CALIFORNIA ENACTS LANDMARK ESG LEGISLATION

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INTRODUCTION

On 7 October 2023, California Governor Gavin Newsom signed into law landmark legislation mandating corporate climate and climate-related financial risk disclosures. Together, SB 253 and SB 261 apply to public and private companies with annual revenues above certain thresholds and will impose Scope 1, 2, and 3 GHG emissions reporting requirements.

CA SENATE BILL 253, THE *CLIMATE CORPORATE DATA ACCOUNTABILITY ACT*

Senate Bill 253 takes broad aim at public and private businesses that have more than US$1 billion in annual revenues and do business in California. Beginning in 2026, such companies will be required to report Scope 1 (direct) and Scope 2 (indirect) greenhouse gas emissions, with Scope 3 greenhouse gas emissions (those that are generated up and down the company's value chain, such as transportation-related emissions) required to be reported beginning in 2027. In preparation for these requirements, the California Air Resources Board (CARB) will adopt regulations by 1 January 2025 to provide further guidance. Disclosure must be consistent with the Greenhouse Gas Protocol standards and guidance, and reporting businesses will be required to obtain third party assurance of their disclosures.

The requirements of SB 253 go beyond comparable portions of the SEC's proposed climate-related disclosure rules. Chairman Gensler has stressed that the SEC will take steps to ensure private companies bear no reporting burdens in response to comments from concerned lawmakers. Sen. Jon Tester (D-MT) and Rep. Dan Meuser (R-PA) in particular have both expressed concern about the potential reach of the SEC's proposed rules, and stated that the SEC and its actions have already unduly burdened private companies during respective Senate Banking Committee and House Financial Services Committee hearings.

SB 253 requires CARB to promulgate disclosure requirements based on the GHG Protocol Corporate Accounting and Reporting Standard and the GHG Protocol Corporate Value Chain (Scope 3) Accounting and Reporting Standard developed by the World Resources Institute and the World Business Council for Sustainable Development. The SEC's proposed rules do not go so far as to require a particular reporting standard, and Chairman Gensler has been extremely hesitant for the SEC to mandate use of a specified framework. For example, in response to Rep. Andy Ogles's (R-TN) concerns during a hearing that attempting to impose environmental standards quickly leads into the realm of the arbitrary, Chairman Gensler insisted that both the proposed climate-related disclosure rules and the SEC's recently finalized "Names Rule" are meant to ensure transparency, and that the SEC is "not an environmental regulator."

Democratic members from California, however, strongly support the new California legislation. Led by Reps. Juan Vargas (D-CA) and Adam Schiff (D-CA), 26 representatives from the California delegation signed a letter to Chairman Gensler on 12 October 2023 urging him to include Scope 3 greenhouse gas reporting requirements in the final SEC rules. They lauded SB 253, stating that it "virtually eliminates the cost of compliance with a federal Scope 3 disclosure requirement" for public companies subject to SB 253.

CA SENATE BILL 261, THE *CLIMATE-RELATED FINANCIAL RISK ACT*

SB 261 will require companies doing business in California with annual revenues in excess of US$500 million to provide a publicly available report outlining the company's climate-related financial risks and the measures adopted by the company to reduce and adapt to those risks. These disclosures are to be provided in accordance with the framework established by the Task Force on Climate-related Financial Disclosures (TCFD). In both SB 253 and SB 261, "doing business in California" remains undefined, and Governor Newsom's comments during the signing ceremony suggest that modifications may be needed.

SB 261's definition of climate-related financial risk is taken as "material risk of harm to immediate and long-term financial outcomes due to physical and transition 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." This is an expansion and clarification of previous definitions of the concept, such as that found in CA Govt Code § 7510.5.

LOOKING AHEAD

Despite speculation thatpressure from Democrats in Congress and the new California laws will spur the SEC to publish final climate-related disclosure rules more quickly, or that they could catalyze the SEC to include Scope 3 greenhouse gas emissions reporting requirements in the final rule, Chairman Gensler has reiterated that the SEC does not like to do things "against a clock" and that it will consider the full range of feedback before issuing the final rule. Moreover, potential legal challenges to the scope and extent of SB 253 and SB 261 are likely.

In any case, SB 253 and SB 261 are the most recent action in global regulatory efforts focused on sustainability disclosures, particularly with respect to greenhouse gas emissions. Corporate entities increasingly are providing sustainability disclosures in response to investor calls for greater disclosure of material financial risks. It is anticipated that standards issued by the International Sustainability Standards Board (ISSB) will create a global framework for corporate disclosures to help meet emerging regulatory requirements in California, Europe, and elsewhere. The firm's Public Policy and Law Group is uniquely positioned to advise clients on the rapidly changing global landscape of sustainability-related regulations and disclosures.

RELATED RESOURCES

To learn more about the current state of ESG in American politics, as well as the firm's role in this space, please visit our previous publications, including:

- "GOP ESG Bills Await US House Floor Consideration";

- “The ESG Debate Heats Up: State AGs Investigating Asset Manager Involvement in ESG Initiatives and Related Proxy Voting”;
- “ESG Investing and Proxy Voting: DOL's New Final Rule”;
- “SEC Adopts Final Rule Requiring Additional Proxy Voting Disclosures”;
- “Déjà Vu All Over Again: SEC Reverses 2020 Proxy Rules Changes and Proposes Shareholder Proposal Rule Changes”;
- “SEC Takes First Step Toward Standardized ESG Disclosures for Funds and Investment Advisers”;
- “SEC Issues Climate-Related Risk Disclosure Rule Proposal”; and
- “2023 ESG State Legislation Wrap Up”

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