Climate Disclosure Laws with Increasingly Long Arms*

***How the new Emissions Disclosure requirements in California and the EU will apply to companies worldwide.**

ISABEL VERKES

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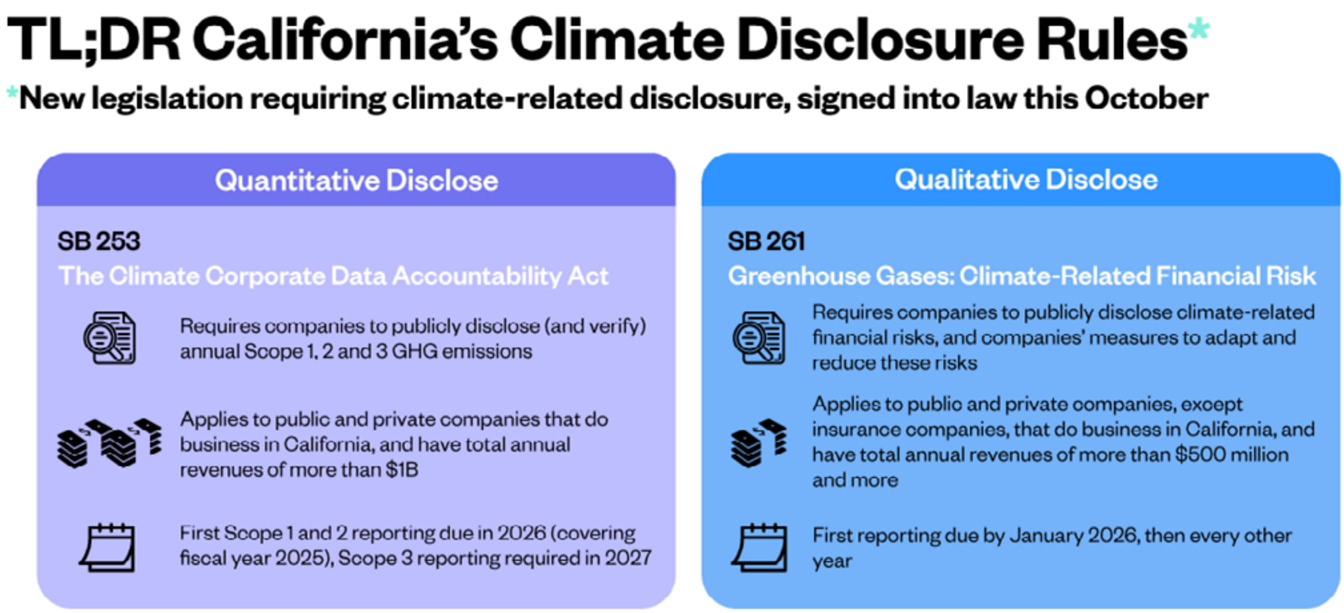
As the 5th largest economy in the world, and an upcoming 4th by some estimates, California matters. The state accounts for about 15% of U.S. national GDP, is home to a large tech and services sector, dominates the US entertainment market, and ranks first in cash receipts from agriculture in the U.S.

Recent climate-related pushes reinstate California's economic importance, with national consequences and even ramifications beyond the U.S. In September, California sued several large US oil companies, alleging oil and gas executives pushed out misinformation about the negative impacts of relying on fossil fuels. Whatever may come from that, another landmark climate development followed on October 7, when California's governor signed into law Senate Bill 253 ("SB-253") and Senate Bill 261 ("SB-261"), the core of California's "Climate Accountability Package."

The broader reach of California's new climate legislation plays out in three ways:

1. By unequivocally requiring Scope 3 emissions disclosure, California's rules have the potential to reach every part of a company's value chain.
2. California's legislation sets the U.S. standard for climate-related disclosures, being the first mandatory climate disclosure rule in the U.S.
3. Many US companies headquartered outside California will fall under its scope, that is U.S. as well as foreign companies.



As the national market regulator, the U.S. SEC has proposed rules requiring companies to disclose climate data last year. However, the SEC hasn't finalized those rules amidst pushbacks: including cost concerns for data collection and compliance, disagreement about whether Scope 3 should be included in the disclosure requirements, and an "anti-ESG" sentiment in the US. The SEC has been wary of facing legal challenges to its climate disclosure rule. Now that California's new rules preceded the SEC's rule, this state legislation will set the stage nationally.

First, California's climate rule affects more companies than the ones directly covered under California's rules. By requiring Scope 3 disclosure, companies disclosing under California's rule will build capabilities for emission data across their value chain, notably suppliers that might not otherwise look at their emission footprint.

Furthermore, California's disclosure requirements reach beyond state borders. California's climate regulation will apply to over 10,000 companies, of which 5,000 will have to provide both the quantitative disclosure of GHG emissions (SB-253) and qualitative disclosure of climate risk (SB-261). Approximately 80% of those 5,000 are privately held and not otherwise subject to the proposed climate regulation by the SEC. Where California's governor is "concerned about the overall financial impact of this bill on businesses," California plans to monitor the cost impact as it implements this new bill. If anything, this supports the SEC's efforts to require companies to disclose their climate-related information, also by addressing the compliance cost concern once companies are used to California's rules. In the words of SEC Chair Gensler: "If those companies were reporting to California, then it would be in essence less costly because they'd already be producing that information." Even if national climate disclosure rules take longer, New York lawmakers are following California's footsteps and proposing similar legislation this year after failing last year.

The far-reaching scope of California's climate disclosure regulation is not unique. As regulators seek to require climate disclosure from the largest companies in their local economies, inevitably this may include multinationals. This is only natural in a globalized economy.

The European Union's Corporate Sustainability Reporting Directive (CSRD) is the EU's approach to setting common European disclosure rules for non-financial data. We see the significant extra-territoriality of the requirements play out in practice. The arms of the CSRD reach further than only European companies. It applies to non-European companies with securities listed on EU markets (irrespective of where the company is established), or non-European companies with an EU-based net revenue of at least €150 million, or a branch with €40 million, and at least a subsidiary or branch in the EU. That is many conglomerates. Goldman Sachs estimates that about 47% of the MSCI ACWI (72% of market cap), and 67% of companies in the S&P 500 (representing ~83% of market cap) will fall under the scope of the CSRD.[1]

The CSRD is indeed on the minds of many corporate sustainability officers outside the EU whose companies operate in Europe.

A U.S. semiconductor company like Qualcomm will prepare its CSRD reporting, even though less than 8% of its revenues come from the EU, it checks the €150 million EU revenue requirement. And as Qualcomm is California-based, it will recycle some of the information it prepared for the CSRD to comply with the new California climate disclosure rule.

Emissions Disclosure Regulation Compared

	California's SB 253	U.S. SEC (Draft)	EU CSRD
Who?	Public Companies; Private Companies	Public Companies; Private not included	Public Companies; Private Companies
Scope 1 and 2	✓	✓	Based on materiality assessment, covering both impact and financial materiality
Scope 3	✓	Only if material, or if part of reduction target. But this is controversial and might be watered down.	Based on materiality assessment, covering both impact and financial materiality
When first reported?	2026 2026 for FY 2025	• • • TBD	2025 Earliest 2025

1. GS Sustain Equity Research (June 23, 2023), Measuring the global scope of CSRD and CSDD

The long arms of local climate disclosure rules, reaching beyond regulatory territories where companies are located, may not be as problematic in practice. The data to be disclosed under these specific climate disclosure rules is quite similar across jurisdictions (i.e. company CO2e emissions). Global standards underpin local regulation and increasingly standardize what is asked of companies worldwide. For example, the GHG Protocol underpins most national and local disclosure requirements on emissions. The TCFD further frames what is understood as climate risk disclosure, and so do the new International Sustainability Standards Board's (ISSB) standards.

For companies, the disclosure burden may be significant for those who are new to non-financial disclosure. It's a capability that will need to be developed. This is where ESG Book can help. For investors, the extra-territorial reach of these rules is a huge benefit; it allows for more consistent data sets covering thousands of companies worldwide. Companies will need to develop disclosure practices as the disclosure requirements will be phased in over the coming years. All of this takes time. Yet, California's latest rules pulled in thousands of companies across the US to disclose their climate-related information. Whatever happens on a national policy level with the SEC, the die has been cast.

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or call us on +44 20 7113 3503

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