PRIVATE EQUITY STAKEHOLDER PROJECT

March 21, 2025

California Air Resources Board
1001 I Street
Sacramento, CA 95814

Information Solicitation to Inform Implementation of California Climate-Disclosure Legislation: Senate Bills 253 and 261, as amended by SB 219 – Private Equity Stakeholder Project

Dear Chair Randolph and Members of the Board,

The Private Equity Stakeholder Project (PESP) is a non-profit financial watchdog organization that seeks to bring transparency and accountability to the private equity industry for the benefit of impacted communities and investors.

We appreciate this opportunity to provide feedback to help inform the California Air Resources Board's (CARB) work to implement Senate Bills (SB) 253 and 261, both as amended by SB 219. The implementation of this legislation will provide the public, including investors like public pension funds, with important details related to a company's ability to manage and mitigate climate risks.

Strong climate disclosure regulations are urgently needed because, due to the lack of standardized reporting, climate disclosures are often piecemeal and subjective. This asymmetric situation can put public retirement money at risk, especially in the opaque private funds industry.

Growth of Private Markets underscores need for climate-related disclosures

The physical and financial risks from climate change and the energy transition may be the biggest challenge faced by the capital markets, shared by both public and private markets. Investors across these markets do not currently have adequate information about climate-related risks. For private market investors, these risks may be amplified due to illiquidity of closed-end investment vehicles, reliance on leverage and the lack of transparency about the investments held within such funds.

Private markets have grown enormously, and the SEC has tabulated the gross assets at $18 trillion.[1] Research by Vanguard found that "the asset size of the private equity market has been

[1] *Statement on Private Fund Advisers Proposal, SEC, February 2022;* *https://www.sec.gov/news/statement/gensler-statement-private-fund-advisers-proposal-020922*

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gradually growing on an absolute basis and relative to the public equity market over the last 20 years."[2] The number of companies backed by private equity has grown – McKinsey found that the number of US-private-equity backed companies doubled to 8,000 between 2006 and 2017 – while the number of publicly traded firms dropped to 4,300.[3]

The shift from public to private markets is happening for carbon-intensive assets as well, with publicly-listed companies seeking to shed conventional energy assets through sales where private equity is frequently on the buying side of the deal. *The Economist* noted several "multibillion-dollar deals, with giants such as Blackstone, Carlyle and KKR carving out huge oilfields, coal-fired power plants or gas grids from energy groups, miners and utilities. Many other deals, sealed by smaller rivals, get little publicity."[4]

The capital private equity firms deploy for such deals comes in large part from institutional investors with fiduciary obligations to public and private pension funds, all of which need fuller disclosure to understand the risks.[5]

Public pension funds have diversified portfolios that are invested across capital markets in publicly traded and alternative assets, with $5.85 trillion in assets.[6] These funds invest on behalf of nearly 15 million public sector workers and over 11 million retirees, distributing $323 billion in benefits each year.[7]

Alternative assets such as private equity have grown in importance to public pension funds, reaching an average allocation of 19 percent.[8] Pension funds and other institutional investors continue to increase their allocations to private equity.[9] Additionally, private equity firms and

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[2] *Vanguard, "The role of private equity in strategic portfolios," October 2020*

[3] *McKinsey Global Private Markets Review 2019* *https://www.mckinsey.com/~/media/mckinsey/industries/private%20equity%20and%20principal%20investors/our%20insights/private%20markets%20come%20of%20age/private-markets-come-of-age-mckinsey-global-private-markets-review-2019-vf.ashx*

[4] The Economist, Feb. 12, 2022, "Who buys the dirty energy assets public companies no longer want?" https://www.economist.com/finance-and-economics/who-buys-the-dirty-energy-assets-public-companies-no-longer-want/21807594

[5] Institutional Investors, "The World's Dominant Investors in Private Equity," November 6, 2020 https://www.institutionalinvestor.com/article/b1p4bkg405f9k3/The-World-s-Dominant-Investors-in-Private-Equity

[6] https://www.nasra.org/content.asp?admin=Y&contentid=200

[7] https://publicplansdata.org/quick-facts/national/

[8] https://www.nasra.org/investment

[9] McKinsey, Global Private Markets Review 2021, published April 2021 and Wall Street Journal, "Retirement Funds Bet Bigger on Private Equity," Jan. 10, 2022 https://www.wsj.com/articles/retirement-funds-bet-bigger-on-private-equity-11641810604

other private funds managers have been seeking to expand from institutional clients to retail investors.[10]

The convergence of the increasing risks of climate change with the growth of private markets, paired with increasing reliance of institutional investors on private market alternatives to achieve their rates of return all underscore the value of California providing regulatory guidance on climate disclosures across both public and private companies.

Private Markets Investors Face Climate-Related Risks

The current limited transparency in private equity means investors in private equity and other private funds have exposure to undisclosed risks due to climate change, greenhouse gas emissions, and the energy transition. These risks exist across portfolios but may be most acute in carbon-intensive industries like energy. Pitchbook data show that private equity invested over $1.1 trillion in energy between 2010 and 2021.[11]

Last October, the Private Equity Stakeholder Project, Global Energy Monitor, and Americans for Financial Reform released the Private Equity Climate Risks scorecard, which studied 21 private equity firms that manage $6 trillion worth of companies and found that two-thirds of the energy companies in their portfolios are invested in fossil fuels.[12]

The Scorecard found that these fossil fuel assets are responsible for 1.17 billion metric tons CO2 equivalent of emissions a year in upstream oil and gas, liquefied natural gas (LNG) terminals, and coal-fired power plants. That gigaton level of emissions is over three times as much as from the energy used to power all the homes in America. It exceeds the global aviation industry, and is on the scale of the Canadian wildfires of 2023.[13]

The risks to investors in energy investments through private funds are illustrated through an examination of fund performance and particular examples of failures. For example, the private equity-backed Limetree Bay Refinery in the U.S. Virgin Islands filed for bankruptcy in 2021, resulting in hundreds of millions in losses for investors in private equity firm Arclight Capital

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[10] McKinsey, Global Private Markets Review 2021, published April 2021

[11] *Private Equity Stakeholder Project, "Private Equity Propels the Climate Crisis" October 2021,* *https://pestakeholder.org/wp-content/uploads/2021/10/PESP_SpecialReport_ClimateCrisis_Oct2021_Final.pdf*

[12] 2024 Private Equity Climate Risks Scorecard, published October 2024 https://www.peclimaterisks.org/2024scorecard/

[13] 2024 Private Equity Climate Risks Scorecard, published October 2024 https://www.peclimaterisks.org/2024scorecard/

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Partners.[14] The Environmental Protection Agency in 2021 invoked emergency powers to shut the facility down just weeks after Arclight resumed operations as part of a revival of the previously mothballed facility.[15]

In 2017, a $2 billion energy-focused private equity fund managed by firm EnerVest collapsed under the weight of its debt and was reduced to virtually nothing when commodity prices in the oil market plunged, causing investors to lose millions.[16]

Private equity investments in coal plants also serve as an illustration of the risks of acquiring assets on the decline. The Institute for Energy Economics and Financial Analysis (IEEFA) pointed out that public pension funds have private fund exposure to coal even as investors increasingly shun fossil fuels. "Right now, investors in fossil fuels in private equity funds are facing a bumpy exit. They face investment losses," said IEEFA's Tom Sanzillo.[17]

One example of private equity's risk appetite in coal is in KKR's failed bet on the Longview Power coal plant in West Virginia. Four years after acquiring the plant out of bankruptcy, KKR landed the plant in its second bankruptcy in 2020, retiring $350 million in debt.[18] Through the plant's restructuring, KKR lost nearly all of its 42 percent equity stake and subordinated debt in the company "with cumulative losses of several hundred million dollars," according to a KKR attorney.[19]

Another example of a troubled coal plant is the General J.M. Gavin coal plant in Ohio, owned by Blackstone Group and Arclight Capital Partners, currently being sold to Energy Capital Partners/Bridgepoint. An analysis by IEEFA noted that "Gavin is the fourth-largest carbon dioxide

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[14] *Laura Sanicola, Tim Mclaughlin "Private equity bet on troubled Caribbean refinery blows up on retirement funds," Reuters, June 3 2021.* *https://www.reuters.com/business/energy/exclusive-private-equity-bet-troubled-caribbean-refinery-blows-up-retirement-2021-06-03/*

[15] *https://www.epa.gov/newsreleases/epa-uses-emergency-powers-protect-st-croix-communities-and-orders-limetree-bay-refinery*

[16] *Wall Street Journal, "From $2 billion to zero: A private-equity fund goes bust in the oil patch,"* *https://www.wsj.com/articles/from-2-billion-to-zero-a-private-equity-fund-goes-bust-in-the-oil-patch-1500210002*

[17] https://ieefa.org/ieefa-u-s-pension-funds-investing-in-ohios-gavin-coal-plant-face-financial-and-reputational-risks/

[18] *S&P Global*, "Longview emerges from bankruptcy, retires $350m in debt" August 3, 2020, https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/longview-power-emerges-from-bankruptcy-retires-350m-in-debt-59724693

Wall Street Journal, Becky Yerak, "KKR-Backed Longview Power Files for Bankruptcy, WSJ Reports KKR - The Fly," April 14, 2020, https://www.wsj.com/articles/kkr-backed-power-company-files-for-bankruptcy-after-tapping-stimulus-funds-11586891236 and https://thefly.com/landingPageNews.php?id=3072249&headline=KKR-KKRbacked-Longview-Power-files-for-bankruptcy-WSJ-reports

[19] *Bloomberg Law*, Yerak; Jeremy Hill, "KKR Power Plant Sought Federal Cash Without Firm's Knowledge," April 17, 2020.

emitter among power plants in the United States, according to the Environmental Protection Agency. In 2021, the plant emitted more than 7.3 million tons of CO_2 during the first six months of the year."[20]

Another indicator of the risks faced by private market investors is the string of bankruptcies in the oil and gas sector in 2020, driven by price swings in oil markets induced by the COVID pandemic. The majority of oil produce bankruptcies were filed by private-equity backed companies.[21] Notably, 2020 saw an increase in bankruptcies with debt loads greater than $1 billion, with an unusually high number relative to the prior six years. More than two thirds (71%) of 2020's multibillion-dollar bankruptcies by oil and gas producers were backed by private equity.[22]

Private energy funds have experienced disappointing returns overall for investors. Based on an analysis of Preqin data, *Bloomberg* reported in April 2020 that oil- and gas-focused funds have been among the lowest-yielding asset classes for private capital over the prior 10 years. The median internal rate of return (IRRs) for these funds was about five percentage points lower than those of comparable buyout firms.[23]

Specific Feedback

General: Applicability

Given the risks posed to communities and investors by private equity fossil fuel investments, CARB should ensure it creates strong regulations to hold both public and private companies accountable for their carbon emissions. Scope 1 and Scope 3 disclosures must also account for the fact that the majority of emissions that may be attributed to a private fund that does business in California will come from the fund's investment portfolio, which may include companies outside of California, and not from the fund or the supply chain directly.

Question 3a: How can CARB ensure regulations address California-specific needs and are also kept current and stay in alignment with standards incorporated into the statute as these external standards and protocols evolve?

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[20] https://ieefa.org/ieefa-u-s-pension-funds-investing-in-ohios-gavin-coal-plant-face-financial-and-reputational-risks/ and https://ampd.epa.gov/ampd/

[21] *Private Equity Stakeholder Project, "Private Equity-backed companies dominate 2020 oil and gas bankruptcies," https://pestakeholder.org/private-equity-backed-companies-dominate-2020-oil-and-gas-bankruptcies/*

[22] *Private Equity Stakeholder Project, "Private Equity-backed companies dominate 2020 oil and gas bankruptcies," https://pestakeholder.org/private-equity-backed-companies-dominate-2020-oil-and-gas-bankruptcies/*

[23] *Rachel Adams-Heard, "Private Equity Can't Escape the Pain of Shale Country's Collapse," Bloomberg, April 1, 2020, https://www.bloomberg.com/news/articles/2020-04-01/private-equity-can-t-escape-the-pain-of-shale-country-s-collapse*

As applied to private funds that do business in California, either directly or through their portfolio companies, we encourage CARB to consider the [Climate Standards for Private Markets Investors](), which builds off the research of the Private Equity Climate Risk consortium.[24] These standards include concrete timelines to ensure private markets portfolios pivot to adhere to a 1.5 degree pathway and adapt for the energy transition in order to reduce financial risk for funds currently tied to fossil fuels investments.

Question 3c: To the extent the standards and protocols incorporated into the statute provide flexibility in reporting methods, should reporting entities be required to pick a specific reporting method and consistently use it year-to-year?

Private funds that do business in California, either directly or through their portfolio companies, should use a reporting method that discloses information substantially similar to what is requested in the [Climate Risk and Energy Transition Questionnaire for Private Equity Managers]().

Conclusion

Thank you again for the opportunity to provide feedback on the implementation of SB 253 and 261, both as amended by SB 219. Strong regulations requiring public and private funds to disclose carbon emissions in their portfolios would be a major step forward in creating climate risk transparency. Such transparency would benefit the public, including investors in private funds, by providing them with consistent, comparable, and decision-useful information about a company's carbon emissions.

Best,

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Private Equity Stakeholder Project

[24] https://peclimaterisks.org/