

California – First State to Enact Climate Reporting Legislation

October 13, 2023

On October 7, 2023, California Governor Gavin Newsom signed into law two expansive climate disclosure bills (SB 253 and SB 261), making California the first state in the U.S. to impose requirements on greenhouse gas (“GHG”) emissions disclosure and mandate reporting on climate-related financial risks. The SB 253 legislation requires both public — and private — U.S. entities that conduct business in California and have total annual revenue in excess of \$1 billion U.S. dollars, to report on their GHG emissions annually and the SB 261 legislation requires entities that conduct business in California and earn at least \$500 million U.S. dollars in revenue to report biennially on their climate-related financial risks. The California legislature’s stated purpose in adopting this legislation is to address the impact of climate change on the state’s residents and economy – a state that has already faced devastating wildfires, sea level rise, drought and extreme weather events, to increase corporate transparency and informed decision making, to standardize climate-related disclosure and to increase corporate accountability in the effort to move toward a net-zero carbon economy. If implemented as adopted, these bills are likely to result in significant costs for a broad swath of U.S. companies doing business in California.

The legislation further advances the ongoing global trend of companies providing more comprehensive climate reporting. California is already a leader in this effort in the U.S., with initiatives such as requiring state pension funds to report climate-related financial risks and establishing the Climate-Related Risk Disclosure Advisory Group.^[1] Thousands of companies globally are already voluntarily disclosing climate-related financial risks, and other jurisdictions, like Illinois and France, are mandating sustainability policies.^[2] At the federal level in the U.S., President Joseph Biden signed an executive order in May 2021 emphasizing the need to address climate-related risks and in March 2022, the Securities and Exchange Commission (“SEC”) proposed a sweeping set of rules that, if adopted, would require publicly traded companies to disclose climate-related impacts on their operations and financial condition.^[3]

However, in the view of the California legislature, current standards for climate risk disclosure fall short in addressing the swiftly escalating climate risks. To that end, the California legislature passed these two bills to establish more consistent, higher-level and mandatory disclosure requirements for all major economic players, and by mandating disclosures from U.S. entities conducting business in California, rather than solely those headquartered within the state, California's intent is to ensure that the impact of this new legislation is as far-reaching as possible.

Climate Corporate Data Accountability Act (SB 253)[\[4\]](#)

SB 253, authored by Senator Scott Wiener (D-San Francisco), establishes GHG emissions disclosure requirements that extend beyond the GHG disclosures contemplated by the SEC's proposed rulemaking released in March 2022. Whereas the SEC's rulemaking would only extend to public companies, the new California legislation applies to **both** public and private entities that are organized in the United States, have total annual revenues exceeding \$1 billion[\[5\]](#) and conduct business[\[6\]](#) in California ("Reporting Entities").[\[7\]](#) The SB 253 legislation is expected to impact over 5,300 companies and will make California the first and only state in the U.S. (so far) that requires companies to disclose their GHG emissions.[\[8\]](#)

Reporting Entities subject to the SB 253 legislation will be required to publicly disclose their Scope 1 and Scope 2 GHG emissions starting in 2026 (on a date to be determined by the state board) and annually thereafter, and, starting in 2027, their Scope 3 GHG emissions, and annually thereafter (within 180 days after publicly disclosing their Scope 1 and Scope 2 GHG emissions) to a newly established statewide emissions reporting organization.

Scope 1 emissions are direct GHG emissions from sources that a Reporting Entity owns or directly controls, regardless of location, including fuel combustion activities.

Scope 2 emissions are indirect GHG emissions from consumed electricity, steam, heat or cooling purchased or acquired by a Reporting Entity, regardless of location.

Scope 3 emissions are indirect upstream and downstream GHG emissions (other than Scope 2 emissions), from sources that the Reporting Entity does not own or directly control and may include purchased goods and services, business travel, employee commutes and processing and use of sold products.

These definitions align with internationally recognized standards like the Greenhouse Gas Protocol, which is also the basis used by the SEC in defining reportable emissions in its proposed rules on climate related disclosures. However, unlike the SEC's proposed rules, which, in addition to requiring the disclosure of Scope 1 and Scope 2 emissions, only require the disclosure of Scope 3 emissions in certain circumstances, the California legislation requires Scope 3 emissions reporting for all Reporting Entities.

The California Air Resources Board ("CARB") will be responsible for developing and adopting regulations to implement this program by January 1, 2025, after considering input from various stakeholders, including contracting with an emissions reporting organization to develop a reporting program to receive and make the required disclosures publicly available. The Reporting Entities will also be required to pay an annual fee to CARB (to be set in an amount sufficient to cover CARB's cost of administering and implementing the bill), to be deposited into the Climate Accountability and Emissions Disclosure Fund, a new fund to be created to fund CARB's activities under this legislation.

The law further requires independent verification of a Reporting Entity's disclosures by a third-party assurance provider with expertise in GHG emissions accounting. Required assurance levels for Scope 1 and Scope 2 emissions will increase from "limited" to "reasonable" in 2030. In 2026, CARB will assess third-party assurance requirements for Scope 3 emissions and may establish a requirement for such engagements by January 1, 2027. Assuming that a higher assurance requirement is not established, starting in 2030, assurance engagements for Scope 3 emissions will be conducted at a "limited" assurance level. Reporting Entities initially will be required to measure and report their emissions following the Greenhouse Gas Protocol's guidelines.^[9] However, starting in 2033 and subsequently every five years, CARB will be authorized to review existing GHG accounting and reporting standards to determine if an alternative standard would better advance the objectives of SB 253.

The legislation requires CARB to structure the GHG emissions reporting in a way that minimizes duplication of effort and allows a Reporting Entity to submit reports prepared to meet other national and international reporting requirements, including any reports required by the federal government, as long as those reports satisfy all of the requirements of SB 253. By July 1, 2027, CARB is required to contract with an academic institution to prepare a report on the public disclosures made by Reporting Entities, and the emissions data disclosed by the Reporting Entities and CARB's report on those disclosures will need to be made accessible to the public through a digital platform within 30 days of receipt.

Failure to comply with these GHG reporting obligations could result in penalties of up to \$500,000 per reporting year imposed on the Reporting Entity, although CARB will consider all relevant circumstances in determining the penalty amount, including the violator's past and present compliance with SB 253 and whether the violator took good faith steps to achieve compliance. There is an express safe harbor provision for misstatements regarding Scope 3 GHG emissions made in good faith with a reasonable basis, and until 2030, penalties relating to Scope 3 reporting will only apply for non-disclosure.

Climate Related Financial Risk Act (SB 261)[\[10\]](#)

SB 261, authored by Senator Henry Stern (D-Los Angeles), requires covered entities to report on their climate-related financial risks on or before January 1, 2026, and biennially thereafter. SB 261 is expected to impact over 10,000 companies.[\[11\]](#)

The law applies to any corporation, partnership, limited liability company or other business entity formed under the laws of California, the laws of any other state of the United States or the District of Columbia, or under an act of the Congress of the United States with total annual revenues in excess of \$500 million dollars and that does business in California[\[12\]](#) (a "Covered Entity"). The climate-related financial risks requiring reporting under this legislation relate to the material risk of harm to immediate and long-term financial outcomes due to physical and transitional risks, including, but not limited to, risks to corporate operations, provision of goods and services, supply chains, employee health and safety, capital and financial investments, institutional investments, financial standing of loan recipients and borrowers, shareholder value, consumer demand and financial markets and economic health.

The climate-related financial risk report must be made in accordance with the framework and disclosures set forth in the Final Report of Recommendations of the Task Force on Climate-Related Financial Disclosures (June 2017) published by the Task Force on Climate-Related Financial Disclosures (TCFD), or any subsequent publication, along with any measures the Covered Entity has taken to mitigate and adapt to the disclosed climate-related financial risks.[\[13\]](#)

The legislation allows for climate-related financial risk reports to be consolidated at the parent company level, even if a subsidiary of a parent company qualifies on its own as a Covered Entity.

If the Covered Entity is unable to complete the report with all of the required disclosures, it must provide as much information as possible, explain any gaps in reporting and outline the steps it will take to provide complete disclosures.

The report will need to be made publicly available on the Covered Entity's website, with the initial report due by January 1, 2026, and biennially thereafter. Unlike SB 253, SB 261 does not require CARB to establish additional regulations or for Covered Entities to submit reports directly to CARB.

However, CARB is required to engage a climate reporting organization to biennially prepare a public report that evaluates the disclosure of climate-related financial risks in industry-specific reports; analyzes systemic and sector-wide climate-related financial risks, including potential impacts on economically vulnerable communities; and identifies any reports that are deemed inadequate or insufficient. The organization would also be responsible for gathering input from various stakeholders regarding the most current and effective methods for disclosing climate-related financial risks, including updates to the definition of "climate-related financial risk" and the related reporting framework or disclosure standards.

Under SB 261, Covered Entities will be required to pay an annual filing fee, to be determined by CARB, to cover CARB's costs of administering and implementing this legislation. Failure to comply with these climate-related financial risk disclosure obligations could result in penalties of up to \$50,000 per reporting year imposed on the Covered Entity, although, as with SB 253, CARB will consider all relevant circumstances in determining the penalty amount, including the violator's past and present compliance with SB 261 and whether the violator took good faith steps to achieve compliance.

Challenges Presented by the New Legislation

In his signing message, Governor Newsom expressed his concerns about the infeasibility of the implementation timelines under both SB 253 and SB 261, and noted that the reporting protocol under SB 253 could result in inconsistent reporting among the applicable Reporting Entities. As a result, he directed his administration to work with the legislature to seek amendments via new legislation in 2024, so it is very likely the implementation deadlines will be extended and the reporting protocols clarified.

The California Department of Finance noted the high cost of implementing SB 253, which will include the need for additional permanent staff at the California Air Resources Board. Governor Newsom similarly expressed concern regarding the overall financial impact of both SB 253 and SB 261 on businesses and instructed CARB to closely monitor the cost impact of implementing the bills and to make recommendations to streamline the programs to ensure achieving the goals of “full transparency and consistency” with respect to GHG emissions and encouraging businesses to “adopt practices . . . to minimize and avoid” climate-related risks.

Preparation Strategies

As with California’s board diversity legislation, the SEC’s climate change reporting rules and other “ESG” focused legislation and rulemaking proposed or adopted at the Federal or state level, the new California legislation may draw significant legal challenges from various stakeholders given the sweeping scope and nature of the requirements. Nevertheless, given the time-intensive nature of collecting and synthesizing GHG emissions data and the likelihood that many companies will need to establish new internal systems to comply with these new requirements as currently adopted, businesses subject to SB 253 or SB 261 should consider taking steps early on to proactively prepare for these new regulations:

- **Conduct Gap Analysis.** Entities already disclosing their GHG emissions data may need to make adjustments to align with the new requirements, while other entities may need to start their preparations from scratch. Conduct a comprehensive analysis to identify gaps between existing climate reporting practices and the requirements of SB 253 and SB 261.
- **Internal Organization.**

1. Assign internal responsibility and establish collaborative workflows among teams involved in the reporting process;
 2. Implement or refine the protocols for monitoring and tracking GHG emissions and climate-related risks;
 - 3i. Consider forming a dedicated climate reporting committee, comprising members from relevant departments;
 - 4i. Focus on increasing the proficiency of relevant teams in understanding the language, guidelines and frameworks of climate regulation and reporting, particularly as outlined in the Greenhouse Gas Protocol and the Task Force on Climate-Related Financial Disclosures;
 5. Initiate the process of obtaining and understanding GHG emissions data across the business' entire value chain.
- **Engage Outside Advisers.**
 - 1i. Secure experienced GHG emissions accounting firms with industry-specific expertise.
 - 2ii. Engage an independent third-party assurance firm for preparation of the assurance report required under SB 253
 - 3iii. Consult with legal advisors regarding any legal implications related to the new disclosure requirements. Please contact the Proskauer team to learn more.
 - **Participate in the Rulemaking Process.** Actively monitor the rulemaking process initiated by CARB. There will be a public notice and comment period, during which businesses should consider submitting comments. This engagement is essential to ensure that the implementing regulations align with industry practice needs and considerations.

[1] See CA Govt Code § 7510.5 (2022); Press Release, Governor's Office of Planning and Research, [State of California launches Advisory Group on Climate Risk Disclose](#) (April 2021).

[2] See State of Illinois' Sustainable Investing Act (PA 101-473) (2020); France's Energy Transition Law (Article 173) (2015).

[3] See [Climate-Related Financial Risk: \(Net\) Zeroing in on Key Private Equity Considerations under the Biden Administration’s Executive Order](#), Proskauer (June 2021), [SEC Proposes Broad New Climate Change Disclosure Requirements, Proskauer](#) (March 2022).

[4] Available at [SB-253 Climate Corporate Data Accountability Act](#).

[5] Applicability will be determined based on the Reporting Entity’s revenue for the prior fiscal year. [SB-253 Climate Corporate Data Accountability Act](#).

[6] “Existing law defines ‘doing business’ in California as engaging in any transaction for the purpose of financial gain within California, being organized or commercially domiciled in California, or having California sales, property or payroll exceed specified amounts: as of 2020 being \$610,395, \$61,040, and \$61,040, respectively.” [Senate Floor Analysis, SB 253](#) (September 11, 2023) (citing CA Revenue & Tax Code § 23101 (2022)).

[7] A “Reporting Entity” can be a partnership, corporation, limited liability company, or other business entity formed under the laws of California, the laws of any other state of the United States or the District of Columbia, or under an act of the Congress of the United States.

[8] See [Assembly Floor Analysis, SB 253](#) (September 2, 2023).

[9] See Greenhouse Gas Protocol, *supra* note 8, at 62-67.

[10] Available at [SB-261 Greenhouse gases: climate-related financial risk](#).

[11] See [Senate Floor Analyses, SB 261](#) (September 12, 2023).

[12] See Footnote 6, *supra*.

[13] A Covered Entity will have satisfied its reporting obligations under SB 261 if it prepares a publicly accessible biennial report that includes climate-related financial risk disclosure information (i) pursuant to a law, regulation, or listing requirement issued by any regulated exchange, national government, or other governmental entity, or (ii) voluntarily using a framework that meets reporting requirements similar to those published by the Task Force on Climate-related Financial Disclosures or the requirements of the International Financial Reporting Standards Sustainability Disclosure Standards, as issued by the International Sustainability Standards Board.

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