Climate Disclosure Spotlight Shifts To 2 Calif. Laws

By **Loyti Cheng and David Zilberberg** (January 14, 2025)

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With the election of Donald Trump spelling the all-but-certain demise of the U.S. Securities and Exchange Commission's climate disclosure rules, California's S.B. 253 (the Climate Corporate Data Accountability Act) and S.B. 261 (the Climate-Related Financial Risk Act) currently stand as the nation's only broadly applicable climate disclosure legal requirements, with initial data gathering requirements potentially beginning as early as this year.

While California regulators have recently provided some breathing room for these near-term requirements, companies should begin to determine whether they are subject to the laws and — if they are — begin to put the right measures in place to comply.

Unlike the SEC climate disclosure rules, which consist of hundreds of Federal Register pages of regulatory text and commentary, S.B. 253 and S.B. 261, signed into law on Oct. 7, 2023, are relatively sparse in language, which is both a blessing and a curse.

On the one hand, the core requirements of these laws are fairly straightforward — S.B. 253 requires in-scope companies to annually report their greenhouse gas emissions, and S.B. 261 requires in-scope companies to publish a biennial climate-related financial risk report. On the other hand, the laws leave the regulated community with limited guidance as to key details regarding scope and substantive disclosure requirements.

That said, on Dec. 16, 2024, the California Air Resources Board solicited comments from the public on a number of topics to assist in its implementation of the two laws. Whether CARB regulation or guidance will aid in-scope companies in making sense of the very skeletal legislative text remains to be seen.

Key Requirements and Timelines

The following chart highlights the similarities and differences between the two laws.

	S.B. 253	**S.B. 261**
Who has to disclose?	• Reporting entity • Annual revenues in excess of $1 billion • Does business in California • Formed in the U.S.	• Covered entity • Annual revenues in excess of $500 million • Does business in California • Formed in the U.S.
What has to be disclosed?	Scopes 1, 2 and 3 • Greenhouse gas emissions for the prior fiscal year	Climate-related financial risks

When and how often?	• 2026 (scopes 1 and 2) • 2027 (scope 3)	By Jan. 1, 2026, and every two years thereafter
Assurance	Scopes 1 and 2 • Beginning in 2026: limited assurance • Beginning in 2030: reasonable assurance Scope 3 • Beginning in 2030: limited assurance	N/A
Implementation	CARB to issue regulations on or before July 1, 2025	Disclosure standards are self-implementing

Key Interpretive Issues

Doing Business in California

As noted above, S.B. 253 and S.B. 261 apply to companies formed in the U.S. that do business in California with revenues in the prior fiscal year exceeding $1 billion, in the case of S.B. 253, or $500 million, in the case of S.B. 261.

While the laws do not define what "doing business in California" means, the legislative history references the definition of that phrase in the California tax code,[1] which defines the phrase expansively to include "actively engaging in any transaction for the purpose of financial or pecuniary gain or profit" in California; being "organized or commercially domiciled" in California; or having California sales, property or payroll above specified amounts — in 2024, these amounts were $735,019, $73,502 and $73,502, respectively.[2]

In its Dec. 16 comment request, CARB specifically sought input on whether this definition should formally be adopted. As a practical matter, under this definition, companies with minimal California connections, such as having one employee, could be considered in scope.

Treatment of Affiliated Corporate Entities

S.B. 253 and S.B. 261 also fail to provide guidance on how the scope provisions apply to affiliated corporate entities where some — or all — of them don't exceed the revenue thresholds separately but do exceed the thresholds on an aggregate basis, or if only certain affiliates have the requisite California contacts.

On the one hand, both laws appear to assess applicability based on the revenues and business activities of a discrete legal entity — "a partnership, corporation, limited liability company, or other business entity … with total annual revenues … and that does business in California."

On the other hand, the legislative histories of the laws provide some support for a reading that treats corporate affiliates on a consolidated basis. The Senate floor analysis memo for

S.B. 253 states that an "estimated 5,344 companies … would be required to report under this bill,"[3] which is based on an analysis that appears to consider entities on a consolidated basis.

Without further guidance from California, it is not possible to definitively resolve this ambiguity. However, one practical approach might be to look at a company's accounting policies in determining whether aggregation is appropriate.

For example, if a parent corporation with the requisite California contacts has several subsidiaries and reports revenues in excess of $1 billion for the entire corporate group on a consolidated basis, it would seem advisable for the parent corporation to consider itself in scope for S.B. 253, even if each corporate entity within the group is below the threshold on an individual basis.

We would also note that under the Greenhouse Gas Protocol, the standards that CARB is required to incorporate in its forthcoming regulations under S.B. 253, parent corporations are generally required to include the emissions of subsidiaries in their reporting. This would suggest that a parent corporation in the above scenario may be required to include the emissions of its subsidiaries, even if those subsidiaries have no California contacts.

In addition, in its Dec. 16 comment request, CARB specifically sought input about methods in which it can track parent/subsidiary relationships to ensure that in-scope companies that report under a parent are clearly identified and included in any reporting requirements.

Content of a Climate-Related Financial Risk Report under S.B. 261

As noted above, S.B. 261 requires in-scope companies to publish on their website a climate-related financial risk report on or before Jan. 1, 2026, and biennially thereafter, but provides little guidance as to the content of this report. Specifically, S.B. 261 provides as follows:

- The report is to cover a company's (1) "climate-related financial risk," defined as "material risk of harm to immediate and long-term financial outcomes due to physical and transition risks"; and (2) measures adopted to reduce and adapt to climate-related financial risk.
- The report must disclose a company's climate-related financial risk in accordance with the June 2017 recommendations of the Task Force on Climate-related Financial Disclosures, or TCFD, or any successor frameworks. International Financial Reporting Standards, or IFRS, Sustainability Disclosure Standards are considered an acceptable alternative.

Importantly, S.B. 261 does not require companies to publish a TCFD report, but rather a report of a company's material climate-related financial risks in accordance with the TCFD or IFRS framework. However, the TCFD framework calls for a range of information other than a company's climate-related risks, such as certain metrics, targets, and information regarding its governance and risk management systems.

S.B. 261 does not appear to require reporting of this information. Instead, S.B. 261 appears to incorporate the section of the TCFD framework relating specifically to reporting on a company's climate-related risks. These standards are grouped under the "strategy" section of the TCFD framework.

Note that the TCFD's — as well as the IFRS' — disclosure standards for the reporting of climate-related financial risk includes a requirement to conduct a scenario analysis, which is an exercise that tests the resilience of a company's climate-risk strategy taking into consideration different climate-related scenarios. S.B. 261 would therefore appear to incorporate this requirement.

The TCFD specifically requires companies to test a scenario where global temperature rise is limited to 2 degrees Celcius or lower — i.e., a scenario that assumes some level of economywide decarbonization necessary to realize this result — and analyze how this scenario would affect the company. Beyond this requirement, TCFD guidance — and similar guidance in the IFRS — provides companies with the flexibility to vary the rigor and scope of their scenario analysis based on the level of risk that climate change is anticipated to pose.

S.B. 253 and S.B. 261 are currently subject to an ongoing legal challenge in the U.S. District Court for the Central District of California in U.S. Chamber of Commerce v. CARB. It should be noted that in this litigation, the state of California filed a brief defending S.B. 261 by advancing a rather narrow reading of the reporting requirement under that law:

> [Under S.B. 261, c]ompanies must disclose their actual policies and actual planning pertaining to climate-related financial risks as assessed by the company. … [I]f an entity does not currently evaluate climate-related risks, its disclosure could state merely that (i.e., that it has no climate-related governance, strategy, risk management plans, or metrics and targets), and still comply with S.B. 261's disclosure requirements.[4]

Under this reading, in-scope companies would merely be required to report what they actually do to assess climate risk, and would not have to conduct any assessment — such as a scenario analysis — that goes beyond their existing practices. Whether California adopts this interpretation in administering or enforcing the law remains to be seen, but this interpretation would appear to be inconsistent with the statutory text of S.B. 261.

Although the disclosure standards under S.B. 261 would appear to be self-implementing, in its Dec. 16 comment request, CARB specifically sought input on the timing and other aspects of S.B. 261 reporting requirements.

Key Considerations for Companies

Near-Term Compliance Priorities and the CARB Enforcement Notice

If they haven't already, companies should determine whether they are subject to S.B. 253 and S.B. 261. If they are in scope, companies should assess any gaps that exist between their current climate-related disclosure practices and the disclosures required under the laws, and determine what steps need to be taken to address those gaps.

The nearest-term compliance obligations under the laws are Scope 1 and 2 emissions reporting, which will be due sometime in 2026 covering emissions during the 2025 fiscal year.

However, on Dec. 5, CARB issued an enforcement notice stating that for 2026 reporting of 2025 Scope 1 and 2 greenhouse gas emissions, in-scope companies can report their emissions "that can be determined from information the reporting entity already possesses or is already collecting" as of the date of the notice, and that "CARB will not take

enforcement action for incomplete reporting against entities, as long as the companies make a good faith effort to retain all data relevant to emissions reporting for the entity's prior fiscal year."[5]

This is a sensible move by CARB given that the current timetable effectively requires in-scope companies to collect emissions data before knowing what the rules are going to require them to report, as those rules are not due to be issued until July 1, 2025.

In light of the notice, in-scope companies that currently collect and report Scope 1 and 2 greenhouse gas emissions data can continue their current practices and plan on complying with S.B. 253 based on this data for their 2026 report and await further rulemaking from CARB to prepare for 2027 reporting of 2026 greenhouse emissions, which will cover Scopes 1, 2 and 3 emissions.

However, in-scope companies that currently do not collect any Scope 1 and 2 greenhouse gas emissions data are advised to begin the process of doing so starting in 2025. CARB is unlikely to consider not collecting any data to constitute good faith efforts under the enforcement notice. We would note that a very basic Scope 1 and 2 greenhouse gas emissions data inventory is relatively straightforward to put into place for most companies.

CARB Comment Request and Rulemaking

As noted above, CARB issued a notice on Dec. 16 seeking comments from the public on a number of topics to assist CARB in implementing the two laws.

For example, CARB notes that the Greenhouse Gas Protocol, which CARB is required to use as the basis for developing and adopting regulations under S.B. 253, provides companies with flexibility in a number of areas, and seeks input on whether greenhouse gas emissions reporting should be standardized instead of maintaining this flexibility.

Other topics for which CARB is seeking comment include the appropriate definition of "does business in California," methods to ensure CARB regulations are aligned with evolving third-party standards referenced in the laws, and ways to minimize duplication of effort for companies that separately report climate-related information under other legal regimes.

The comment period ends on Feb. 14. Companies are advised to participate as appropriate in this process and continue to follow the rulemaking process.

Federal Legal Challenge

All of this may become moot if the legal challenge to S.B. 253 and S.B. 261 currently pending in the Central District of California succeeds. The legal challenge seeks to invalidate the laws on the grounds that they violate the First Amendment and the supremacy clause of the U.S. Constitution, and constitutional limitations on extraterritorial regulation.

On Nov. 5, the court denied the plaintiffs' motion for summary judgment for impermissibly compelling speech in violation of the First Amendment. According to the court, the factual record wasn't sufficiently compelling to support a facial challenge to the laws, which required the plaintiffs to show that the unconstitutional applications of the laws "substantially outweigh[ed]" applications of the law that are constitutional. While this decision allowed the laws to remain in place for now, the litigation will continue to discovery.

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[1] Cal. Rev. and Tax Code § 23101.

[2] https://www.ftb.ca.gov/file/business/doing-business-in-california.html.

[3] 05/23/23 - Senate Floor Analyses, https://leginfo.legislature.ca.gov/faces/billAnalysisClient.xhtml?bill_id=202320240SB253.

[4] Defendants' Opposition to Plaintiffs' Motion for Summary Judgment on Claim I, Chamber of Commerce v. CARB in the U.S. District Court for the Central District of California.

[5] https://ww2.arb.ca.gov/sites/default/files/2024-12/The%20Climate%20Corporate%20Data%20Accountability%20Act%20Enforcement%20Notice%20Dec%202024.pdf.