The Implementation and Legal Risks of California’s New Climate Disclosure Laws

By Abby Husselbee

December 20, 2023

In September 2023, California’s legislature passed two bills that require public and private companies that meet monetary thresholds to disclose their greenhouse gas (GHG) emissions and their climate-related financial risks.¹ That same month, the legislature passed a related third bill that requires companies to disclose their voluntary carbon offsets and provide evidence supporting their net-zero emissions claims.² On October 7, 2023, Governor Newsom signed all three bills into law.³ The California Air Resources Board (CARB) is now tasked with developing regulations to implement the GHG emissions and financial risk disclosure laws. The offset and net-zero disclosure law takes effect without implementing regulations as it gives state prosecutors civil enforcement authority.

With these disclosure laws, the state aims to inform investors and empower consumers, but many factors will determine how well they accomplish these goals. For example, the GHG emissions and financial risk laws give CARB significant flexibility to define which businesses it regulates. Even before CARB starts to develop the implementation proposals, opposition groups have argued that California’s disclosures will be too costly and it is likely they will challenge the laws and implementing rules in court.

In this piece, I explain what California’s three laws require and describe implementation questions and litigation risks; explain federal preemption risks related to the Security and Exchange Commission’s (SEC) climate-risk disclosure proposal; and evaluate legal criticisms of the laws, including arguments related to the dormant Commerce Clause doctrine.

The Climate Corporate Data Accountability Act (SB-253) and Greenhouse Gases: Climate-Related Financial Risk (SB-261)

Both laws require disclosures from public and private companies “doing business” in California. The Climate Corporate Data Accountability Act (SB-253, hereinafter the GHG

---

emissions disclosure law), requires entities\(^4\) with total annual revenues over $1 billion to disclose their scope 1, 2, and 3 GHG emissions, using the World Resource Institute and World Business Council for Sustainable Development’s Greenhouse Gas Protocol.\(^5\) Companies must provide third-party audits of their submissions.\(^6\)

Greenhouse Gases: Climate-Related Financial Risk (SB-261, hereinafter the financial risk law), requires entities\(^7\) with total annual revenues over $500 million to post their climate-related financial risks on their own websites and describe how they plan to mitigate those risks.\(^8\)

Both laws require CARB to develop implementing regulations. Specifically, the laws require CARB to take several actions:

- hire an experienced emissions reporting organization to collect the GHG emissions disclosures and make them public on a website;
- collaborate with an academic institution to publish a report on the GHG emissions disclosures; and
- hire an experienced climate reporting organization to write a biennial report on the financial risk and adaptation disclosures.

The laws also direct CARB to impose penalties for noncompliance by companies.\(^9\) If an entity fails to report its GHG emissions as required,\(^10\) CARB may impose an administrative penalty

\(^4\) Defined as “corporation[s], partnership[s], limited liability company[ies], or other business entity[ies] formed under the laws of [California], the laws of any other state...or the District of Columbia, or under an act of the Congress of the United States.” The Data Accountability Act calls regulated companies reporting entities but the Financial Risk Act refers to the same kinds of organizations as “covered” entities.

\(^5\) In keeping with the protocol, the GHG emissions disclosure law defines scope 1 as “all direct greenhouse gas emissions that stem from sources that a reporting entity owns or directly controls regardless of location, including, but not limited to, fuel combustion activities;” scope 2 emissions as “indirect greenhouse gas emissions from consumed electricity, steam, heating, or cooling purchased or acquired by a reporting entity, regardless of location” and scope 3 emissions as “indirect upstream and downstream greenhouse gas emissions, other than scope 2 emissions, from sources that the reporting entity does not own or directly control.” These emissions “may include, but are not limited to, purchased goods and services, business travel, employee commutes, and processing and use of sold products.” S.B. 253, 2023-2024 Leg. (Cal. 2023). After 2033, CARB is no longer bound to the Greenhouse Gas Protocol and could use other reporting standards. S.B. 253, 2023-2024 Leg. (Cal. 2023).

\(^6\) S.B. 253, 2023-2024 Leg. (Cal. 2023).

\(^7\) Using the same definition as S.B. 253.

\(^8\) S.B. 261, 2023-2024 Leg. (Cal. 2023).


\(^10\) For the GHG emissions disclosure law, CARB may impose penalties for “non filing, late filing, or other failure to meet the requirements of [the law].” CARB must also consider whether the company took good faith to comply with the law and whether the company has complied with the law in the past. Until 2030, CARB may only impose a penalty on scope 3 reporting if an entity fails to file their scope 3 emissions. S.B. 253, 2023-2024 Leg. (Cal. 2023)
of up to $500,000. If an entity fails to report its financial risk or publishes an inadequate or insufficient report,\textsuperscript{11} CARB may impose a penalty of up to $50,000.

California’s legislature designed the GHG emissions disclosure law to streamline industry requirements with other disclosure regimes by directing CARB to write regulations that "minimize[] duplication" with disclosures for other jurisdictions provided those disclosures are at least as comprehensive as California’s.\textsuperscript{12} Similarly, the financial risk law directs CARB to accept disclosures prepared for “any regulated exchange, national government, or other governmental entity.”\textsuperscript{13}

**The Voluntary Carbon Market Disclosures Business Regulation Act (AB-1305)**

In addition to these two high-profile disclosure laws, California’s legislature also passed the Voluntary Carbon Market Disclosures Business Regulation Act (AB-1305, \textit{hereinafter} the offsets and net-zero law).\textsuperscript{14} This law is broad in terms of scope and applicability. It requires disclosure of offsets as well as evidence supporting net-zero claims. Additionally, unlike the other two laws, the offsets and net-zero law does not include any monetary thresholds, but it does prescribe several categories of companies that must post disclosures.

First, the law requires companies marketing or selling voluntary carbon offsets in California to disclose the following on their website for each carbon offset project:

- which protocol the company uses to estimate emissions reductions or removal benefits;
- the project’s location, timeline, and start date;
- any changes in the project, including dates and quantities of the changes;
- the type of project (e.g., carbon removal, avoided emissions);
- whether the project meets any nonprofit or legal standards;
- the durability period for any project that the seller knows or should know (if less than the atmospheric lifetime of carbon dioxide);
- any third-party validation of the project;
- annual emissions reduced or carbon removed; and
- if a seller fails to meet projected emissions or removal benefits, the law requires sellers to disclose any “accountability measures” they take.

\textsuperscript{11} For the financial risk law, CARB may impose penalties for “a covered entity that fails to make the report required by this section publicly available on its internet website or publishes an inadequate or insufficient report.” CARB must also consider whether the company took good faith to comply with the law and whether the company has complied with the law in the past. S.B. 261, 2023-2024 Leg. (Cal. 2023).
\textsuperscript{12} S.B. 253, 2023-2024 Leg. (Cal. 2023).
\textsuperscript{13} S.B. 261, 2023-2024 Leg. (Cal. 2023).
\textsuperscript{14} A.B. 1305, 2023-2024 Leg. (Cal. 2023).
Second, the law requires companies that operate within California or that purchase or use offsets sold within the state to make certain disclosures if they “make[] claims” about net-zero or GHG emissions. Such companies must disclose on their website:

- who they are buying the offset from;
- the project identification number (if there is one);
- the offset registry or program and the project name from the registry or program (if there is one);
- the type of project type (e.g., carbon removal, avoided emission) and location;
- which protocol the seller uses to estimate emissions reductions or removal benefits;
- any third-party validation of the project.

Third, and most significantly, the law applies to companies that do not purchase offsets but “make[] claims” related to net zero. Although the law’s purpose is to regulate companies that market, purchase, use, and sell of voluntary carbon offsets, the law also requires companies that operate or “make[] claims” within California to disclose “all information” describing:

- how they “determined” the accuracy of such claims about net zero, their GHG emissions, or related claims about products;
- how they are measuring progress toward their goals, and
- whether they have third-party verifications of their claims.

Unlike the GHG emissions and financial risk laws, the voluntary carbon offsets and net-zero law does not require CARB or any other agency to write implementing regulations. However,

---

15 “An entity that purchases or uses voluntary carbon offsets that makes claims regarding the achievement of net zero emissions, claims that the entity, related entity, or a product is ‘carbon neutral,’ or makes other claims implying the entity, related entity, or a product does not add net carbon dioxide or greenhouse gases to the climate or has made significant reductions to its carbon dioxide or greenhouse gas emissions shall disclose on the entity’s internet website all of the following information pertaining to each project or program:” The law does not further define the phrase “makes claims.” A.B. 1305, 2023-2024 Leg. (Cal. 2023).

16 For example, the Legislative Counsel’s Digest reads “[t]his bill would require a business entity that is marketing or selling voluntary carbon offsets, as defined, within the state to disclose … The bill would also require an entity that purchases or uses voluntary carbon offsets that makes claims regarding the achievement of net zero emissions or other, similar claims, as specified, to disclose… The bill would require an entity that makes these claims to disclose…” (emphasis added).

17 “An entity that makes claims regarding the achievement of net zero emissions, claims that the entity, a related or affiliated entity, or a product is ‘carbon neutral,’ or makes other claims implying the entity, related or affiliated entity, or a product does not add net carbon dioxide or greenhouse gases, as defined in Section 38505, to the climate or has made significant reductions to its carbon dioxide or greenhouse gas emissions, as described in Section 38505, shall disclose on the entity’s internet website all of the following information pertaining to all greenhouse gas emissions associated with its claims.” A.B. 1305, 2023-2024 Leg. (Cal. 2023).

18 The law requires the company to post “All information documenting how, if at all, a ‘carbon neutral,’ ‘net zero emission,’ or other similar claim was determined to be accurate or actually accomplished and how interim progress toward that goal is being measured. This information may include, but not be limited to, disclosure of independent third-party verification of all of the entity’s greenhouse gas emissions, identification of the entity’s science-based targets for its emissions reduction pathway, and disclosure of the relevant sector methodology and third-party verification used for the entity’s science-based targets and emissions reduction pathway.” A.B. 1305, 2023-2024 Leg. (Cal. 2023).
it authorizes the California attorney general and district, city, and county attorneys to enforce the law through penalties. Prosecutors can charge companies who violate any section of this law $2,500 per day, up to $500,000, for each violation of the law.\textsuperscript{19} Thus, California’s enforcement offices will make implementing decisions for the law.

**Implementation questions we are watching**

Governor Newsom signed the three bills into law, but several implementation questions remain. For example, the GHG emissions law gives CARB significant discretion to “adopt or update any other regulations that it deems necessary and appropriate to implement this section,”\textsuperscript{20} and CARB’s interpretation of this latitude could be significant.

Below are some of the biggest implementation issues we will be watching.

*How CARB defines “does business”*

Both the GHG emissions and the financial risk laws apply to companies that meet the monetary thresholds and “do business” in California. However, neither law defines “does business in California.” Thus, CARB will determine the phrase’s meaning through its implementing regulations. While the statute does not indicate a preference for CARB to adopt an existing definition, the agency may look to other examples under existing laws. CARB has not previously defined the term on its own, but other agencies have applied the term broadly. For example, under California’s Franchise Tax Board, a company does business in California if it:

- “engage[s] in any transaction for the purpose of financial gain within California”;
- is “organized or commercially domiciled in California”;
- has sales, personal property, or payroll in California in excess of $690,144, $69,015, or $69,015 respectively; or
- has more than 25% of its sales, personal property, or payroll in the state.\textsuperscript{21}

Under the other definition from California’s Corporate Code, a company does business in the state if it “enter[s] into repeated and successive transactions” in California “other than interstate or foreign commerce.”\textsuperscript{22}

The approach CARB takes will affect how many companies the laws regulate. Thus, the agency is likely to receive significant feedback on this point and other aspects of its discretion during notice and comment.

\textsuperscript{19} California has existing greenwashing laws that prosecutors enforced as early as 2011. See, *California v. Endo Plastics*, Docket No. 30-2011-00518091-CU-MC-CJC (Cal. Super. Ct. 2011). Thus, this law may work with existing greenwashing and state consumer protection regimes that prohibit false claims.

\textsuperscript{20} S.B. 253, 2023-2024 Leg. (Cal. 2023).

\textsuperscript{21} Cal. Rev. & Tax. Code § 23101.

\textsuperscript{22} Cal. Corp. Code § 191(a).
How prosecutors interpret “operates” and other aspects of their discretion

Under the carbon offset and net-zero law, the requirements apply to companies that buy, market, use, sell, “operate,” or “make[] claims” in California. However, the law does not require implementing regulations, and prosecutors and courts will determine which companies they penalize for violations of the law. This and other prosecutorial decisions may further clarify the definitions of key terms, though other political factors often contribute to prosecutorial decisions.23

When California’s reporting obligations commence

Companies have a short timeline to prepare compliance with the laws. They must start recording their 2025 scope 1 and 2 emissions to report in 2026, and their 2026 scope 3 emissions and financial risk for reporting in 2027. Companies can face penalties when the regulations take effect; however, CARB will only assess penalties for a narrow set of scope 3 violations until 2030.24

The GHG emissions law requires CARB to issue final regulations to implement the emissions reporting requirements by Jan. 2025. Before CARB can finalize the rule, the agency will release a proposed rule, accept comments on the proposed rule, and conduct other stakeholder engagement. Despite these clear timeline provisions, Governor Newsom’s signing statement indicated that the laws’ deadlines may be impractical. He asked his administration to work with the bills’ authors to address these issues.25 However, unless the legislature passes an amendment to the bills in the 2024 session, these timelines are unlikely to change.

23 California elects its prosecutors, so a range of factors can contribute to prosecution decisions.
24 Before 2030, CARB cannot assess penalties on scope 3 emissions if the company is late or files an inadequate report. However, CARB can assess penalties if a company fails to file their Scope 3 emissions. The GHG emissions law requires companies to measure their scope 3 emissions using the Greenhouse Gas Protocol standards and guidance for 2027 to 2033 emissions. After 2033, the law authorizes CARB to adopt other globally-recognized accounting standards. CARB may assess alternative standards every 5 years after 2033. For some industries, scope 3 may represent the majority of companies’ emissions, but data collection methods and calculations for scope 3 emissions are still likely to evolve in the coming years. For example, EPA notes that “many organizations will improve the accuracy of scope 3 emissions over time and expand to include more categories as adequate data become available.” EPA, Scope 3 Inventory Guidance, https://www.epa.gov/climateleadership/scope-3-inventory-guidance (last visited Nov. 2, 2023). Standardization across industries could increase accuracy over time.
While politics are likely to drive any legislative changes, many large companies will soon have to disclose their GHG emissions and financial risks under programs from other jurisdictions. These companies are likely to be more prepared for disclosure with each passing year. For example, beginning in 2025, the European Union (EU) will begin phasing in requirements to file sustainability disclosures that will apply to certain US companies. Beginning in 2029, many US companies will have to comply with these EU requirements. For a detailed list of additional international disclosure regimes, their applicability, and their timelines see EELP Research Assistant Eric Zhao’s (JD 2025) table on Global Climate Disclosure Regimes. For a comparison of California’s and the EU’s financial risk and GHG emissions disclosure timelines see the chart below.

---

**EU and California GHG Emission and Financial Risk Disclosure Timelines**

<table>
<thead>
<tr>
<th>2025</th>
<th>2026</th>
<th>2027</th>
<th>2028</th>
<th>2029</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>California Data Accountability Act (SB 253); Financial Risk (SB 261)</strong></td>
<td>CARB must adopt regulations for scope 1, 2, 3 emissions</td>
<td>Regulated entities must start reporting scope 1 and 2 emissions and climate-related financial risk</td>
<td>Regulated entities must start disclosing scope 3 emissions</td>
<td>US companies that generate a net turnover of more than €150 million in the EU that have a large European subsidiary, a subsidiary listed on a European market, or have a large European branch must file disclosures</td>
</tr>
<tr>
<td><strong>The EU Corporate Sustainability Reporting Directive (CSRD (EU) 2022/2464)</strong></td>
<td>Large entities that are already subject to the Non-Financial Reporting Directive must file a disclosure. This category encompasses large companies that are listed on an European exchange and have more than 500 employees</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

---

26 If the SEC does release a final climate-risk disclosure rule, it is not clear what deadlines it would set. In the proposal, the SEC proposed deadlines “assuming that the effective date of the proposed rules occurs in December 2022 and that a registrant has a December 31 fiscal year-end.” The Enhancement and Standardization of Climate-Related Disclosures for Investors, 87 Fed. Reg. 21,334, 21,392 (Apr. 11, 2022).

27 The EU’s emission and financial risk disclosure regime is likely more comprehensive than what CARB will require. Companies covered under the EU program must report on their operations, business models, and their scope 1, 2, and 3 emissions (not accounting for offsets or GHG removal), as well as other environmental, social, and governance factors. Many expect that CARB will allow companies complying with both jurisdictions to submit their EU disclosures to California. The EU also allows companies to satisfy their requirements by submitting a disclosure to their home jurisdiction that is “equivalent” to the EU’s standards. However, the EU has not yet determined which standards are “equivalent.” Commission Delegated Regulation of 31.7.2023 supplementing the 2013/34/EU of the European Parliament and of the Council as regards sustainability reporting standards, p. 9 N. 26; p. 1 N. 3.
The timing for the offset and net-zero law, however, is even sooner as companies must add their offset and net-zero disclosures to their websites by January 1, 2024. Assuming this deadline is not adjusted, the California requirements will be effective before any requirements that may result as part of the EU’s Green Claims directive, which is only a proposal at this time.

**Opponents may argue a final SEC rule preempts the California program**

This spring, the SEC may finalize its climate risk disclosure rule, which would regulate many of the same companies as California’s law. Opponents of the California rules may try to argue that the SEC rule, if finalized as proposed, preempts California’s program. While Congress has not explicitly preempted state disclosure rules, courts have sometimes found implied preemption in other circumstances where the federal government intended to impose a ceiling or create a uniform system of federal regulations. California could mitigate this risk by allowing companies to submit their SEC disclosures to comply with the state’s laws. Implied preemption cases are challenging for petitioners to raise successfully, as courts are often reluctant to find implied preemption where Congress did not clearly intend it. Additionally, many states already require climate risk disclosures from insurance companies, which the SEC acknowledged in the economic analysis of its proposal.

---

28 On Nov. 30, 2023, the offset bill’s author filed a letter with the Chief Clerk of the Assembly stating that his intent was for the first disclosures to be due on January 1, 2025. This letter does not have legal effect, but the author does state that he will be filing a letter to the Assembly Daily Journal when the legislature reconvenes in January 2024. See Letter from Jesse Gabriel to Sue Parker on Legislative Intent—Assembly Bill No. 1305 (Nov. 30, 2023), https://www.politico.com/f/?id=0000018c-3b62-d0ce-a98c-7f6a88a50000.


30 The SEC and California will regulate an overlapping, but separate group of companies. Unlike California, the SEC will not regulate private companies. California will not regulate public companies who fall below the annual revenue thresholds.


33 In some ways, the laws are similar to the SEC’s proposal. For example, the SEC proposed to require companies to report their climate-related financial risks and their scope 1 and 2 emissions. For more on the SEC’s proposal see Sara Dewey’s [Signs of Progress on Corporate Climate Disclosure Ahead of SEC’s Final Rule](https://www.politico.com/f/?id=0000018c-3b62-d0ce-a98c-7f6a88a50000).

34 Courts have used the “presumption against preemption” inconsistently in recent years, but is still sometimes invoked by the court. See Jay Sikes & Nicole Vanatko, Federal Preemption: A Legal Primer, R45825 (2019).

Potential dormant Commerce Clause challenges

If opponents challenge the implementing regulations under the dormant Commerce Clause doctrine, California has successfully defended such challenges on other rules, and those insights will likely influence CARB’s approach.

Under the dormant Commerce Clause doctrine, courts first consider whether a state law discriminates against out-of-state economic interests on its face, in its purpose, or through its practical effects.\(^{36}\) If a state law does not discriminate, courts may also perform the *Pike* balancing test, in which they evaluate whether a law imposes burdens on interstate commerce that are “clearly excessive” in relation to the described local benefits.\(^{37}\) Under *Pike*, courts uphold a law with “only incidental effects” on interstate commerce unless it determines that the burdens are clearly excessive.

Earlier this year, in *National Pork Producers Council v. Ross*, the Supreme Court narrowed the range of potential dormant Commerce Clause challenges.\(^{38}\) While the Court scrapped the dormant Commerce Clause’s extraterritoriality prong and rejected pork producers’ *Pike* claims as applied,\(^{39}\) the Court upheld the *Pike* balancing test for use in future cases. Thus, many expect opponents will try to apply that in any challenges to the rules.\(^{40}\)

In such a challenge, the compliance costs will be a key consideration because under *Pike*, courts evaluate whether the burdens on commerce are excessive relative to their potential benefits.\(^{41}\) California’s Chamber of Commerce,\(^{42}\) the American Banking Association,\(^{43}\) and

---


\(^{38}\) 598 U.S. 356 (2023).

\(^{39}\) Although the Supreme Court rejected a per se rule against state laws with extraterritorial effects, the Chief Justice’s concurrence would allow courts to consider extraterritoriality effect in future *Pike* balancing test cases.

\(^{40}\) For more on the dormant Commerce Clause doctrine, including how California has defeated dormant Commerce Clause challenges in the past, see State Resource Guide: Drafting a Clean Fuel Standard to Manage Legal Risks. For more on *National Pork*’s fractured opinion and the recent changes to the dormant Commerce Clause doctrine, see Ari Peskoe’s recent analysis.

\(^{41}\) In his signing statement, Governor Newsom told CARB to monitor costs, and the agency could use its discretion to respond to such concerns.


many other industry organizations expressed concerns that compliance with California’s GHG emissions and financial risk laws will be too costly, and Governor Newsom directed CARB to monitor these costs.\textsuperscript{44} Pike arguments, however, are usually challenging for plaintiffs—and though Justices Sotomayor and Kagan recently upheld the test in their \textit{National Pork} concurrence, they directed courts to proceed “with caution.”\textsuperscript{45}

Next Steps

Though implementation questions remain, these three laws will provide a window into companies net-zero target setting and implementation strategies. We will continue following CARB’s stakeholder engagement and rulemaking processes as well as other jurisdictions’ relevant requirements. Agencies in California must complete a rulemaking calendar in January, and we should know more on CARB’s likely timing in the new year.\textsuperscript{46} For updates on the SEC’s rule, follow our Financial Regulation, Climate Change, and Climate-related Risk Disclosure Regulatory Tracker page.

\textsuperscript{44} Some large companies, including Apple, expressed support for the bill. Isla Binnie, \textit{Apple Endorses California Bill to Oblige Companies to Report Carbon Footprint}, Reuters (Sep. 8, 2023) https://www.reuters.com/sustainability/apple-Endorses-california-bill-oblige-companies-report-carbon-footprint-2023-09-08/.

\textsuperscript{45} \textit{National Pork}, slip op. at 3 (Sotomayor, J., concurring). See also \textit{Yamaha v. Jim’s Motorcycle Inc.}, 401 F.3d 560, 568 (4th Cir. 2005).