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PERSPECTIVE

# Practical advice for companies preparing for California's new emissions laws

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California Gov. Gavin Newsom signed two broad-reaching bills imposing robust climate disclosure obligations into law on Oct. 7: Senate Bill 253 (SB 253), also known as the Climate Corporate Data Accountability Act, and Senate Bill 261 (SB 261), also known as the Climate-Related Financial Risk Act.

SB 253, which applies to companies doing business in California with annual revenues exceeding $1 billion, requires qualifying companies to disclose (i) their Scope 1 emissions (direct emissions from a company's operations) and Scope 2 emissions (indirect emissions from purchased electricity, heating, and cooling) starting in 2026 and (ii) their Scope 3 emissions (indirect emissions associated with a company's value chain) starting in 2027. Sen. Bill No. 253 (2023-2024 Reg. Sess.) § 2. Further, qualifying companies are required to have their Scope 1 and 2 emissions reporting audited by a third-party and their Scope 3 emissions reporting reviewed by a third-party starting in 2030. *Id.* Importantly, all reporting must adhere to Greenhouse Gas Protocol (GHGP) standards, which were created following the Paris Climate Agreement to provide a standardized measurement of greenhouse gas emissions, and be publicly accessible through a nonprofit registry organization to be selected by the California Air Resources Board (CARB). *Id.* Non-compliance with SB 253 could result in penalties of up to $500,000 per year. *Id.*

SB 261, which applies to companies doing business in California with annual revenues exceeding $500 million, requires qualifying companies to report certain climate-related financial risks, including risks to corporate operations, the provision of goods and services, supply chains, the financial standing of loan recipients and borrowers and shareholder value, to CARB by Jan. 1, 2026 (and biennially thereafter). Sen. Bill No. 261 (2023-2024 Reg. Sess.) § 2. Importantly, reports must also be made publicly available on a qualifying company's website, include a description of the measures being taken to mitigate identified risks and follow the guidelines established by the Task Force on Climate-Related Financial Disclosures (TCFD). *Id.* Non-compliance with SB 261 could result in penalties of up to $50,000 per year. *Id.*

While SB 253 and SB 261 are similar to the Securities and Exchange Commission's (SEC) proposed emissions disclosure rules that are expected to be finalized this month, there are notable differences. In particular, the SEC's proposed rules apply to publicly traded companies and emphasize the disclosure of Scope 1 and Scope 2 emissions; Scope 3 emissions are only required if certain conditions are met. The Enhancement and Standardization of Climate-Related Disclosures for Investors, 87 Fed. Reg. 21,334, 21,345 (Apr. 11, 2022) (to be codified at 17 C.F.R. pts. 210, 229, 232, 239, and 249). By contrast, California's legislation applies to both public and private companies and, in the case of SB 253, mandates the disclosure of all three emission types. Sen. Bill No. 253, *supra*, at § 2.

Companies preparing for the implementation of SB 253 and SB 261 should consider taking the following initial steps in the near term:

**1. Determine whether the laws apply to you**

a. *Determine whether your company is "doing business" in California.* As described in Section 23101 of the California Revenue and Taxation Code, a company is considered to be "doing business" in California if it, among other things: (i) engages in an in-state transaction for financial gain; (ii) is commercially domiciled or organized within the state; (iii) incurs in-state sales tax in excess of approximately $690,000 in 2022; or (iv) incurs in-state property or payroll taxes in excess of approximately $69,000 in 2022. Rev. & Tax. Code § 23101 (2022). Given the complexities of the analysis, consult your legal and tax advisors when making this determination. Importantly, US subsidiaries of non-US companies may be subject to these disclosure obligations.

b. *Determine whether any exemptions or consolidated reporting rules apply.* For example, insurance companies regulated by the California Department of Insurance are fully exempt from SB 261 but are not exempt from SB 253. Sen. Bill No. 261, *supra*, at § 2. Further, a subsidiary may not need to report separately if its parent company prepares a consolidated report.

**2. Familiarize yourself with GHGP standards (SB 253) and TCFD recommendations (SB 261)**

a. *GHGP* standards. A widely used set of guidance materials developed by the World Resources Institute and the World Business Council for Sustainable Development, GHGP standards cover the accounting and reporting of various greenhouse gasses as outlined by the Kyoto Protocol. "*About GHG Protocol*," Greenhouse Gas Protocol (Oct. 12, 2023), https://ghgprotocol.org/about-us.

b. *TCFD Recommendations.* Contemplates disclosure related to four core pillars: (i) Governance (including the board's oversight of climate-related risks and opportunities); (ii) Strategy (including a description of climate-related risks and opportunities the company has identified over the short, medium and long term); (iii) Risk Management (including the company's processes for identifying and assessing climate-related risks); and (iv) Metrics and Targets (including disclosure of the metrics and targets used by the organization to assess and manage, respectively, climate-related risks and opportunities). "*Recommendations of the Task Force on Climate-related Financial Disclosures,*" T.C.F.D. (Oct. 12, 2023), https://www.fsb-tcfd.org/recommendations/.

**3. When available, familiarize yourself with specific CARB regulations.** While SB 253 and SB 261 provide a broad framework, CARB will be required to implement specific rules and regulations by Jan. 1, 2025. Sen. Bill No. 253, *supra*, at § 2. Of particular interest will be whether disclosures prepared in accordance with commonly used accounting frameworks (i.e., the "big three") would satisfy SB 253's requirements, as none currently fully align with GHGP standards. And, because the rulemaking process will likely involve public notice and comment, consider participating.

**4. Gather internal and external resources, and implement necessary processes, to reliably track and report emissions**

a. *Internal Resources.* This may include hiring internal experts, providing training to applicable members of your team, building out governance processes and identifying carbon-emitting assets within your business, including sources of indirect emissions within your supply chain.

b. *External Resources.* This may include engaging third-party auditors and carbon accounting platforms, including to build auditable, investor-grade emissions calculations, ensuring adherence to GHGP standards, TCFD recommendations and, when available, CARB regulations. In collaboration with internal resources, use a carbon accounting platform to begin collecting emissions data in 2025 to meet the initial 2026 reporting requirements. Note that third-party auditors and platforms may become inundated with requests, so consider reaching out early.

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