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The Future of Climate Policy and Corporate Accountability

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California's S.B. 253 and 261 as well as the SEC's [Final Rule for the Enhancement and Standardization of Climate-Related Disclosures for Investors](#) (Final Rule) face significant legal challenges from business and environmental groups. This article explores the specifics of these laws, the lawsuit arguments, and the potential ramifications of these legal disputes.

SEC Climate Rule

On March 6, 2024, the U.S. Securities and Exchange Commission (SEC) implemented its Final Rule, which aims to augment transparency in how publicly traded companies disclose climate-related risks and emissions, offering consistent, reliable information for investors, regulators, and the public.

Legal Challenges

In March 2024, business and environmental groups filed several [federal lawsuits](#) challenging the SEC's Final Rule. The business plaintiffs argue the Final Rule imposes excessive burdens, making legal arguments similar to those challenging the California law. The environmental plaintiffs challenge the Final Rule on grounds that its disclosure obligations do not protect investors. In response to multiple lawsuits being filed in various federal districts, the Judicial Panel on Multidistrict Litigation consolidated all the business and environmental plaintiff cases before the Eighth Circuit.

On April 4, 2024, the SEC issued an [order](#) staying the Final Rule pending litigation completion. The SEC's stay aims to expedite judicial resolution by streamlining litigation, without undermining its belief in the Final Rule's legality.

Continue reading the article below or watch this short video for key points and takeaways.

California Climate Statutes

California's laws, predating the SEC's Final Rule, are among the strictest in the U.S. On Oct. 7, 2023, Governor Newsom enacted two climate disclosure laws, S.B. 253 and 261. These statutes mandate certain businesses to report their greenhouse gas emissions and other climate-related risks to enhance transparency and promote environmental responsibility. Senator Scott Wiener emphasized on Sept. 17, 2023, that these laws hold businesses accountable for ineffectively addressing the climate crisis, as stated by the California Legislature.

By 2026, the [Climate Corporate Data Accountability Act](#) (S.B. 253) will require companies in California with annual revenues exceeding \$1 billion to report both direct and indirect greenhouse gas emissions. This encompasses emissions from owned sources, purchased electricity, and all other indirect emissions across a company's value chain. The California Air Resources Board (CARB) may impose penalties up to \$500,000 per reporting year for non-compliance.

The [Greenhouse Gases: Climate-Related Financial Risk Act](#) (S.B. 261) mandates biennial reporting on the financial risks of climate change for companies with revenues exceeding \$500 million starting in January 2026. These reports must adhere to guidelines from the

Task Force on Climate-Related Financial Disclosures (TCFD). CARB may levy penalties up to \$50,000 per reporting year for non-compliance.

Legal Challenges

Plaintiffs have filed a federal lawsuit challenging S.B. 253 and 261 on First Amendment, federal preemption, and dormant Commerce Clause grounds.

On First Amendment grounds, plaintiffs argue that S.B. 253 and 261 compel companies to engage in costly and controversial climate change discourse. The California Attorney General's retort is that these laws call for emission-based disclosures amounting to commercial speech which receives less protection under the First Amendment.

On federal preemption grounds, plaintiffs allege that California's laws surpass federal regulations, such as the [Clean Air Act](#), invoking the Supremacy Clause of the U.S. Constitution which holds that federal law is the "Supreme Law of the land." In response, the California Attorney General counters that S.B. 253 and 261 do not raise federal preemption arguments, as these laws require informational disclosures and do not dictate emission levels, so there is no federal law that would be preempted by mere disclosures.

Regarding the dormant Commerce Clause, plaintiffs allege that S.B. 253 and 261 interfere with interstate commerce by imposing unique greenhouse gas disclosure and reporting obligations that an out-of-state business must comply with, resulting in conflicting regulations across states. The California Attorney General maintains these laws apply to all businesses within the state and address significant local concerns like environmental protection.

Climate Disclosures: State or Federal Issue?

The CA and SEC legal disputes highlight a narrative that seeks a balance between economic needs and the urgent requirements of climate mitigation. The outcomes of ongoing legal challenges to California's laws and the SEC's Final Rule will impact corporate

climate accountability and change regulatory frameworks and corporate decision-making in a dynamic policy landscape.

The jurisdiction question—whether state or federal—over corporate climate disclosures is crucial. If the legal challenge to California’s S.B. 253 and 261 fails, it may encourage other states to adopt similar climate-disclosure regulations, creating a more uniform climate reporting framework across the United States. Conversely, if they fail, it may dissuade other states from regulating corporate climate disclosures, potentially leaving the creation of national standards to the federal government, in line with the SEC’s Final Rule, if it survives ongoing legal challenges or as amended.

Regarding the legal challenge to California’s S.B. 253 and 261, that lawsuit does not forestall the initial compliance disclosure requirements. Under S.B. 253, covered organizations would need to report their 2025 [Scope 1 and 2 greenhouse gas emission](#) (GHG) beginning in 2026. S.B. 261 requires covered entities to submit their annual climate-related financial risk reports that disclose their climate effects and mitigation measures by Jan. 1, 2026.

The SEC’s stay of its Final Rule may not impact companies that would also be subject to California’s S.B. 253 and 261, or the climate reporting obligations imposed under the European Union’s (EU) [Corporate Sustainability Reporting Directive](#) (CSRD). While the prospect of protracted litigation may concern some companies that have not established climate reporting protocols, businesses operating in the EU have been required to comply with CSRD reporting obligations.

Preparing for Disclosures

The ultimate value of climate disclosure is its profound ability to provide regulators, investors, and the public with crucial information on how corporations handle environmental challenges.

Enforcement

Climate-related disclosures aim to enhance corporate accountability, preventing corporations from claiming ignorance about their environmental impacts and facilitating enforcement.

Climate-related disclosures, mandated by S.B. 261 and guided by standards and frameworks like the [Taskforce on Climate-Related Financial Disclosures](#) (TCFD), also provide regulators with critical data to monitor and enforce environmental standards. For more information on voluntary ESG standards and Frameworks, see [Practical Guidance: ESG Stakeholders, Frameworks & Regulation](#).

If companies report their climate risks inaccurately or insufficiently, they may face legal and financial repercussions. It's important, therefore, for companies that are subject to the SEC's, California's S.B. 253 and 261 and the EU's climate reporting requirements to impose climate disclosure protocols that include legal and audit oversight. Entities subject to compliance under the SEC's Final Rule must concern themselves with Scope 1 and 2 reporting obligations. Businesses subject to California's and the EU's laws may have to meet Scope 1, 2 and 3 reporting requirements. It's a complex reporting scheme that warrants rigorous legal and auditing oversight to avoid violating state, federal, and international reporting requirements.

Governance

Climate-related disclosures require changes to corporate governance structures because they necessitate a deeper integration of environmental risk management into strategic decision-making. This shift demands that boards have specific expertise and processes to oversee the assessment and mitigation of climate risks effectively, ensuring that sustainability goals align with business operations and compliance with state, federal, and international climate reporting requirements.

Effective board oversight is crucial to ensure that climate-related goals and targets are not only set but also actively pursued. Disclosures that transparently outline a company's approach to managing climate risks and progress towards environmental targets provide a basis for board actions. They enable directors to hold management accountable for meeting specific benchmarks, adjusting strategies in response to environmental changes, and integrating sustainability into the organizational culture and operations.

Shareholder Engagement

Disclosures on climate-related issues may prompt additional shareholder engagement. A company can respond to greater shareholder engagement by increasing the level of detail and frequency of climate-related disclosures to meet shareholder demands for transparency. This can involve reporting not only on direct impacts and risks but also on the company's strategies and progress towards mitigating environmental harm.

A company can also assuage and, better still, avoid shareholder climate-related disclosure concerns, by facilitating regular discussions and meetings with shareholders to discuss climate issues, strategies, and disclosures—incorporating board and management teams with environmental expertise to ensure knowledgeable decision-making and credible communication with shareholders regarding climate issues.

To learn what these legal disputes might mean for your business, please contact the author or any member of the [Environmental Practice Group](#) at Frost Brown Todd.

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