

SUSTAINABILITY: CARBON ACCOUNTING, NET ZERO REPORTING, AND GHG DISCLOSURES

CALIFORNIA LAWS LEADING BUSINESS SUSTAINABILITY EFFORTS

PRESENTED BY: JONATHAN S. STORPER, ESQ.

HANSON BRIDGETT LLP

FEBRUARY 22, 2024

GOING GREEN? TIME TO PROVE IT IN CALIFORNIA

- California's new first-in-the-nation environmental, social, and corporate governance laws mandate companies to comply with required climate disclosures and assurances.
- The new laws are intended to increase transparency, gain data addressing climate change, standardize disclosures, and provide regulators, stakeholders, consumers, and the public with transparent and credible climate information.
- With the 5th largest GDP, where California goes, the world follows.
- Companies should start NOW to gather the data required for compliance.

THE CLIMATE CORPORATE DATA ACCOUNTABILITY ACT (S.B. 253)

- Both public and private businesses with annual revenues more than \$1 billion and doing business in California, regardless of where company is headquartered.
- 5300 companies are likely covered.

THE CLIMATE CORPORATE DATA ACCOUNTABILITY ACT (S.B. 253) - Continued

- The law requires:
 - Beginning in 2026, covered companies must measure and report greenhouse gas (GHG) emissions in conformance with the Greenhouse Gas Protocol standards and guidance, including the Greenhouse Gas Protocol Corporate Accounting and Reporting Standard 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, including guidance for scope 3 emissions calculations that detail acceptable use of both primary and secondary data sources, including the use of industry average data, proxy data, and other generic data in its scope 3 emissions calculations.

THE CLIMATE CORPORATE DATA ACCOUNTABILITY ACT (S.B. 253) - Continued

- Disclosure must be made to an “emissions reporting organization” and made publicly available on a digital platform.
- Assurance performed by independent third-party assurance provider with certain experience and competency requirements. Phased requirements for limited (2026) and reasonable (2030) assurance for scopes 1 and 2; scope 3 assurance requirement (at the limited assurance level) takes effect in 2030.
- Compliance with the California Air Resources Board (CARB) regulations adopted on or before January 1, 2025.

WHAT IS AN “EMISSIONS REPORTING ORGANIZATION”?

- “Emissions reporting organization” means a nonprofit emissions reporting organization contracted by CARB that currently operates a greenhouse gas emission reporting organization for organizations operating in the U.S. and has experience with greenhouse gas emissions disclosure by entities operating in California.

SCOPE EMISSIONS DEFINED

- Scope 1 emissions are direct emissions from owned or controlled sources.
- Scope 2 emissions are indirect emissions from the generation of purchased or acquired electricity, steam, heat, or cooling.
- Scope 3 emissions are indirect upstream and downstream greenhouse gas emissions, other than scope 2 emissions, from sources that the reporting company does not own or directly control and may include, but are not limited to, purchased goods and services, business travel, employee commuting, and processing and use of sold products.

THE CLIMATE CORPORATE DATA ACCOUNTABILITY ACT IN ACTION

- Annual reporting begins in 2026 for the prior fiscal year for scopes 1 and 2; and in 2027 for scope 3 (180 days after publication of scope 1 and 2).
- Consequences of noncompliance: administrative penalties for non-filing, late filing, or not meeting requirements. The maximum yearly penalty is \$500,000.
 - However, misstatements given on a reasonable basis and in good faith of scope 3 emissions will not give rise to a penalty through 2030.
 - Penalties assessed on scope 3 reporting, between 2027 and 2030, may occur for non-filing.
 - Practical impact: could influence Federal (SEC) and other states' regulations.

THE CLIMATE-RELATED FINANCIAL RISK ACT (S.B. 261)

- The law covers all United States businesses with annual revenue over \$500 million and doing business in California, regardless of where a company is headquartered in the U.S.
- Exemptions: Companies regulated by California Department of Insurance, or that are in the insurance business in another state.
- Requires biennial climate-related financial risk report disclosing:
 - The company's climate-related financial risk.
 - The measures adopted to reduce and adapt to such climate-related financial risk.
- Companies must make a copy of the report available to the public on the company's website.

THE CLIMATE-RELATED FINANCIAL RISK ACT IN ACTION

- The biennial reporting requirement begins on January 1, 2026.
- Consequences of noncompliance: administrative penalties not to exceed \$50,000 in a reporting year.
- In imposing penalties for a violation of the law, CARB will consider all relevant circumstances, including:
 - both violator's past and present compliance,
 - whether the violator took good-faith measures to comply,
 - when those measures were taken.

WHAT DOES “DOING BUSINESS” IN CALIFORNIA MEAN?

- S.B. 253 and S.B. 261 apply to companies that "do business" in the state, which is not defined in these two laws.
- Doing business is typically broadly defined in other statutes. This includes:
 - Engaging in any transaction for the purpose of financial gain within California (i.e., having an employee in California).
 - Anticipate the definition of "doing business" to be determined by CARB's regulations implementing the laws.

FIRST STEPS TOWARDS COMPLIANCE TO SB 253 AND 261

- Companies should first determine whether they are a covered company subject to these regulations.
- Companies with an existing reporting practice or assurance should evaluate the extent in which they already comply and determine additional actions.
- Companies should formalize internal leadership, governance, oversight, and policies to review emissions sources and financial risks for compliance with California's laws.
- Companies should consider participating in the CARB's rulemaking this coming year regarding SB 253 and 261.

THE VOLUNTARY CARBON MARKET DISCLOSURES ACT (A.B.1305)

- The law covers any company, public or private that:
 - Operates within California.
 - Purchases or uses VCOs sold in California, and makes claims about achieving net zero emissions, carbon neutrality, or emissions reduction claims (e.g., "net zero" or "carbon neutral").
 - Makes claims in California about significant emission reductions or not adding any net carbon dioxide or greenhouse gas emissions.
 - Note: without guidance from the law, companies should assume that law will be broadly applied.
- Companies must publish disclosures on company website.

VCOS DEFINED

- VCOs are defined as any product sold or marketed in the state that claims to be a greenhouse gas emissions offset, a voluntary emissions reduction, a retail offset, or any like term that connotes that the product reduces or prevents greenhouse gases. VCOs don't include products that represent or correspond to legal or regulatory mandates for reducing or preventing greenhouse gas emissions.

THE VOLUNTARY CARBON MARKET DISCLOSURES ACT: DISCLOSURES AND DATA

- The law requires companies to take a coordinated approach to validating data for VCO projects and should be able to disclose the following:
 - the specific protocol.
 - The project type, location, start date, and project timeline.
 - The durability period for any project.

THE SPECIFIC PROTOCOL

- Provide the specific protocol used to estimate emissions reductions or removal benefits.
- Protocol means a documented set of procedures and requirements to quantify ongoing greenhouse gas reductions or greenhouse gas removal enhancements achieved by an offset project.
- It includes baseline calculations such as specification of relevant data collection and monitoring procedures, emissions factors, and methodologies to account for uncertainty, activity-shifting and market-shifting leakage risks associated with an offset project, and whether an independent third party validated or verified the protocol or results.

THE PROJECT TYPE

- Provide whether the offsets are derived from a carbon removal, or an avoided emission.
- In the case of a project with both carbon removals and avoided emissions, the breakdown of offsets from each.
- Provide the business selling and purchasing the offset, the registry or program, and the project identification number, if applicable.

THE DURABILITY PERIOD

- The durability period for any project that the seller knows (or should know) that greenhouse gas reductions or removal enhancements is less than the atmospheric lifetime of carbon dioxide emissions.
- Durability means the duration over which an offset project operator commits to maintaining its greenhouse gas reductions and removal enhancements.

ACCOUNTABILITY MEASURES

- Companies must disclose details about failed projects: those that aren't completed or don't meet the projected emissions reductions or removal benefits.
- Companies must disclose detail about actions the company, either directly or by contract, will take if the carbon storage projects are reversed or if emissions aren't reduced as planned.

THE VOLUNTARY CARBON MARKET DISCLOSURES ACT IN ACTION

- Some uncertainty as of date law is in effect. Author of law has indicated that the law was intended to go into effect January 1, 2025.
- Consequences of noncompliance: individual violations are subject to a civil penalty of \$2,500 for each day the information is unavailable or is inaccurate on your company's website (not to exceed \$500,000).

UPDATES AND DEVELOPMENTS TO THE NEW GREEN LAWS

- Governor Newsom has recognized that the laws have aggressive implementation deadlines. The legislature may consider amendments to the laws, or that CARB may consider extending the timing of the new laws.
- Assembly Member Jesse Gabriel alerted the Office of the Governor, Attorney General, California Air Resources Board, and Chief Clerk of the Assembly that he intended that AB 1305's first annual disclosure would be on January 1, 2025.
- The U.S. Chamber of Commerce, along with other business groups, filed a constitutional challenge against the State of California and CARB over the laws.

THE BOTTOM LINE

- Companies should act immediately to comply with California's new laws.
- Companies should be prepared for the extra scrutiny and required information about their environmental claims.
- Companies should recognize an increased trend: carbon market regulation is coming, and it's time for companies to pay close attention.
- Companies will need to show evidence on sustainability in transparent, traceable, and accurate disclosures. Companies should conduct due diligence on their purchased carbon offsets, review their existing and future environmental claims, and prepare to verify these claims with data using proper calculation methods.
- Companies should report their required disclosures with the assistance of adequate financial and legal counsel.

QUESTIONS?

Jonathan S. Storper, Esq.

Partner

Hanson Bridgett LLP

Direct No. (415) 995-5040

Email: jstorper@hansonbridgett.com