

SENATE JUDICIARY COMMITTEE
Senator Thomas Umberg, Chair
2023-2024 Regular Session

SB 1036 (Limón)
Version: February 6, 2024
Hearing Date: April 9, 2024
Fiscal: Yes
Urgency: No
CK

SUBJECT

Voluntary carbon offsets: business regulation

DIGEST

This bill makes it unlawful to engage in certain conduct related to voluntary carbon offsets.

EXECUTIVE SUMMARY

Carbon offsetting is an activity that compensates for, or balances out, greenhouse gas emissions generated by an organization through its activities and operations. Essentially, an entity that wants to mitigate its greenhouse gas emissions can pay another entity or person to eliminate, reduce, or refrain from greenhouse gas emissions, *offsetting* the first party's emissions.

Verifying that these emissions are actually being offset is core to voluntary carbon offsets. Unlike the state's cap and trade program, the voluntary carbon offset market is largely unregulated. This has driven concerns that there is rampant fraud in the industry and that many of these offsets are essentially worthless.

Identical to SB 390 (Limón, 2023), which passed out of this Committee last year, this bill seeks to use existing deceptive practices law to explicitly outlaw fraudulent claims and other misconduct in this industry and subject it to the civil enforcement mechanisms that already exist. The bill also painstakingly defines key terms related to voluntary offset markets. The ultimate aim of the bill is to incentivize greater self-regulation within the offsets markets and improve the overall quality of offsets being offered to Californians. This bill is author sponsored. It is supported by NextGen California and various environmental advocacy organizations. It is opposed by a variety of industry members, including Capricorn Investment Group. The bill passed the Senate Environmental Quality Committee on a 5 to 0 vote.

PROPOSED CHANGES TO THE LAW

Existing law:

- 1) Establishes the Unfair Competition Law (UCL), which provides a statutory cause of action for any unlawful, unfair, or fraudulent business act or practice and unfair, deceptive, untrue, or misleading advertising, including over the internet. (Bus. & Prof. Code § 17200 et seq.)
- 2) Defines unfair competition for purposes of the UCL to mean and include any unlawful, unfair or fraudulent business act or practice and unfair, deceptive, untrue or misleading advertising and any act prohibited by Chapter 1 (commencing with Section 17500) of Part 3 of Division 7 of the Business and Professions Code. (Bus. & Prof. Code § 17200.)
- 3) Establishes the False Advertising Law (FAL), which proscribes making or disseminating any statement that is known or should be known to be untrue or misleading with intent to directly or indirectly dispose of real or personal property. (Bus. & Prof. Code § 17500 et seq.)
- 4) Provides remedies for individuals who have suffered damages as a result of fraud or deceit, including situations involving fraudulent misrepresentations. (See Civil Code §§ 1709-1710, 1572-1573.)
- 5) Makes it unlawful for a person to make an untruthful, deceptive, or misleading environmental marketing claim, whether explicit or implied. (Bus. & Prof. Code § 17580.5.)
- 6) Defines “greenhouse gas” to include the following gases: carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons, sulfur hexafluoride, and nitrogen trifluoride. (Health & Saf. Code § 38505.)
- 7) Defines terms related to the cap-and-trade program, including the California Air Resources Board’s (CARB) Compliance Offsets Program. (Title 17 CCR, Section 95802)

This bill:

- 1) Makes it unlawful for a person to do the following:
 - a) verify an offset project for the purposes of issuing a voluntary carbon offset if the person knows or should know that the greenhouse gas (GHG) reductions or GHG removal enhancements of the offset project are unlikely to be quantifiable, real, and additional;

- b) certify or issue a voluntary carbon offset if the person knows or should know that the GHG reductions or GHG removal enhancements of the offset project related to the voluntary carbon offset are unlikely to be quantifiable, real, and additional;
 - c) maintain on a registry a voluntary carbon offset if the person knows or should know that the GHG reductions or GHG removal enhancements of the offset project related to the voluntary carbon offset are unlikely to be quantifiable, real, and additional;
 - d) market, make available or offer for sale, or sell a voluntary carbon offset if the person knows or should know that the GHG reductions or GHG removal enhancements of the offset project related to the voluntary carbon offset are unlikely to be quantifiable, real, and additional;
 - e) market, make available or offer for sale, or sell a voluntary carbon offset if the person knows or should know that the durability of the voluntary carbon offset's GHG reductions or GHG removal enhancements is less than the atmospheric lifetime of carbon dioxide emissions, unless the person explicitly markets the voluntary carbon offset as not being physically equivalent to the climate impact of carbon dioxide emissions;
or
 - f) market, make available or offer for sale, or sell a voluntary carbon offset if the person knows or should know that the atmospheric lifetime of the GHGs associated with the voluntary carbon offset's GHG reductions or GHG removal enhancements is less than the atmospheric lifetime of carbon dioxide emissions, unless the person explicitly markets the voluntary carbon offset as not being physically equivalent to the climate impact of carbon dioxide emissions.
- 2) Specifies that violations are not a crime but are subject to all available civil remedies applicable to a violation of the article in which it is found within the Business and Professions Code.
- 3) Defines the relevant terms.

COMMENTS

1. California's consumer protection laws

The Legislature has long considered consumer protection to be a matter of high importance. State law is replete with statutes aimed at protecting California consumers from unfair, dishonest, or harmful market practices. These consumer-protection laws authorize consumers to enforce their own rights and seek remedies to make them whole.

The UCL (Bus. & Prof. Code § 17200) provides remedies for “anything that can properly be called a business practice and that at the same time is forbidden by law.” (*Cel-Tech Communications, Inc. v. Los Angeles Cellular Telephone Co.* (1999) 20 Cal.4th 163, 180 [citations omitted].) The UCL provides that a court “may make such orders or judgments . . . as may be necessary to restore to any person in interest any money or property, real or personal, which may have been acquired by means of such unfair competition.” (Bus. & Prof. Code § 17203; *see also Korea Supply Co. v. Lockheed Martin Corp.* (2003) 29 Cal.4th 1134, 1146 [“An order for restitution, then, is authorized by the clear language of the [UCL.”].) The law also permits courts to award injunctive relief and, in certain cases, to assess civil penalties against the violator. (Bus. & Prof. Code §§ 17203, 17206.)

The False Advertising Law (FAL) proscribes making or disseminating any statement that is known or should be known to be untrue or misleading with intent to directly or indirectly dispose of real or personal property. (Bus. & Prof. Code § 17500 et seq.) Violators are subject to a civil penalty not to exceed \$2,500 for each violation in an action brought by the Attorney General or by any district attorney, county counsel, or city attorney. (Bus. & Prof. Code § 17536.) Similar to the UCL, the FAL provides that a person may bring an action for an injunction or restitution if the person has suffered injury in fact and has lost money or property as a result of a violation of the FAL. (Bus. & Prof. Code § 17535.)

2. Cleaning up the voluntary carbon offset market

Carbon offsets operate where a certain entity absolutely must emit carbon dioxide and so provides for the same amount of the greenhouse gas to be removed from the atmosphere by other means to compensate. Offsets were historically centered on the planting or protection of trees, which absorb carbon dioxide, however, the term has since been applied to a variety of environmental efforts globally:

The vast majority of offsets available fall into a category called “avoided emissions.” These are projects that either protect forests, provide people with alternatives to using fossil fuels, or avert emissions from waste. If done right, such projects can reduce the volume of greenhouse gases being added to the atmosphere while providing other benefits to local communities and promoting biodiversity. Beyond planting or protecting trees, offsets can also be generated by preventing the release of greenhouse gases other than CO₂, like methane or nitrous oxide. Typically, more expensive offsets involve removing carbon dioxide that’s already in the atmosphere and storing it away. That may involve projects like growing a forest or installing machines that vacuum carbon dioxide

out of the air. Just 4% of off sets actually remove CO2 from the atmosphere. . . .¹

The voluntary carbon offsets targeted by this bill are distinct from carbon offsets involved in the state’s cap-and-trade program. Under the cap-and-trade program, industry polluters are legally required to either reduce their emissions by specified amounts over time, or otherwise surrender compliance instruments to cover those emissions. The two available compliance instruments are allowances (which originate from the state providing a set amount each year) and offsets (which originate from entities outside of cap-and-trade offering to reduce or avoid equivalent volumes of emissions). Offsets purchased to comply with cap-and-trade are “compliance offsets”; their use is to comply with mandatory legal obligations.

Voluntary carbon markets are just that, voluntary. Voluntary carbon offsets allow companies, governments, and other organizations to offset their carbon emissions on a voluntary basis, either to meet their own sustainability goals or to demonstrate their commitment to reducing their carbon footprint.

The Federal Trade Commission has issued guidance on appropriate marketing of these products:

- Given the complexities of carbon offsets, sellers should employ competent and reliable scientific and accounting methods to properly quantify claimed emission reductions and to ensure that they do not sell the same reduction more than one time.
- It is deceptive to misrepresent, directly or by implication, that a carbon offset represents emission reductions that have already occurred or will occur in the immediate future. To avoid deception, marketers should clearly and prominently disclose if the carbon offset represents emission reductions that will not occur for two years or longer.
- It is deceptive to claim, directly or by implication, that a carbon offset represents an emission reduction if the reduction, or the activity that caused the reduction, was required by law.²

Despite this guidance, this market is largely unregulated and there are concerns about the legitimacy of these offsets.

According to the author:

¹ Ashkat Rathi & Ben Elgin, *What Are Carbon Offsets and How Many Really Work?* (June 14, 2022) Bloomberg, <https://www.bloomberg.com/news/articles/2022-06-14/what-are-carbon-offsets-and-how-many-really-work-quicktake?leadSource=uverify%20wall>. All internet citations are current as of March 19, 2024.

² *Green Guides*, FTC, <https://www.ftc.gov/sites/default/files/attachments/press-releases/ftc-issues-revised-green-guides/greenguides.pdf>.

Junk carbon offsets undermine our climate goals, defraud purchasers of offsets, and contribute to the greenwashing of corporate operations. These voluntary offsets are purchased by consumers and businesses to counterbalance their carbon footprints. Unfortunately, some offsets are created by projects that fail to provide quantifiable and additional carbon benefits, which completely undermines their purported purpose. While California has a regulatory framework for compliance offsets as part of our cap-and-trade program, there are no state or federal laws that provide clarity or establish standards for voluntary carbon offsets. SB 1036 will establish baseline standards that participants in voluntary carbon offset markets must meet in order to offer their products for sale in our state. If a California consumer or business purchases a carbon offset, that offset must represent the real carbon benefits claimed by the issuer or seller of the offset.

The concerns highlighted by the author are well-documented and widespread.

The brisk sales of meaningless offsets is leading to widespread claims of climate progress that isn't actually happening. As Bloomberg Green previously reported, environmental groups such as the Nature Conservancy and the National Audubon Society have sold credits for protecting trees that weren't in danger of being harvested, leading to misleading claims of emissions reductions by Walt Disney Co., JPMorgan Chase & Co., and other companies. Meanwhile, North America's largest carbon reforestation project, Green Trees, has sold credits for trees that were already planted through government programs, sometimes more than a decade earlier, resulting in inflated carbon reduction claims by Bank of America Corp. and many others. (The Nature Conservancy, Audubon, and Green Trees all said their projects followed the market's rules, while Disney, JPMorgan, and Bank of America each declined to comment.) "There's a distinct possibility that a great deal of existing carbon offsets are effectively fake," says Robert Mendelsohn, professor of forest policy and economics at Yale.³

As the author points out, these "junk offsets" inflict two major harms. First, buyers of offsets who sincerely believe that purchasing an offset will finance projects that generate carbon benefits are defrauded when they are sold a junk offset that fails to deliver such benefits. Second, corporate buyers of junk offsets may greenwash their activities (intentionally or unintentionally) if they use the offsets in their accounting of

³ Ben Elgin, *This Timber Company Sold Millions of Dollars of Useless Carbon Offsets* (Mar. 17, 2022) Bloomberg, <https://www.bloomberg.com/news/articles/2022-03-17/timber-ceo-wants-to-reform-flawed-carbon-offset-market>.

the corporation's carbon footprint, which may result in claims to customers, employees, and investors that are inaccurate and can constitute a form of unfair competition.

This bill defines all the relevant terms involved in these markets. It then makes it unlawful, within the Business and Professions Code, to engage in unfair, deceptive, or fraudulent practices in the market. For instance, the bill makes it unlawful for a person (1) "to verify an offset project for the purposes of issuing a voluntary carbon offset," (2) "to certify or issue a voluntary carbon offset," (3) "to market, make available or offer for sale, or sell a voluntary carbon offset," or (4) "to maintain on a registry a voluntary carbon offset" if the person "knows or should know that the GHG reductions or GHG removal enhancements of the offset project are unlikely to be quantifiable, real, and additional."

Key characteristics of a legitimate carbon offset are that they are quantifiable, real, and additional. "Quantifiable" means the ability to accurately measure and calculate GHG reductions or GHG removal enhancements relative to a project baseline in a reliable and replicable manner for all GHG emission sources, GHG sinks, or GHG reservoirs included within the offset project boundary, while accounting for uncertainty and activity-shifting leakage and market-shifting leakage. "Real" means that GHG reductions or enhancements result from a demonstrable action or set of actions, are quantified using appropriate, accurate, and conservative methodologies that account for all GHG emissions sources, GHG sinks, and GHG reservoirs within the offset project boundary, and account for uncertainty and the potential for activity-shifting leakage and market-shifting leakage. "Additional" means GHG emission reductions or removals that exceed any GHG reduction or removals otherwise required by law, regulation, or legally binding mandate, and that exceed any GHG reductions or removals that would otherwise occur in a conservative business-as-usual scenario.

The goal of the bill is make regulation of these offsets more efficient and therefore more likely. It clearly defines the key terms and then provides the bases for enforcement action. While many of these targeted practices can already be enforced under existing UCL and FAL law, this makes their prohibition explicit. Public prosecutors are then able to more adequately enforce the corruption in this industry.

3. Previous iteration of the bill

This bill is identical to SB 390 (Limón, 2023). That bill passed out of this Committee on a 10 to 0 vote and did not receive a single no vote in either house. Governor Newsom vetoed the bill, stating the following:

This bill makes certain actions related to voluntary carbon offsets subject to the False Advertising Law, including with respect to offsets that a person knows, or should have known, do not durably reduce greenhouse

gases in an amount equal to the “atmospheric lifetime” of carbon dioxide emissions.

I support the author’s intent to bring greater transparency to the verification, issuance, and sale of voluntary carbon offsets, and to address the problem of so-called “junk offsets.” However, by imposing civil liability for even unintentional mistakes about offset quality, this bill could inadvertently capture well-intentioned sellers and verifiers of voluntary offsets, and risks creating significant turmoil in the market for carbon offsets, potentially even beyond California. I encourage the author to consider an alternative approach to ensuring voluntary carbon offset quality that avoids these unintended consequences.

As a general rule, California law provides that persons are responsible, not only for the result of their willful acts, but also for an injury occasioned to another by their want of ordinary care or skill in the management of their property or person, except so far as the latter has, willfully or by want of ordinary care, brought the injury upon themselves. (Civ. Code § 1714(a).) Liability has the primary effect of ensuring that some measure of recourse exists for those persons injured by the willful or negligent acts of others; the risk of that liability has the primary effect of ensuring parties act reasonably to avoid harm to those to whom they owe a duty.

Here the author is making clear that false representations in advertising these products subject persons to liability under California’s major consumer protection statutes, the UCL and FAL. While such unlawful practices are already subject to these laws, the bill provides more clarity to the industry and regulators with respect to the complex nature of these offsets and the claims associated with them. Given the scope of the problem and the murkiness of the products themselves, it is arguably necessary to hold these companies responsible for representations they should have known were likely false, forcing them to do their due diligence before making claims about their products.

It is an extremely high bar for those injured by false representations about products to only be able to seek a remedy when they can prove the company intentionally misrepresented its claims. The bar for private actions under these statutes is already high and requires proof a person has suffered injury in fact and has lost money or property as a result of a violation. Only then can they bring an action for an injunction or restitution. Otherwise enforcement is entirely left to public prosecutors.

4. Stakeholder positions

California Environmental Voters, previously the California League of Conservation Voters, writes in support of the bill:

California Environmental Voters represents over 135,000 members, with a mission to protect and enhance the environment and the health of all California communities by electing environmental champions, advancing critical priorities, and holding policy makers accountable.

SB 1036 brings legal standards into the markets for VCOs, which will incentivize market actors to conduct appropriate due diligence related to the claimed carbon benefits of VCOs that they issue and sell. Currently, VCOs operate outside of any legal frameworks or constructs that reflect the structure of carbon offset markets and the risks associated with junk offsets.

This bill borrows and adapts definitions related to carbon offsets from CARB's regulations that apply to compliance offsets under California's cap-and-trade program. Leveraging those definitions, this bill establishes unlawful business practices related to VCOs by outlawing the issuance or sale of a VCO by a person who knows or should know that the project underlying the VCO is unlikely to deliver carbon benefits that are quantifiable, real, additional, durable, and that account.

Consumer Watchdog makes the case for the bill:

SB 1036 is urgently needed to clarify the application of California's False Advertising Law (FAL) to the voluntary carbon offsets industry.

The global voluntary carbon offsets industry is currently valued at \$2 billion and is expected to grow significantly over the next decade as more companies invest in voluntary carbon credits to reduce their carbon emissions, according to banking analysis.

Unfortunately, some market participants continue to sell carbon offset credits based on questionable project claims or flawed technical methodologies. Consumers can be offered opportunities to lower their carbon emissions or buy a "climate friendly" product or service based on these claims because there is little regulation of voluntary carbon market credit quality standards.

This bill rectifies that by making it unlawful for a person to "certify or issue a voluntary carbon offset, to maintain on a registry a voluntary carbon offset, or to market, make available or offer for sale, or sell a voluntary carbon offset if the person knows or should know that the greenhouse gas reductions or greenhouse gas removal enhancements of the offset project related to the voluntary carbon offset are unlikely to be quantifiable, real, and additional." The bill does the same for verification of an offset project.

This legislation is valuable because it clarifies how California's existing consumer protection laws apply in the context of industry claims about carbon credits. Today's FAL is strong and applies broadly, but there is limited case law specifically on how it applies to climate-related greenwashing. Making its application straightforward to the carbon credit industry is essential to creating much-needed accountability and ensuring that carbon credits reflect accurate claims.

The bill does not change the substantive legal standard applied to false statements in the offsets industry, nor does it affect compliance offset programs like the one incorporated into California's cap-and-trade program. Rather, it simplifies how a court would review claims about misleading marketing claims involving offsets by clarifying how the existing FAL applies to each step of carbon credit verification, issuance, brokering, and sales.

Writing in opposition, A-Gas, Rubicon Carbon, ClimeCo LLC, and a number of other companies argue:

SB 1036 makes it unlawful for a person to verify, certify or issue a voluntary carbon offset, to maintain on a registry a voluntary carbon offset, or to market, make available or offer for sale, or sell a voluntary carbon offset if the person knows or should know that the greenhouse gas reductions or greenhouse gas removal enhancements of the offset project related to the voluntary carbon offset are unlikely to be quantifiable, real, and additional.

While this may seem viable on the surface, the application of these criteria varies by project type and methodology. CARB, carbon standards/registries, carbon credit rating agencies and even the ICVCM have spent years developing project methodologies and/or assessment tools that evaluate these criteria on a project by project basis. Leaving the assessment of these criteria to civil litigants with limited carbon market expertise significantly increases the risk for market participants - even if they are following the guidance issued by a registry or ICVCM. In addition, the term "unlikely" dramatically increases the uncertainty and broadens the scope of risk for any market participant.

A coalition of groups, including the Western States Petroleum Association, writes in opposition:

The Federal Trade Commission (FTC) has contemplated the marketing and selling of voluntary carbon offsets by including within their Green Guides clear direction that offer guidance on the voluntary carbon offset

market, noting specifically that sellers should “properly quantify emissions reductions” and that sellers and end users cannot represent that an offset will “represent emission reductions that have already or will occur” if the emissions reductions take a certain amount of time to materialize³. The FTC is currently in the process of updating their Green Guides to further clarify best practices for the use of voluntary carbon offsets to support corporate climate-related targets⁴. To that end, it would be prudent to await the outcome of FTC’s rulemaking process and determine, what, if any, gaps exist before moving forward.

SUPPORT

California Environmental Voters
Consumer Watchdog
Defenders of Wildlife
Institute for Agriculture and Trade Policy
NextGen California
Pacific Forest Trust
SanDiego350
The Climate Center

OPPOSITION

3degrees Inc.
A-Gas
ACR
Anew Climate LLC
Arcmor Limited
Bezero Carbon
California Bankers Association
California Chamber of Commerce
California Food Producers
California Forest Carbon Coalition
California Independent Petroleum Association
California Manufacturers & Technology Association
Capricorn Investment Group
Carbon Streaming Corporation
Civil Justice Association of California
Climate Action Reserve
Climeco LLC
Cool Effect INC.
Emergent
Evolution Markets, Inc.
Finite Carbon

Ieta

Imperative Global Services, INC.

Independent Energy Producers Association

Pollination Capital Partners LLC

Resilient LLP

Respira International LTD

Rubicon Carbon

Securities Industry and Financial Markets Association

S&P Global Commodity Insights

Terra Global Capital LLC

The Climate Trust

We Mean Business Coalition

Western States Petroleum Association

Xpansiv Ltd.

RELATED LEGISLATION

Pending Legislation: None known.

Prior Legislation:

SB 390 (Limón, 2023) *See Comment 3.*

AB 1305 (Gabriel, Ch. 365, Stats. 2023) requires a business entity that is marketing or selling voluntary carbon offsets to disclose specified information about the applicable carbon offset project and details regarding accountability if a project is not completed or does not meet the projected emission reductions or removal benefits.

SB 343 (Allen, Ch. 507, Stats. 2022) tightened the requirements around the permissible use of the “chasing arrows” recycling symbol to avoid deceptive uses in marketing and otherwise.

PRIOR VOTES:

Senate Environmental Quality Committee (Ayes 5, Noes 0)
