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Via electronic filing and email

Rajinder Sahota
Deputy Executive Officer for Climate Change and Research
California Air Resources Board
1001 I Street
Sacramento, CA 95814

Re: Information Solicitation to Inform Implementation of SB 253 and SB 261, as amended by SB 219

Dear Ms. Sahota:

Hunton Andrews Kurth LLP (Hunton) submits these comments on behalf of a group of companies which, depending on how the statutes are implemented by the California Air Resources Board (CARB or the Board), could potentially be subject to the requirements of California's new climate disclosure legislation. We appreciate CARB's efforts to seek input prior to proposing regulations to implement these provisions. At the same time, we are concerned with the limited timeframes provided in the legislation to implement the requirements. We are also concerned that CARB will struggle to fulfill the stated aims of the bills that companies be able to rely on their development of documents for other reporting regimes. This element was key to the ability of these bills to be passed by the legislature and was an explicit concern of Governor Newsom when he signed the legislation. Indeed, the Governor would have provided a longer time frame for implementation than the legislature ultimately provided in its adoption of SB 219.

Hunton Andrews Kurth LLP has extensive experience working on issues related to climate change and sustainability reporting as well as in climate change law in California, nationwide, and abroad for companies that are subject to the full range of climate reporting regimes. In our experience, the cost of reporting regimes for greenhouse gases has been substantially understated and underestimated by regulatory bodies. Companies have invested significant sums to comply with U.S. EPA's greenhouse gas reporting regulations as well as with reporting regimes being implemented internationally.

Based on our experience, we urge CARB to reflect the following basic principles in its adoption of regulations to implement the Climate Disclosure Laws in California.

1. Applicability should be clear and as narrow as possible based on the statutory language. It should focus on companies that are doing *substantial and direct* business in California and not (either inadvertently or intentionally) bring in entities that have minor or tangential interactions with the state. CARB needs to balance the aims of obtaining a broad range of information that reaches across the country against the potential consequences of overreaching, particularly at the early stages of the program. Expanding applicability would bring in more information, to be sure, but it would also make the information that is received and reported less useful, less understandable, and ultimately less impactful to the aims of the statutes. We agree with commenters that say the requirements should be clear – and in doing so, CARB must be cautious about taking an easy route of being "clearly broad," and should instead put in the work to define applicability, at least initially, narrowly, so that CARB and reporting entities can gain what is surely necessary experience in implementation before extending the program. It is unfortunate that the legislature did not provide CARB with more time to develop a thoughtful regulatory program. Given the time frame allotted, however, that should be taken as an indication from the legislature that an incremental approach is appropriate—*and intended* by the legislature. If a sweeping and complex regulatory program was intended, the legislature would have provided time for CARB to work with stakeholders and to undertake the normal, iterative California rulemaking process with series of workshops, a formal comment period, and supplemental 15-day notices for fine-tuning the regulatory language in response to formal comments. It did not, and the appropriate response is to move deliberately, but *incrementally,* in the rulemaking process to allow for responsible regulatory development.

2. CARB should explicitly recognize and allow for use of reports developed under other regimes. We think that this can be accomplished consistent with California's Administrative Procedure Act's requirements for clarity in regulations. We understand that the Office of Administrative Law just a few days ago returned the Low Carbon Fuels Standard (LCFS) amendment package to CARB for lack of clarity in several provisions. The climate disclosure regulations can avoid these clarity concerns by setting minimum requirements that rely on other reporting regimes as being sufficient.

3. CARB should not be prescriptive or add requirements that would undermine the ability of companies to use the information developed for other reporting regimes, as is suggested in some of the questions that CARB raises in its documents. As CARB has learned in several programs that it has developed over the years, launching a program like this should be done in steps. Future revisions can add requirements (if appropriate and necessary) once the regulated community and CARB staff develop basic experience with implementing the program. CARB will be well-served to recognize that this program will mature and evolve over the next several years. There will be course corrections. The more that CARB

overshoots the requirements and then has to adjust those requirements, the more costly the program will be—without necessarily achieving the intended goals of transparency.

4. CARB should approach these rules with a compliance mindset, rather than a punitive, enforcement mindset. We are encouraged by CARB's enforcement discretion notice as recognizing the underlying purposes of this legislation, to create transparency around climate emissions for companies that are actively and meaningfully participating in and benefiting from the California economy. Good faith efforts, especially as this program develops, should be the point. Historically, CARB has approached other programs in a more punitive manner, such as with enforcement of the LCFS and of AB32 programs. Errors made by a company from which it obtained no financial benefit have been enforced with proposed penalties in the millions of dollars. Having appropriate penalties for *intentional* false statements is a far cry from the significant costs that are imposed on companies for mistakes—mistakes that the companies often find themselves and self-report to CARB. We hope CARB will agree that there is no place for such an approach in the context of implementing SB 253 and SB 261.

We address below several of CARB's specific questions in its solicitation of input as it prepares for proposing regulations:

I. Applicability

Question 1: Doing Business in California

Question 1(a) asks if CARB should adopt the interpretation of "doing business in California" found in Revenue and Tax Code Section 23101 (RTC § 23101). We believe this definition is overbroad and should not be adopted. RTC § 23101defines "doing business in California" as follows:

> (a) Except as otherwise provided, every corporation "doing business" in this State is subject to tax under Chapter 2. ***"Doing business" is defined as "actively engaging in any transaction for the purpose of financial or pecuniary gain or profit."*** This includes the ***purchase and sale of stocks or bonds, endorsing the notes of a subsidiary corporation by a parent corporation and the leasing of real property by the parent corporation to the subsidiary and other tenants, and liquidating activities consisting of sales, rentals, collections on notes, etc.*** A foreign corporation which engages in a transaction for the purpose of financial or pecuniary gain or profit in California is considered "doing business" in this State whether or not the transaction is considered exclusively engaged in interstate commerce, and is therefore subject to tax under Chapter 2. However, if the only activities of employees of foreign corporations within this State engaging exclusively in interstate commerce are the solicitation of orders for goods to be shipped to customers in this State from points outside this State, the corporations are probably within the purview of Public Law 86-272 (15 U.S.C.

> Sections 381, et seq.). Accordingly, such corporations would not be subject to either a tax measured by income imposed under Chapter 2 or the income tax imposed under Chapter 3. However, the corporation may be subject to the minimum tax imposed by section 23153, Revenue and Taxation Code.
>
> (b) The mere receipt of dividends and interest by a corporation and the distribution of such income to its shareholders does not constitute "doing business." (See section 23102, Revenue and Taxation Code). The corporation, however, is subject to tax under Chapter 3 if its income is from California sources.
>
> (c) As used in this regulation, "Chapter 2" refers to Chapter 2 of Part 11, Division 2 of the Revenue and Taxation Code (beginning with section 23101 of the Revenue and Taxation Code) and "Chapter 3" refers to Chapter 3 of Part 11, Division 2 of the Revenue and Taxation Code (beginning with section 23501, Revenue and Taxation Code).

RTC § 23101 (emphasis added).

The purpose of the RTC is to define what entities must file a tax return – not necessarily to define what entities actually owe taxes in the State of California. In filing a tax return, companies then identify what their operations are in the state, and, then, the substantive tax provisions address whether tax is owed. In numerous instances, companies merely file a return because they have the minimum connection to the state to be required to file a return, but that does not mean they owe taxes.

For SB 253 and SB 261, if CARB were to import the tax code's definition, it would cast a wide net and sweep in companies that are not doing business in the state in the commonly understood sense of that phrase. These companies are not routinely interfacing with consumers in California, are not using California as a basis for generating income, and are not marketing themselves in a way that should bring them within the disclosures mandated by these new statutes. This could not have been the intent of the legislature in enacting these provisions.

As an example, using this definition could bring in and treat similarly, a company that has just one remote employee who relocated to California (e.g., as a result of the pandemic) and a company that has major physical operations in California with hundreds of employees. Clearly, the operations of the latter would be more in line with the legislative intent as compared with the former. To illustrate, the Franchise Tax Board's website applies very low payroll thresholds for "doing business in California," requiring California payroll compensation of only $73,502 in 2024. *See* https://www.ftb.ca.gov/file/business/doing-business-in-california.html. Thus, a company with a remote employee that earns $75,000 annually would be considered to do business in California if CARB adopted the RTC definition. That standard is simply not appropriate to apply for determining if a company is "Doing Business in California" under the climate reporting legislation at issue here. Similarly, the RTC definition includes a value threshold for real and tangible property. Given the value of real estate and goods in California, these are exceedingly low thresholds to consider a business to have sufficient activity in California to trigger reporting under the climate disclosure statutes.

We note that the legislature could have explicitly incorporated the RTC definition into either SB 253 or SB 261, but it chose not to do so. We consider this an indication that CARB should exercise sound judgment in ensuring that the scope is below the magnitude of entities that the legislature contemplated would trigger reporting.

With respect to subsidiaries, we offer the following. Specifically, CARB asks in question 2(b) whether it should track parent/subsidiary relationships to assure companies doing business in California that report under a parent are clearly identified and included in any reporting. CARB should make clear in any regulations that subsidiaries of a parent corporation that are headquartered out of state are not required to report under the parent corporation's report and would only be required to be included if they separately meet the criteria for reporting. For example, a company that operates in California, but that has a wholly-owned subsidiary operating in Utah that does no business in California itself, should not be swept into reporting under these bills. Of course, if a parent company wishes to include subsidiaries not otherwise subject to reporting, that would be up to the parent. In response to question 2(b), if a company does consolidated reporting, which is one reason why it might choose to include out-of-state or in-state subsidiaries, it should not be required to break out the contributions, though it could list the entities that are included in the reported amounts. This will allow for simplified reporting, but it would still provide clarity.

The subsidiary question is a clear example of where CARB should set applicability more narrowly at least to start, while it and regulated entities gain experience. CARB can then assess the real costs of the reporting options it selects and the efficacy of the choices it has made.

II. Standards in Regulation

CARB requests comment on several issues related to the standards applicable to reporting. We appreciate that CARB recognizes that its implementation tasks necessarily rely on protocols and standards developed by external and, in some instances, non-governmental entities. One of the key elements in passage by the legislature and signature by the Governor of this legislation was that duplication of effort, costs, and burdens (including enforcement burdens) be minimized.

We understand that the questions were compiled in the spirit of jumpstarting the regulatory process, given that the legislature provided CARB with little time and no specific funding. That said, we think that CARB's approach to the issue should begin with minimizing burdens and redundant effort when there are already numerous reporting regimes in place upon which companies are relying to develop reports and with which extensive experience already exists.

In other words, the first inquiry should be as to how CARB can allow companies to rely on other existing programs to satisfy their reporting requirements. Then, and only once implementation is underway and experience has been gained, CARB would consider whether there is even a need to "address California-specific needs," as indicated in Question 3(a). The question itself assumes that there are in fact California-specific needs that CARB must "ensure" its regulations address. Those needs have not been identified, and given the nature of this legislation, we do not believe there are such needs.

We note that while California is usually a "first-mover" in areas of environmental law, in this case, other jurisdictions and entities have built substantial infrastructure and even regulations to provide extensive information on Scope 1, 2, and 3 emissions. As CARB is aware, reporting in this area is less precise than in a typical regulatory program because it is necessarily based on protocols and emissions factors, and with respect to Scope 3 emissions, estimates using numerous assumptions. This stands in contrast to programs like the LCFS, where CARB was a first-mover and where there is an intricate credit-based program with a market-based compliance system. The level of precision that applies to the LCFS program is simply not appropriate for implementation of SB 253 and SB 261. Certainly, precision will increase as these programs mature and the regulations can be revisited, but at this juncture, we recommend that CARB work to issue regulations that recognize the purpose of the legislation and allow for experience to inform improvements over time.

Questions 3(b) and 7 ask how CARB can work to minimize duplication of effort by reporting companies under these statutes and about specific protocols that might be used. We believe that CARB should start with a premise of accepting reports generated for other reporting entities. Under SB 253, the legislature recognizes existing protocols, like the Greenhouse Gas Protocol Standards and Guidance and the Greenhouse Gas Protocol Corporate Value Chain (Scope 3) Accounting and Reporting Standard developed by the World Resources Institute and the World Business Council for Sustainable Development. In SB 261, the legislature cites the Final Report of Recommendations of the Task Force on Climate-related Financial Disclosures "or any successor thereto" and "equivalent reporting requirements." HSC 38733(b)(1)(A)(i). While business interests rightly pointed out that these recommendations are inherently designed to be voluntary and to take into account materiality and costs and benefits, the legislature nonetheless proceeded. This decision indicates that companies relying on outside protocols are permitted to do so and that CARB's regulations can and should allow reliance on such reporting protocols. Given the timeline for this rulemaking and for companies to achieve reporting compliance, we strongly urge CARB to take a minimalist approach in these regulations that allows for reliance on voluntary and other regulatory programs to provide estimates of Scope 1, 2, and 3 emissions.

With respect to Question 7, specifically, we note that CARB recognizes that the GHG Protocol allows companies flexibility in areas like boundary-setting, apportioning emissions in multiple ownerships, and others. CARB asks if it should standardize some aspects of these. We encourage CARB not to standardized requirements at this time.

We note that setting a minimum standard that allows companies to rely on and submit reports generated for other reporting entities should not present problems under the clarity requirements of the Administrative Procedure Act, provided it is clear that relying on other accepted reports will satisfy the regulatory obligation.

As discussed above, Question 3(a) asks how CARB should ensure its regulations address California-specific needs and are also kept current and stay in alignment with standards incorporated into the statute as such external standards and protocols evolve. We address Question 3(a) here – after 3(b), which focuses on how CARB can rely on and harmonize with pre-existing standards and regimes, because Question 3(a) starts with a premise of departing from that which has already been developed and assuming "California-specific needs" before the base program is even underway. From a resource perspective both for CARB and for reporting entities, we encourage CARB to move step-wise and thoughtfully to avoid repeated and costly revisions to these requirements over time. As experience is gained, and to the extent that California-specific needs that justify the additional resources to meet those needs are identified, the core regulations can be amended at that time. This fundamental orientation for the regulations is important, and we would be happy to discuss it further as the rulemaking proceeds.

III. Costs and Data Reporting

We suggest that CARB consider the Information Collection Request (ICR) data that U.S. EPA has published and routinely renewed pursuant to the Paperwork Reduction Act with the Office of Management and Budget for 40 C.F.R. Part 98. While in our view, EPA's ICRs routinely underestimate costs of regulations, this structure at least provides CARB with a starting point for analysis of this type of reporting regulation.

CARB must ensure that information provided is able to be protected sufficiently under the Public Records Act. As CARB is aware, data inputs for emissions calculations may include confidential business information. To the extent that using a third party organization would compromise confidential business information, CARB would need to prevent the organization from disclosing such information.

Question 8 asks what options exist for third-party verification or assurance of Scope 3 emissions and what standards should be used to define limited and reasonable levels of assurance. Under SB 253, limited assurance is required beginning in 2026, and reasonable assurance begins in 2030. In the context of Securities Exchange Commission filings, under a limited assurance engagement, the third party would express a conclusion as to whether it is aware of any material modifications that should be made to the disclosure for it to be fairly stated or in accordance with the relevant criteria. For limited assurance, the third party's conclusion is stated as a "negative assurance" regarding whether material misstatements have been identified (e.g., the provider did not find any material misstatements in its review of the submittal). A reasonable assurance involves a more extensive evaluation where the third party opines on whether the subject matter is consistent with the relevant criteria in all material respects. It is an affirmative statement that the submittal is free from material misstatements. Under the MRR cited by CARB in the solicitation, "reasonable assurance" is defined as "a high degree of confidence that submitted data and statements are valid." Although it is not entirely clear, we are concerned that the MRR definition imposes a higher burden of assurance than the SEC imposes on financial statements (and would have imposed under its Climate Disclosure Regulation, which have been stayed pending court review and further action in the current administration). We encourage CARB to adopt assurance definitions that are consistent with financial reporting assurance levels, as these are well understood by service providers and reporting entities alike.

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We appreciate CARB seeking input on this important regulation. Please contact me with any questions about these comments.

Sincerely,

Shannon S. Broome

Shannon S. Broome
Climate Change Practice, Co-Chair