Rushed Climate-Reporting Laws Backfiring on California

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A new lawsuit by the U.S. Chamber of Commerce against the California Air Resources Board illustrates the carelessness of the Golden State's legislative process. Pioneering legislation that promised to compel companies to report their greenhouse-gas emissions may ultimately accomplish nothing at all due to defects in its drafting.

Requiring companies to provide climate-related disclosures is a controversial topic, and my Cato Institute colleagues Thomas Berry and Jennifer Schulp have made a strong case against it.But assuming one thinks such mandated reporting is an appropriate policy, California is putting on a master class in how not to implement it.

The implementation problems affect two bills shepherded by state senator Scott Wiener (D., San Francisco) which require large enterprises to report their climate impacts. The legislation parallels an effort by the Securities and Exchange Commission (SEC) to require such reporting. Two years after publishing a proposed rule, the SEC is still fine-tuning its thoughts after digesting over 16,000 comment letters.

By contrast, S.B. 253 and S.B. 261 were pushed through the California state legislature within a few months and then signed by Governor Gavin Newsom who, in his signing statement, said that S.B. 253 "demonstrates California's continued leadership with bold responses to the climate crisis, turning information transparency into climate action." But he recognized there were problems, adding:

The implementation deadlines in this bill are likely infeasible, and the reporting protocol specified could result in inconsistent reporting across businesses subject to the measure. I am directing my Administration to work with the bill's author and the Legislature next year to address these issues. Additionally, I am concerned about the overall financial impact of this bill on businesses, so I am instructing CARB to closely monitor the cost impact as it implements this new bill and to make recommendations to streamline the program.

The Chamber of Commerce and its co-plaintiffs cited Newsom's reservations in their lawsuit, the objective of which is to strike down the new laws. Rather than sign the bills and give the plaintiffs ammunition, Newsom could have spared the state needless litigation and the prospect of an embarrassing loss in federal court by vetoing the legislation and asking Wiener to come back with a more polished legislative product in the next session.

Further, the problems with the climate-reporting bills go well beyond the issues Newsom raised in his signing statement. First, the bill did not provide funding for the California Air Resources Board (CARB) to develop appropriate regulations. The bills authorize CARB to charge companies a filing fee when they submit their climate reports, but it did not provide the startup funding CARB would need to hire industry experts to help it craft effective regulations that take into account the interests of all stakeholders, by, for example, balancing the desire to maximize the amount of information reported while limiting compliance costs for affected companies.

Another issue is that the legislation is overly broad. Rather than limit the reporting requirement to firms incorporated in California, it applies to any company whose revenue exceeds $500 million, operates under any U.S. jurisdiction, and "does business in California." That last rather nebulous criterion is not defined in the legislation, but perhaps CARB would use the state's Franchise Tax Board's definition of "doing business" in the state. That includes engaging "in any transaction for the purpose of financial gain within California," having sales in California in excess of $711,538, possessing property in the state valued at $71,154 or more, or having in-state payroll compensation totaling at least $71,154.

Since the law can be applied to companies that have only a minimal nexus to California, it is especially vulnerable to the First Amendment claim made by the plaintiff; i.e. that the state is compelling speech. This claim may have been more difficult to assert had climate reporting been added to the Statement of Information that California-incorporated companies must periodically file with the secretary of state, thereby expanding an existing regulatory mechanism as opposed to creating a new one.

In contrast to the SEC's planned climate-reporting mandate, the California laws are not limited to publicly traded companies, instead explicitly extending to private corporations and partnerships, and potentially to sole proprietorships and not-for-profits depending on how the law is interpreted. So, unlike the SEC's regulations, S.B. 253 and S.B. 261 cannot be justified as investor-transparency measures (although it should be noted that Wiener did not argue for these bills on that basis).

Finally, S.B. 253, which applies to organizations with more than $1 billion in annual revenue, requires a greenhouse-gas-emissions reporting scope that will be difficult or impossible for affected companies to achieve. Companies above the $1 billion threshold must report the following three categories of emissions:

"Scope 1 emissions" means all direct greenhouse gas emissions that stem from sources that a reporting entity owns or directly controls, regardless of location, including, but not limited to, fuel combustion activities.

“Scope 2 emissions” means indirect greenhouse gas emissions from consumed electricity, steam, heating, or cooling purchased or acquired by a reporting entity, regardless of location.

“Scope 3 emissions” means indirect upstream and downstream greenhouse gas emissions, other than scope 2 emissions, from sources that the reporting entity does not own or directly control and may include, but are not limited to, purchased goods and services, business travel, employee commutes, and processing and use of sold products.

The last of these scopes is especially problematic because it requires the reporting company to gather information from its entire supply chain. As plaintiffs have argued, a food wholesaler would have to gather emissions data from all the family farms from which it buys its agricultural products, irrespective of whether these farms are based in California. If small farmers are unable to provide reliable emissions data, wholesalers would have to stop doing business with them, potentially forcing more industry consolidation.

Of course, this isn’t the first time sloppy errors have made their way into California legislation. The California legislature often receives praise for being a lawmaking machine. In contrast to Congress, which produces relatively little legislation amidst cross-partisan and intra-partisan warfare, California’s one-party state government has few barriers to churning out bills. In 2023, a total of 890 California bills became law.

But this is not an unalloyed good. In fact, the state legislature often passes poorly conceived bills that have serious unintended consequences. For example, A.B. 5, a union-backed measure to force freelancers into full-time employment, had to be substantially dialed back after it jeopardized the news, music, and ridesharing industries.

Possibly the most egregious case of legislative sloppiness came in 2017 with the state senate’s passage of a single-payer health-care bill. No econometric analysis was attempted; instead, legislative staff provided a back-of-the-envelope cost estimate of $400 billion per year, which was well above total state spending at the time. One might expect that such a measure would receive a thorough scoring from a disinterested professional body, like the state’s Legislative Analyst’s Office. Fortunately, the legislation died in the state assembly.

And now we have the case of Wiener’s climate-reporting legislation. Although it may not have been anything to brag about, California could have pioneered corporate climate reporting. Instead, the state has two half-baked laws that risk being struck down in court and will have to be rewritten in the state house before being handed back to CARB for implementation.

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