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

SB 261 (Stern)
Version: April 10, 2023
Hearing Date: April 18, 2023
Fiscal: Yes
Urgency: No
AWM

SUBJECT

Greenhouse gases: climate-related financial risk

DIGEST

This bill requires companies that do business in California and have gross revenues exceeding $500 million annually, excluding insurance companies, to report on their climate-related financial risk, as specified; and requires the California Air Resources Board (CARB) to contract with a qualified climate reporting organization to review and publish an analysis of those reports, as specified.

EXECUTIVE SUMMARY

Climate change is here; the question that remains is how catastrophic it will be. As the effects of climate change are felt around the world, businesses and governments increasingly have to account for climate-related financial risks—the uncertainties and threats caused by climate change that may affect decisionmaking.

The Taskforce on Climate-Related Financial Disclosure (TCFD), founded at the behest of the G20, has developed a recommended framework for corporate climate-risk reporting. The TCFD-recommended disclosures include identifying the actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning, and disclosing how the organization identifies, assesses, and manages climate-related risks. A number of organizations have voluntarily published reports containing some or all of the TCFD-recommended disclosures, and the United Kingdom requires certain organizations to make TCFD disclosures on annual basis, but there is no domestic requirement for companies to make TCFD-recommended disclosures.

This bill requires companies with over $500 million in annual revenues that do business in California, beginning in 2024, to annually submit a report to the CARB disclosing their climate-related financial risks using the TCFD framework; the report must also be posted to the entity's website. The bill further requires that CARB contract with a qualified climate reporting organization to review the reports and annually publish a report analyzing the information provided and a sector-by-sector breakdown of climate-related financial risks. The bill specifies that, if a similar reporting requirement is enacted at the federal level, a reporting entity can satisfy its obligations under this bill by submitting the federal report. Finally, the bill provides that a reporting entity's violation of the reporting requirements is punishable by a civil penalty of up to $500,000, which may be awarded in a civil action brought by the Attorney General.

This bill is sponsored by Ceres and is supported by over 80 organizations, including groups dedicated to minimizing the effects of climate change, businesses, and faith-based organizations. This bill is opposed by over 50 organizations, including the California Chamber of Commerce and local Chambers of Commerce and a range of organization representing various industries. This bill was passed out of the Senate Environmental Quality Committee with a vote of 4-2.

PROPOSED CHANGES TO THE LAW

Existing state law:

1) Establishes the California Global Warming Solutions Act of 2006 (AB 32 (Nunez, Ch. 488, Stats. 2006)), which declares that global warming poses a serious threat to the economic well-being, public health, natural resources, and the environment of California, and that action taken by California to reduce emissions of greenhouse gases will have far-reaching effects by encouraging other states, the federal government, and other countries to act. (Health & Saf. Code, div. 25.5, §§ 38500 et seq.)

2) Requires the CARB to monitor compliance with and enforce the requirements of the California Global Warming Solutions Act of 2006, and deems any violation to result in an emission of an air contaminant that may result in criminal and civil penalties. (Health & Saf. Code, § 38580.)

3) Defines "doing business" in California as engaging in any transaction for the purpose of financial gain within California, being organized or commercially domiciled in California, or having California sales, property, or payroll exceed $610,395, $61,040, and $61,040, respectively, as of 2020. (Rev. & Tax. Code, §§17041, 23101.)

4) Requires, until January 31, 2035, California Public Employees' Retirement System (CalPERS) and California State Teachers' Retirement System (CalSTRS) to publicly report on its analysis of the climate-related financial risk in its public market portfolio, as specified. (Gov. Code, § 7510.5.)

Existing federal law:

1) Gives Congress the authority to regulate commerce with foreign nations and between states, i.e. the commerce clause. (U.S. Const. art. I, § 8.)

2) Directs specified federal officers and bodies, pursuant to an executive order, to develop a comprehensive, government-wide strategy regarding the measurement, assessment, mitigation, and disclosure of climate-related financial risk to federal government programs, assets, and liabilities in order to increase the long-term stability of federal operations. (Exec. Order No. 14030, 86 Fed.Reg. 27967 (May 20, 2021).)

This bill:

1) Makes findings and declarations regarding, among other things, the importance of climate risk in effective decision-making.

2) Defines the following terms:
   a) "Climate reporting organization" is a nonprofit climate reporting organization contracted by the CARB that (1) currently operates a voluntary climate reporting organization for organizations operating in the United States and (2) has experience with voluntary climate-related disclosure by entities operating in California.
   b) "Climate-related financial risk" is 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.
   c) "Climate-related financial risk report" is a report required by 3).
   d) "Covered entity" is a corporation, partnership, limited liability company, or other business entity formed under the laws of this state, the laws of any other state of the United States or the District of Columbia, or under an act of the Congress of the United States with total annual revenues in excess of $500,000,000 and that does business in California; the term does not include business entity that is subject to regulation by the Department of Insurance in this state, or that is in the business of insurance in any other state.

3) Requires a covered entity, on or before December 31, 2024, and annually thereafter, to prepare a climate-related financial risk report disclosing both of the following:
   a) Its climate-related financial risk, in accordance with the recommended framework and disclosures contained in the Final Report of Recommendations of the Task Force on Climate-Related Financial Disclosures

(June 2017) published by the Task Force on Climate-Related Financial Disclosures, or any subsequent publication thereto.
b) Its measures adopted to reduce and adapt to climate-related financial risk disclosed pursuant to 3)(a).

4) Requires a covered entity, on or before December 31, 2024, and annually thereafter, to submit to the CARB, and make available to the public on its own website, a copy of the report required by 3); and to submit to the Secretary of State a statement affirming, not under penalty of perjury, that the report prepared and filed pursuant to 3) discloses climate-related financial risk in accordance with the TCFD framework, as required.

5) Provides that, if a federal law or regulation enacted or promulgated after January 1, 2023, requires a covered entity to prepare an annual report disclosing information materially similar to the information described in 3), a report prepared pursuant to the federal requirement satisfies the requirements of 3) and a covered entity may satisfy its obligations under 4) by submitting the federal report to the CARB.

6) Requires the CARB to contract with a climate reporting organization to prepare an annual public report on the climate risk disclosures required under 3) and ensure the required climate risk disclosures remain consistent with current practices.

7) Requires the climate reporting organization contracted under 6) to do all of the following:
   a) Annually prepare a report that contains: (1) a review of the disclosure of climate-related financial risk contained in the reports submitted to the CARB; (2) an analysis of the systematic and sector-wide climate-related financial risks facing the state based on the contents of the reports, including, but not limited to, potential impacts one economically vulnerable communities; and (3) identification of inadequate or insufficient reports.
   b) Regularly convene representatives of sectors responsible for reporting climate-related financial risks, state agencies responsible for oversight of reporting sectors, investment managers, academic experts, and other stakeholders to offer input on current best practices regarding the disclosure of financial risks resulting from climate change, including, but not limited to, proposals to update the definition of "climate-related financial risk," and the framework or disclosure standard of "climate-related financial risk reports."
   c) Monitor federal regulatory actions among agency members of the federal Financial Stability Oversight Council, as well as nonindependent regulators overseen by the White House.

8) Provides that if the Attorney General finds that a reporting entity has violated the requirements above of 3) or 4), or upon a report received from the CARB, the entity shall be liable for a civil penalty not to exceed $500,000 per violation, which may be

assessed and recovered in a civil action brought in the name of the people of the State of California by the Attorney General in a court of competent jurisdiction.

9) Places 2)-6) within the California Global Warming Solutions Act of 2006.

COMMENTS

1. Author's comment

According to the author:

> It is abundantly clear the worsening effects of climate change pose numerous environmental risks that include extreme drought, rising sea levels, catastrophic wildfires, and extreme weather events. These impacts not only [a]ffect our environment but they also [a]ffect how we live, what services we rely upon and which investments make the most sense. Major corporations and financial institutions face climate related financial risks in their business making decisions, so it is important for these businesses and institutions to assess and share the risks they have identified, and what efforts they are employing to mitigate them. This information is important to provide more transparency to policy makers, investors, and shareholders as it will result in improved decision making on where to invest private and public dollars. Climate related financial risk disclosures are ultimately about good business, partnerships, governance and the solutions and planning necessary to navigate the increasing burdens of a changing climate.

2. Background on climate-related financial disclosures

In 2015, the G20 Finance Ministers and Central Bank Governors asked the Financial Stability Board (FSB) to review how the financial sector could better account for climate-change-related issues.[1] The FSB formed the TCFD, and in 2017 the TCFD released a recommended framework for companies on climate-related financial disclosures.[2] The report explains that "climate change poses significant financial challenges and opportunities," but "[a]t the same time, the risk-return profile of organizations exposed to climate-related risks may change significantly as such organizations may be more affected by physical impacts of climate change, climate policy, and new technologies."[3] As such, the TCFD recommended that companies make climate disclosures in four key areas:

---

[1] Task Force on Climate-Related Financial Disclosures, History, https://www.fsb-tcfd.org/about/#history. All links in this analysis are current as of April 14, 2023.
[2] *See* TCFD, *Recommendations of the Task Force on Climate-related Financial Disclosures* (Jun. 2017), *available at* https://assets.bbhub.io/company/sites/60/2021/10/FINAL-2017-TCFD-Report.pdf.
[3] *Id.* at p. ii.

- Governance: disclose the organization's governance around climate-related risks and opportunities.
- Strategy: disclose the actual and potential impacts of the climate-related risks and opportunities on the organization's businesses, strategy, and financial planning where such information is material.
- Risk management: disclose how the organization identifies, assesses, and manages climate-related risks.
- Metrics and targets: disclose the metrics and targets used to assess and manage climate-related risks and opportunities where such information is material.[4]

The United Kingdom adopted the TCFD as a mandatory disclosure framework for publicly traded companies and large private companies in 2021.[5] As of March 2022, CDP—an organization that provides a platform for TCFD-aligned disclosures—reports that over 680 financial institutions with over $130 trillion in assets had called on nearly 10,400 companies to disclose TCFD climate-related data.[6] Major investment firms, such as BlackRock, have also made TCFD climate-risk reports.

Here in California, the Legislature in 2018 enacted SB 964 (Allen, Ch. 731, Stats. 2018), which requires CalPERS and CalSTRS to make public climate-related financial risk disclosures on a triannual basis.[7] CalSTRS, writing in support of the bill, has noted that the task of determining its own climate-related financial risk would be significantly simplified if companies covered by this bill were also required to make TCFD-aligned disclosures.

3. <u>This bill requires very large companies doing business in California to disclose their climate-related financial risks beginning in 2024</u>

This bill requires companies who do business in California and whose gross revenues exceed $500 million annually, excluding insurance companies, to annually disclose their climate-related financial risks under the TCFD framework, beginning in 2024. The report must be submitted to the CARB and posted on the company's own website. Insurance companies are exempted because the National Association of Insurance Commissioners, which includes California's Insurance Commissioner, already require

---

[4] *Id.* at p. 14.

[5] United Kingdom Department for Business, Energy & Industrial Strategy, MD Treasury, Press Release, UK to enshrine mandatory climate disclosures for largest companies in law (Oct. 29, 2021), https://www.gov.uk/government/news/uk-to-enshrine-mandatory-climate-disclosures-for-largest-companies-in-law.

[6] CDP, *More than 680 financial institutions with US$130+ trillion in assets call on nearly 10,400 companies to disclose environmental data through CDP* (Mar. 14 2022), https://www.cdp.net/en/articles/media/More-than-680-financial-institutions-call-on-nearly-10400-companies-to-disclose-environmental-data-through-CDP.

[7] Gov. Code, § 7510.5. The requirement is set to sunset on January 31, 2035. (Gov. Code, § 7510.5(f).)

insurance companies to report their climate-related risks in alignment with TCFD.[8] The bill provides that a company that violates the bill's reporting requirements may be liable for a civil penalty of up to $500,000, which may be recovered in a civil action brought by the Attorney General in the name of the people of the State of California.

The bill also requires the CARB to contract with an experienced climate reporting organization to analyze the reports. The contracted entity must, on an annual basis, prepare a public report that reviews the climate-related financial risk disclosures and provides breakdowns of risk by sector and identify inadequate or insufficient reports.

An earlier version of the bill did not account for the possibility that the federal government may impose a similar climate-related-risk reporting requirement. As the Senate Environmental Quality Committee's analysis notes, the Securities and Exchange Commission (SEC) is considering its own potential climate disclosure rules which may overlap with this bill's disclosures. While the SEC's rules would apply only to publicly traded companies, imposing a dual reporting requirement could unduly burden companies or result in a conflict with federal requirements. The author has accordingly amended the bill to provide that, if federal laws or regulations are enacted to require climate-risk reporting, a covered entity can comply with this bill by submitting the federally required report to the CARB, rather than creating a second report.

4. This bill does not present a clear dormant interstate commerce clause issue

Section 8 of Article I of the United States Constitution grants the United States Congress the power to regulate interstate commerce.[9] Since the early nineteenth century, the Supreme Court has held that obverse proposition—that states may not usurp Congress's express power to regulate interstate commerce—must also be true.[10] This rule against state interference in interstate commerce, sometimes known as the dormant interstate commerce clause, serves as an absolute bar to regulations that discriminate against interstate commerce, i.e., by favoring in-state businesses or excluding out-of-state businesses.[11] But when a state passes a law that " 'regulat[es] even-handedly [across all in-state and out-of-state businesses] to effectuate a legitimate local public interest,' " that law " 'will be upheld unless the burden imposed upon such commerce is clearly excessive in relation to the putative local benefits.' "[12]

There is no facial dormant Commerce Clause issue here. This bill grants no favoritism for in-state companies—all U.S.-based companies doing business in California with

---

[8] *See* National Association of Insurance Commissioners, U.S. Insurance Commissioners Endorse Internationally Recognized Climate Risk Disclosure Standard for Insurance Companies (Apr. 2, 2022), https://content.naic.org/article/us-insurance-commissioners-endorse-internationally-recognized-climate-risk-disclosure-standard.
[9] U.S. Const., art. I, § 8, cl. 3.
[10] *See Gibbons v. Ogden* (1824) 22 U.S. 1.
[11] *E.g.*, *Dean Milk Co. v. Madison* (1951) 340 U.S. 349, 354.
[12] *South Dakota v. Wayfair, Inc.* (2018) 138 S.Ct. 2080, 2091.

annual revenues in excess of $500 million are subject to the bill's reporting requirement. That leaves only the questions of whether the bill's reporting requirement serves a legitimate local interest, and whether the burden imposed by the reporting requirement is clearly excessive in relation to the benefits conferred.

5. <u>Arguments in support</u>

According to Ceres, the bill's sponsor:

> Climate change poses a significant risk to our long-term economic success, impacts the health and livelihood of the communities in which we operate and live, and disrupts the value chains on which we rely. Consistent, comparable, and reliable information at scale is necessary to fully assess companies' risk exposure and to navigate the path to a net-zero future.
>
> Companies need to invest in climate disclosure analysis and reporting because ignoring the risks will be very costly, while finding the path towards a net-zero future offers economic stability and growth. The current state of voluntary climate disclosure is inadequate for meeting rapidly accelerating climate risks, and the SEC's climate risk disclosure would only apply to publicly traded US entities. Climate disclosure is needed from non-listed actors as well. SB 261 sets the bar on robust, multi-sector disclosure and holds companies accountable for managing climate risk to ensure a sustainable, resilient, and prosperous future for California.

6. <u>Arguments in opposition</u>

According to a coalition of over 50 organizations writing in opposition:

> By mandating an annual report in accordance with the Final Recommendations of the Task Force on Climate-Related Financial Disclosures, SB 261 is itself in conflict with the recommendations. The recommendations are designed to be voluntary and to maintain the standard of materiality, the report notes that "any disclosure recommendations by the Task Force would need to be voluntary, would need to incorporate the principle of materiality and would need to weigh the balance of costs and benefits." The recommendations also assert the need for flexibility. Further the report acknowledges the importance of a deliberate transition, noting that "As understanding, data analytics, and modeling of climate-related issues becomes more widespread, disclosures can mature accordingly." Unfortunately, SB 261 was drafted with a degree of rigidity that doesn't allow for flexibility based on the maturation of our understanding of data collection and analytics as noted in the Task Force's own findings.

> The Task Force's recommendations seem to be designed to offer guidance to those in the business community on how best to mitigate risk, yet the approach taken by SB 261 would actually impose the greatest amount of risk on those most susceptible to financial uncertainty: the small business community. SB 261 takes a one-size fits all approach to the business community and applies a reporting standard that would impact a broad array of businesses here in California. The Task Force's own findings note that there should be a proportional approach to developing disclosure requirements to ensure that smaller organizations are not subject to risk. Risk that the report clearly identifies in the form of "litigation given the high degree of uncertainty around future timing and magnitude of climate-related impacts." While larger institutions might be able to assume that risk, that is often not the case for smaller businesses here in California. And, at an even more granular level, the impact to the small business community will vary based on geographic location, which is not accounted for in this proposal. Unfortunately, SB 261 does not follow the guidance offered in the report and puts the small business community at risk writ large.

SUPPORT

Ceres (sponsor)
350 Bay Area Action
350 Conejo/San Fernando Valley
350 Humboldt
350 Juneau
350 Marin
350 Sacramento
350 South Bay Los Angeles
350 Southland Legislative Alliance
350 Ventura County Climate Hub
Alter Eco
Americans for Financial Reform
Avocado Green
Ban SUP (Single Use Plastic)
California Environmental Voters
California State Teachers' Retirement System (CalSTRS)
CALPIRG
Catholic Network US (Colorado)
Center for Biological Diversity
Citizens' Climate Lobby, Sacramento/Roseville Chapter
Climate 911
Climate Action California
Climate Action Campaign, Humboldt
Climate Hawks Vote

Climate Reality Project, Los Angeles
Climate Reality Project, San Fernando Valley
Coalition for Clean Air
Coastside Jewish Community
Colorado Businesses for a Livable Climate
Community for Sustainable Energy
Conejo Climate Coalition
Cool Planet Group of First Presbyterian Church, Palo Alto
Divest Oregon
DSM North America
E2
East Valley Indivisibles
Environment California
Environmental Defense Fund
Extinction Rebellion San Francisco Bay Area
Fossil Free California
Friends Committee on legislation of California
Friends of the Earth
Giniw Collective
Glendale Environmental Coalition
Greater New Orleans Housing Alliance
Grove Collaborative
Honor the Earth
Indivisible Alta Pasadena
Indivisible Ambassadors (Colorado)
Indivisible California Green Team
Indivisible California: StateStrong
Leading Change Consulting and Coaching
Littleton Business Alliance
Mental Health & Inclusion Ministries
Mind Eye World
Mothers Out Front California
Natural Resources Defense Council
North Range Concerned Citizens
Oil & Gas Action Network
Peninsula Interfaith Climate Action
Public Citizen
RapidShift Network
San Fernando Valley Climate Reality
San Francisco Bay Physicians for Social Responsibility
Santa Cruz Climate Action Network
Save EPA
Sierra Club California

Sierra Nevada Brewing Co.
Silicon Valley Youth Climate Action
SoCal 350 Climate Action
SolidarityINFOService
Southwest Organization for Sustainability
Spirit of the Sun, Inc.
Stand.earth
System Change Not Climate Change
The Climate Center
The Phoenix Group
The Vessel Project of Louisiana
Third Act
Transformative Wealth Management, LLC
Trinity Respecting Earth and Environment
Union of Concerned Scientists
Urban Ecology Project

OPPOSITION

Advanced Medical Technology Association
African American Farmers of California
Agricultural Energy Consumers Association
American Beverage Association
American Composites Manufacturers Association
American Pistachio Growers
Antelope Valley Chambers of Commerce
Auto Care Association
Building Owners and Managers Association
California Advanced Biofuels Alliance
California Apartment Association
California Apple Commission
California Asphalt Pavement Association
California Blueberry Association
California Blueberry Commission
California Building Industry Association
California Business Properties Association
California Chamber of Commerce
California Construction and Industrial Materials Association
California Cotton Ginners and Growers Association
California Credit Union League
California Date Commission
California Fresh Fruit Association
California Fuels and Convenience Alliance
California Hispanic Chamber of Commerce

California Independent Petroleum Association
California Life Sciences
California Manufacturers & Technology Association
California Poultry Federation
California Retailers Association
California Walnut Commission
Can Manufacturers Institute
Carlsbad Chamber of Commerce
CAWA
Chino Valley Chamber of Commerce
Citrus Heights Chamber
Costa Mesa Chamber of Commerce
Danville Area Chambers of Commerce
Far West Equipment Dealers Association
La Cañada Flintridge Chamber of Commerce
Long Beach Area Chamber of Commerce
Los Angeles Area Chamber of Commerce
National Association of Industrial and Office Properties
Nisei Farmers League
North San Diego Chamber of Commerce
Oceanside Chamber of Commerce
Olive Growers Council of California
Orange County Business Council
Palos Verdes Peninsula Chamber of Commerce
Rancho Cordova Chamber of Commerce
Santa Barbara South Coast Chamber of Commerce
Securities Industry and Financial Markets Association
Southern California Leadership Council
Specialty Equipment Market Association
The Greater High Desert Chamber of Commerce
Torrance Area Chamber of Commerce
Walnut Creek Chamber of Commerce
West Precast Prestressed Concrete Institute
West Ventura County Business Alliance
Western Agricultural Processors Association
Western Growers Association
Western Plant Health Association
Western States Petroleum Association
Wine Institute

RELATED LEGISLATION

Pending Legislation:

SB 253 (Wiener, 2023) requires any partnership, corporation, limited liability company, or other U.S. business entity with total annual revenues in excess of one billion dollars and that does business in California to publicly report their annual greenhouse gas (GHG) emissions, as specified by the CARB. SB 253 is pending before this Committee and is scheduled to be heard on the same date as this bill.

SB 252 (Gonzalez, 2023) prohibits the boards of the Public Employees' Retirement System and the State Teachers' Retirement System from making new investments or renewing existing investments of public employee retirement funds in a fossil fuel company, as defined, and would require the boards to liquidate investments in a fossil fuel company on or before July 1, 2030. SB 252 is pending before the Senate Judiciary Committee.

Prior Legislation:

SB 449 (Stern, 2021) was substantially similar to this bill, in that it would have required certain California-based financial institutions to prepare and disclose climate-related financial risk reports disclosing the institution's climate-related financial risk and its measures to reduce and adapt to those risks and established an entity to review the institutions' reports and prepare analysis of the systemic and sector-wide climate-related financial risk. SB 449 died in the Senate Appropriations Committee.

SB 260 (Wiener, 2021) would have required the CARB to develop regulations to require a reporting entity—defined as a business entity with total annual revenues over one billion dollars that does business in California—to report to an emissions registry, as defined, their Scope 1, Scope 2, and Scope 3 emissions, as defined. The bill also would have required the ARB to prepare a report by January 1, 2026, on those disclosures, and it requires the emissions registry to establish a public data platform to view the disclosures. SB 260 died on the Assembly Floor.

SB 964 (Allen, Ch. 731, Stats. 2018) requires CalPERS and CalSTRS to make public climate-related financial risk disclosures on a triannual basis until January 1, 2035.

PRIOR VOTES:

Senate Environmental Quality Committee (Ayes 4, Noes 2)

****