of different activities and definitely the public policy incentives that are being implemented are something to look forward to, but some of your programs seem to be geographic based, like communities themselves have incentivized the activity helped underwrite or offset the capital expense. I'd love to hear a little bit at how you think about tax credits when you're looking at your portfolio as a whole and what you can invest in in the physical buildings, what else you are thinking about to achieve your E goals and the returns associated.

Eric Tilden:
I mean, honestly, we're always on the hunt for support and reducing the initial capital costs of projects. Again, the Inflation Reduction Act has allowed huge potential to help REITs like ours,

where previously we couldn't take advantage of tax credits as a REIT when we deployed renewable energy onsite. We did not have that available to us when we built our two solar arrays in DC. With the Inflation Reduction Act, there's the potential that a REIT can then sell our tax credit that we would earn by installing solar or any other renewable onsite and selling it to an entity or another organization that does have a tax implication that can use that.

It creates a market that's very interesting for us. We're monitoring it with our solar consultants closely to see how can we deploy that in 2023 is we want to increase our onsite renewables and reduce our greenhouse gas emissions as much as possible, because it benefits us. I know that residents benefits the local grid. When it comes to other monetary possibilities, I mean, again, we look at local utility rebates. I mean, I would assure everybody if you have a local utility, connect with them to see what rebate programs they have available for energy efficiency. We also connect with them for things like EV charging.

A growing number of our residents have electric vehicles. Previously when we came into 2022, only 5% of our communities had electric vehicle charging stations. As we leave 2022 and we've entered into 2023, 42% of our communities now have electric vehicle charging stations and the infrastructure to build upon them. We installed two, three charging stations initially because that met the demand, but we have the ability to build off of that infrastructure down the road. The great thing about that is in Maryland and in Virginia, we coordinated with the local utilities, as well as like, for instance, the State of Maryland to receive cash rebates on the installation of those EV chargers including equipment and work and labor. It took a huge chunk of the initial capital investment and offset it right off the bat. It added an amenity to our residents that we didn't have. The EV chargers eventually pay for themselves through the cost of the electricity. Obviously, we're setting the cost of the rates at which people can charge their vehicles, and we don't go very much above the utility.

We want to get our money back when it comes to the cost of the electricity and a little bit more just to pay for the maintenance of that vehicle charging station. But over 50% of the cost of those to be installed was covered by cash rebates, which REITs can take advantage of. I really encourage everybody to look out for the money in their local area because a lot of times it's out there. It's just going through the process of applying and submitting and collecting the information and connecting with that respective body to receive it.

Alison Johnson:
One of the aspects of environmental stewardship is that there is an opportunity for resident service, brand building and recognition. What are you hearing from residents? Are they noticing the efforts?

Eric Tilden:
Yeah, absolutely. We survey residents on a regular basis, and we obviously communicate with them from the property management level around all of our sustainability initiatives and ESG initiatives that are going on at the building and at the company. We have a lot of support from our residents, but it's also mixed reviews. I mean, I think our residents reflect a diversity of backgrounds, a diversity of ways of life, a diversity of political viewpoints.

When we do survey our residents, we have a number of them that come back and love the sustainability programs and the education that we provide and the events that our property managers put in place to engage the residents around sustainability and social impact. And then we have residents that don't really care, for lack of a better word. They're not really wanting to be involved. They might even have anti-sustainability sentiments and voice those. You know what?

We take every resident with a full level of respect for your political viewpoint, and we want to ensure that we are engaging those that want to be engaged and supporting those that want to participate and be a part of it, and then obviously accommodating those who do not. There are certain things that we have shifted due to necessarily almost like requirements. For instance, a lot of our communities are the ones like DC and Maryland have reporting requirements where we need to report our energy use and our water use to the local municipality on an annual basis.

In those cases, we've installed green lease language or lease language which says, if you do have an energy bill or a water bill that you receive personally as part of your lease, you'll share that information with us. Because in the end of the day, we do have to report that to the local authority. Even in buildings where we don't have that requirement, we still try to utilize that lease language. Because at the end of the day, we as an organization are reporting our greenhouse gas emissions and our water consumption.

We try to ensure we have full data coverage or as much data coverage as we can, which we can go into a long conversation around data coverage when it comes to energy consumption, but engaging residents in that way to say, "Hey, we oftentimes can go to the utility and get aggregated data, but it might require a letter of authorization or some other form, and it's part of your lease. You're agreeing to support us in that effort, even if you don't care about low flow water heads."

We have a number of residents who change out our shower heads when they move in to a more higher flow, and then our maintenance team will change them back. It's a battle back and forth, but we want to make sure we're accommodating everybody while doing what we can to improve our sustainability performance.

Alison Johnson:
With regard to the data, there are massive amounts of data being collected from the devices. There's a lot of new technology out there that is helping with the monitoring part of energy use, water use, and et cetera. What is your approach to that? Because I mean, thinking through data privacy and security of that data is also an aspect of ESG that, or more importantly, the governance piece. How is your role thinking about that holistically?

Eric Tilden:
Data is one of the things that there are a lot of devices out there now that can support it, but it still tends to be a thorn in the side of a lot of organizations, especially multifamily real estate, because of the way in which utilities are set up at a lot of the buildings that we own, where residents are directly metered and their accounts are directly with the local utility company. There's 700 of them in a community, which could be just a massive amount of data, and we don't necessarily own nor have access to any of that data. What we do is we kind of go through a tiered approach when it comes to data collection is obviously we track and monitor our data.

When it comes to common area bills, when it comes to bills for buildings that are primary metered and then submetered down to residents, we make sure that we're monitoring and tracking all of that information. When it comes to communities that are directly metered for each resident, we reach out to the utility companies to obtain aggregated data, so that way we can't necessarily see a single individual's energy or water use. What we see is a complete water use for that site. That helps with the security of information because utility companies can provide that level of information or a number of them can.

A number of them have to, depending on where you are geographically, they have to make that data available and accessible because of local reporting requirements. Typically, we go down that avenue when we don't have data coverage already for a site. When it comes to certain geographies where there is no benchmarking or reporting requirement and the utility has no obligation to give us aggregated data or perhaps they don't even have the ability to do so, they just don't have it set up, then we look at device metering. And that means looking at how can we capture as much data coverage for this site for energy use that's not ours.

It is the residents. They call it a Scope 3 emission, if you want to get technical. How can we meter that so that we can get some aggregated data around that site, around that community of total energy consumption, of total greenhouse gas emissions from energy use, and so looking at metering technology and putting that into our data set. But to your point, we have a really tight and well run IT and cybersecurity department because we deal with a lot of resident data beyond just energy use. Obviously we process rent payments and all sorts of information. When it comes to any vendor that steps foot into our organization or onto our properties, they go through a cybersecurity background check, and they go through this thorough process in which our team evaluates their process and ensures that there's little chance as possible that any data breach or anything like that could occur.

Alison Johnson:
Thinking about what is happening right now in the world, California has just experienced a deluge after going through a period of drought, all eyes are focused on the term resilience, community resilience. How does climate change really factor into what you're thinking through for the future of your investments?

Eric Tilden:
I mean, great question. I used to live in California during the drought period, so understand the troubles that they're going through now. The drought period's over. And with that much rain, the mudslides and everything. Here at Elme Communities, we look at climate related risk for our existing assets, as well as any asset that we might acquire. As part of our due diligence process when it comes with our investment team is when we look at an asset or a community we're looking to acquire, we complete a thorough ESG evaluation, including transitional risk and physical climate risk.

Physical climate risk, how are storms, heat stress, wildfire, how are they going to impact the building today, how are they going to change over the next decades, and understanding what risks come with that. A good example would be wildfire. We had a property in Georgia that we were assessing, that we evaluated. I'm using Moody's tool, it's a climate analytics tool, and they said, you're in a wildfire prone area. At all of our properties, we take that information and we go

a step forward. We have an onsite evaluation by a professional engineering team. Oftentimes it's the same people that do our property condition assessment, but not necessarily.
In this case, we saw the shrubbery that had grown right on up to the walls of the communities. It just had not been taken care of. I mean, it didn't look bad necessarily, but what it was is it was very tinder prone. Basically it was just ready to go up in flames if wildfire was in the area. In a wildfire prone area, really in any area, you should have about a 100-foot buffer of what they call the defensible zone around your building, so that if you do have a wildfire, you don't have that vegetation right on up that could catch fire and then catch your building on fire. When we evaluated that community, we estimated the cost of remedying that was over a million dollars of landscaping work to remove that vegetation.

That went into the board memo, the memo that goes to the board, around all of our findings and whether or not we should or should not acquire that property for a variety of reasons, including that one. We didn't acquire that specific property, but it's part of that process where we identified that climate risk. Another one we always look at is drainage. I mean, mostly we're in the southeast, in the Mid-Atlantic. Drainage is a major issue here. Princeton researchers recently developed a new map because everything when it comes to drainage is based off of things like the 100-year storm or the 100-year flood.

This is now my civil engineering background, which what we're finding is that 100-year storm is much more frequent now than it was at the time that that was evaluated. Now, Princeton estimates that the 100-year flood in the southeast can occur every year to every 30 years. That means we're having very large storms, a lot of rain in a short period of time. We want to make sure our drainage capabilities are there to accommodate that storm and that we have the preventative maintenance aspects, so forth. Our existing assets, we look at preventative maintenance of stormwater management systems, installing better improved stormwater management systems.

Even down to the gutters, ensuring that the gutters are clear and things like that, which is often overlooked or could go months between clearing, and then you have all those pine needles built up and stuff like that. We really look at all those. When it comes to transitional risk, transitional risk is really as the world and different economies transition to a carbon-free economy, there's risk of your building being stranded or left behind, because now it doesn't comply with certain standards. A great example is here in DC. DC has released a Building Energy Performance Standards, which means that every building within the district has to comply or meet a certain level of energy efficiency relative to its peers.

If it does not, it has five years to fix that or start receiving penalties in the form of fines. That's a financial risk to obviously our shareholders and us. We want to make sure that we are not underperforming, that we're meeting that compliance. As we look at our existing markets, our existing assets, as well as future ones, we're really looking at what legislation is in the pipeline, what legislation exists, how will that legislation potentially change with time and that certain geography where we may be purchasing an asset that does not meet compliance standards and therefore we'll receive penalties and fines without some major capital improvements, and then what are those capital improvements.

Really we're taking a really big look at climate risk, both the physical risk that you see in California, as well as the financial transitional risk as cities and states rollout legislation related to carbon and energy efficiency.

Alison Johnson:
It's a lot to take in. Eric, thank you so much for distilling these concepts for us and pointing our audience and even myself in the direction of some resources and places to look for more information. It's very helpful. I want to thank you so much, Eric Tilden, senior director of ESG at Elme Communities, for being with us on Code 53, The Apartment Podcast.

Eric Tilden:
Thanks, Alison. Thanks for having me.

Alison Johnson:
And thanks to everyone downloading and sharing this podcast. Coming up on our next episode, rent payment reporting, how new regulations from FHFA are empowering tenants with mortgage lenders. Subscribe and meet us right back here on Code 53, The Apartment Podcast.