Published on *The National Law Review* https://www.natlawreview.com

California to Require Climate Disclosures from Large Companies

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The California Legislature recently passed two new laws that impose significant climate-related disclosure obligations on many businesses. The passage of SB 261 and SB 253 are the latest steps in a growing trend to mandate climate-related disclosures. The laws will require companies to disclose climate-related financial risks and greenhouse gas (GHG) emissions beginning in 2026. Governor Newsom has indicated that he will sign the bills into law.

Key Takeaways

What is happening? California has adopted two bills—SB 253, the Climate Corporate Data Accountability Act, and SB 261, focused on

“Greenhouse gases: climate-related financial risk” and related disclosure (collectively, the “Acts”). The Acts create significant disclosure requirements regarding greenhouse gas (GHG) emissions and climate-related financial risks for large companies doing business in California.

What is the background? The Acts are two of three bills in California’s Climate Accountability Package. The California legislature attempted to pass similar legislation in prior legislative sessions, most recently with SB 260, which largely mirrored SB-253 but ultimately failed on the floor of the Assembly.

Who is impacted? SB 253 applies to all companies that do business in California and have a total global annual revenue of over $1 billion. SB 261 applies to companies that do business in California with a total global annual revenue of over $500 million. Clarity on how total revenue will be evaluated, for example, net versus gross revenue or if the calculation will include affiliate companies that do not operate in the United States, will likely be a key focus of forthcoming California Air Resources Board (CARB) rulemaking.

SB 253. The Climate Corporate Data Accountability Act

Under SB 253, any partnership, corporation, limited liability company, or other U.S. business entity with total global annual revenues over $1 billion dollars that does business in California is subject to the disclosure requirements.

Disclosure Requirements

Reporting entities must publicly and annually disclose their scopes 1, 2, and 3 GHG emissions on the following schedule:

Beginning in 2026, annually and publicly disclose to the emissions reporting organization its scope 1 emissions and scope 2 GHG emissions for the entity's prior fiscal year.

Beginning in 2027, and annually thereafter, publicly disclose its scope 3 GHG emissions no later than 180 days after it discloses its scope 1 and scope 2 GHG emissions for the prior fiscal year.

The Act adopts the Greenhouse Gas Protocol's definitions of scope 1, scope 2, and scope 3 emissions. Under the Act, covered entities must use the Greenhouse Gas Protocol Corporate Accounting and Reporting Standard and the Greenhouse Gas Protocol Corporate Value Chain (Scope 3) Accounting and Reporting Standard to calculate emissions. The Act requires that public disclosures be made in a manner that is easily understandable, accessible, and "maximizes access" for consumers, investors, and other stakeholders.

The Act also requires disclosures to:

Include the name of the reporting entity and any fictitious names, trade names, assumed names, and logos used by the reporting entity.

Be structured to allow reporting entities to submit reports that meet other national and international reporting requirements.

Consider acquisitions, divestments, mergers, and other structural changes that can impact GHG reporting.

The Act also requires reporting entities to pay an annual fee upon filing their disclosure. The fee amount has not been determined, but must be an amount sufficient to cover the state board's costs for administering and implementing the Act.

Assurance Requirements

Reporting entities must obtain an assurance engagement, performed by an independent third-party assurance provider, of their public disclosure, and provide the assurance report as part of their disclosure to the emissions reporting organization. The Act takes a phased approach to the type of assurance required.

Initially, assurance is only required for scope 1 and scope 2 emissions and must be performed at a limited assurance level beginning in 2026, and at a reasonable assurance level in 2030. CARB may establish, on or before January 2027, but no later than 2030, an assurance requirement for scope 3 emissions, which would be performed at a limited assurance level. Assurance providers must meet explicit qualifications outlined in the law, including experience in evaluating greenhouse gas emissions reporting. The qualifications for assurance providers are to be reviewed and updated by CARB as necessary in 2029.

Penalties

CARB may seek administrative penalties for non-filing, late filing, or failure to meet the Act’s requirements. Administrative penalties must be imposed and recovered in administrative hearings and must not exceed $500,000 in a reporting year. CARB must consider “all relevant circumstances” when imposing penalties, **including:**

> The violator’s past and present compliance with the Act’s requirements.
> Whether the violator took good faith measures to comply with the Act and when the violator took those measures.

The Act provides a safe harbor for Scope 3 emissions, noting that a reporting entity will not be subject to an administrative penalty for any misstatements regarding scope 3 emissions disclosures made with a reasonable basis and disclosed in good faith. In addition, between 2027 and 2030, penalties on scope 3 reporting are authorized only for non-filing entities.

SB 261. Greenhouse gases: climate-related financial risk

SB 261 requires a “covered entity” – any partnership, corporation, limited liability company, or other U.S. business entity with total global annual revenues over five hundred million dollars that does business in California – to biennially prepare a climate-related financial risk report (“report”). The entity’s revenue for the prior fiscal year determines whether a covered entity meets the threshold.

Reporting Requirements

The report must disclose (1) the business' climate-related financial risk, in accordance with the recommended framework and disclosures contained in the Final Report of Recommendations of the Task Force on Climate-Related Financial Disclosures (June 2017) or any subsequent publication thereto, and (2) the measures taken to reduce and adapt to the disclosed climate-related financial risks.

Companies must make this report publicly available on their own website on or before January 1, 2026, and update it biennially thereafter. Companies are also required to pay an annual fee to CARB to cover the Board's costs in administering this section, the amount of which has yet to be established. If a covered entity fails to complete a report, it must provide the recommended disclosures to the best of its ability, provide a detailed explanation for any reporting gaps, and describe steps it will take to prepare complete disclosures. Failure to provide these disclosures or adequately outline steps to compliance may lead to administrative penalties not to exceed $50,000 per reporting year.

The Act also requires covered entities to pay an annual fee upon filing their disclosure. The fee amount has not been determined, but must be an amount sufficient to cover the state board's costs for administering and implementing the Act.

More Mandatory Climate-Related Disclosures

to Come

Other climate-related disclosure laws are being developed at the federal level and in jurisdictions around the world.

Last year, the Securities and Exchange Commission (SEC) issued proposed rules that would require publicly traded companies to include certain climate-related disclosures in their registration statements and periodic reports, including information about climate-related risks reasonably likely to have a material impact on their business or financial condition. The SEC is expected to finalize these rules in October 2023—although the SEC's deadlines for this rule have slipped before. Unlike the SEC's proposed rules, which only would apply to public companies, California's laws apply broadly to all companies meeting the threshold requirements.

The Department of Defense, General Services Administration, and National Aeronautics and Space Administration have also proposed to amend the Federal Acquisition Regulation (FAR) to require certain federal contractors to disclose their GHG emissions and climate-related financial risk and set science-based targets to reduce their emissions. The proposed FAR amendments received significant contractor push-back but remain under consideration.

The European Commission adopted the first set of European Sustainability Reporting Standards (ESRS) over the summer, which contain the reporting

requirements outlined in the Corporate Sustainability Reporting Directive. There are 12 ESRSs, two of which are cross-cutting standards that apply to all sustainability matters, while the remaining 10 focus on specific environmental, social, and governance issues.

Taken together, these emerging initiatives each have their own requirements and nuances, which differ from disclosure requirements in other jurisdictions as well as some of the voluntary disclosure frameworks. It is vital to understand these differences to ensure timely compliance with the suite of reposing and disclosure obligations now facing many large businesses in the United States.

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National Law Review, Volumess XIII, Number 269

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