Whitepaper

California Climate package SB 261

CEMAsys

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Context & Rationale

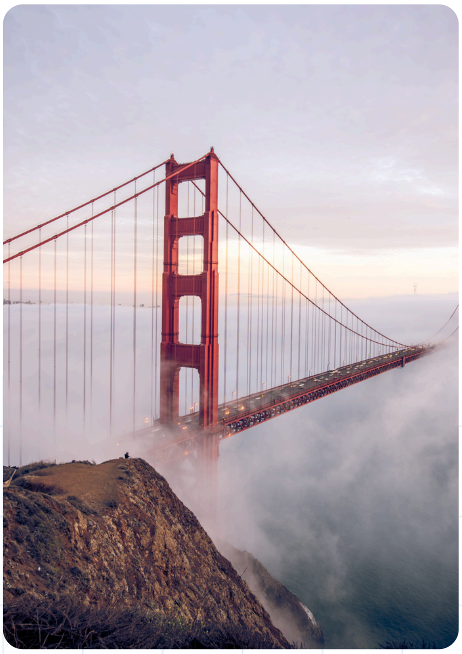
In 2023, California enacted two landmark laws: SB 253 and SB 261. Together, they form what's called the California Climate Accountability Package. These laws make California the first U.S. state to mandate both greenhouse gas emissions disclosure and climate-related financial risk reporting from large companies.
The state's motivation is clear: while many organizations have voluntarily published climate or sustainability information in recent years, the quality, consistency, and comparability of those disclosures have varied significantly. Policymakers identified a growing need for standardized, decision-useful information that investors, regulators, and the public could rely on to assess corporate exposure to climate risks and opportunities.

→ **SB 253** addresses the quantitative side of climate accountability, requiring companies to measure and disclose their greenhouse gas emissions, effectively answering the question: "How much carbon do you emit?"
→ **SB 261**, on the other hand, turns to the qualitative and financial dimensions of the issue, asking: "How does climate change affect your company's financial performance, resilience, and long-term strategy?"

While both laws work in tandem, this whitepaper focuses on SB 261, providing the context, requirements, and practical guidance you'll need to stay informed and prepare your organization to meet California's new climate disclosure expectations.

Why California?

California has long been a pioneer in climate regulation. The state is home to some of the world's largest businesses, capital markets, and investor bases. It faces firsthand the physical risks of climate change, from wildfires that we've seen all over the news, droughts impacting the American west, to coastal flooding and erosion. The legislature recognized that climate impacts are not confined by geography: the financial risks borne by companies operating in California often ripple across supply chains and markets nationwide.
By enacting SB 261, California aims to fill the gap between emissions accounting and financial disclosure, creating a more complete picture of corporate climate risk exposure. The law also signals to federal and international regulators that state-level leadership can set de facto national standards, even before similar SEC rules are finalized.



What is SB 261

Regulation Scope

SB 261 applies to any U.S. business entity, including corporations, partnerships, limited liability companies, and other forms of organization, that meets both of the following criteria:

1. Total annual revenues exceed US $500 million, and
2. The entity is "doing business in California."

The term "doing business in California" was originally tied to the California Revenue and Taxation Code § 23101, which determines whether an entity has sufficient economic presence, or "nexus," in the state.

Under this standard, an entity is considered to be doing business in California if it is:

1. Is commercially domiciled or organized in California, or
2. Exceeds certain thresholds in sales, property, or payroll within the state (adjusted annually for inflation).

CARB also introduced a refined approach intended to make the process more transparent and consistent across both laws. Specifically, CARB indicated that it plans to align the "doing business" definition with data maintained by the California Secretary of State's Business Entity Database, meaning that any entity registered or authorized to do business in California would likely meet the "doing business" test for the purposes of climate disclosure.

CARB has acknowledged that the final applicability guidance, particularly around multi-entity corporate structures and consolidated reporting, will be further clarified during 2025 rulemaking. In the interim, companies should use the Revenue and Taxation Code criteria as the primary reference point for determining whether they fall within scope.

Importantly, SB 261's reach extends well beyond California-headquartered companies. Any U.S.-based entity that meets the revenue and in-state activity thresholds may be subject to the law. For example, a Delaware-incorporated manufacturer with national operations and substantial sales in California would likely qualify, even if it has no physical facilities in the state.

Timing and Frequency

The first reporting deadline under SB 261 is January 1, 2026, covering the most recent fiscal year, and subsequent disclosures will be required every two years for the most recent fiscal year thereafter.

Subsidiaries

Under the statute as written, each individual U.S. entity, whether a parent or a subsidiary, is subject to SB 261 if it independently meets the two applicability criteria: **annual revenues above US $500 million** and a **business presence in California**, as defined by the state's Revenue and Taxation Code § 23101. In other words, a subsidiary that meets these thresholds on its own is considered a covered entity and therefore has a standalone reporting obligation.
However, CARB's implementation guidance and the 2024 amendment (SB 219) recognize the impracticality of multiple filings within a single corporate group. The amendment allows companies to submit one combined, parent-level report that covers all their subsidiaries. This means that if the parent company's report clearly lists the subsidiaries included and explains how their risks and operations were considered, those subsidiaries do not have to file separate reports.

However, if a company's main report doesn't clearly show that a particular subsidiary is covered, or if that subsidiary meets the SB 261 criteria on its own and isn't mentioned, then that subsidiary would still need to submit its own individual report.

In simple terms, companies can choose to report once for the entire organization instead of filing multiple reports for each branch or business unit, but they must make it obvious which parts of the company are included. Most large organizations are expected to take this combined reporting approach, since it's easier to manage, keeps the information consistent, and better reflects how climate risks are managed across the whole company.

What Must Be Reported

SB 261 explicitly directs companies to align their climate-related financial risk disclosures with the Task Force on Climate-related Financial Disclosures (TCFD) or an equivalent framework such as IFRS S2. This ensures that the resulting reports are comparable, decision-useful, and grounded in international best practice.

Importantly, SB 261 only requires companies to disclose climate-related risks that are material to their business. That is, the only risks that need to be disclosed are risks that could reasonably affect the organization's financial condition, operating performance, or long-term value. Companies are not expected to report on every possible environmental issue, but rather to focus on those physical or transition risks that are most relevant to their strategy and financial outlook. The law follows the same materiality principle used in financial reporting and the TCFD framework: the emphasis is on significance, not volume.

A well-structured SB 261 report should be organized around the four pillars of the TCFD framework: Governance, Strategy, Risk Management, and Metrics & Targets.
Each pillar addresses a distinct but interconnected aspect of how an organization understands and manages climate-related financial risk.

Governance

The governance section explains who is responsible for overseeing climate-related risks and opportunities and how those responsibilities are exercised.
CARB expects this section to demonstrate that climate risk oversight is integrated into the company's existing governance architecture rather than treated as a separate sustainability initiative.

Companies should describe:
- The board's role in reviewing and guiding climate-related matters, such as approving strategy, risk appetite, and major capital decisions.
- How management committees or executives identify, assess, and manage climate-related risks.
- The frequency and format of reporting between management and the board.
- How oversight of climate risk interacts with other risk governance mechanisms, such as enterprise risk management (ERM), audit, or finance committees.

Clear governance disclosure shows investors and regulators that climate risk is a strategic and fiduciary issue, not merely an environmental one. When a company can demonstrate that its board of directors and senior management are actively overseeing climate-related risks, it signals that those issues are treated with the same seriousness as other strategic or fiduciary matters such as capital allocation, financial reporting, or enterprise risk management.

Strategy

The strategy section is the heart of the SB 261 report. It explains how climate change may influence the company's business model, value chain, and financial performance over the short, medium, and long term. Companies should identify and discuss both physical risks (such as droughts, floods, wildfires, or extreme temperatures) and transition risks (including changes in policy, regulation, technology, or market demand).

They should also address potential opportunities, such as new markets, products, or efficiency improvements. While scenario analysis is not required in the first reporting cycle, CARB encourages qualitative discussion of different climate futures and how those might affect the company's resilience. For example, a company might compare how its operations would perform under a "low-emissions transition" scenario versus a "high-emissions" scenario.

This section should link climate considerations directly to strategic and financial planning, for instance, by discussing capital expenditures, supply-chain dependencies, insurance coverage, or location-based vulnerabilities. Investors and regulators will look for evidence that climate issues are embedded in the company's decision-making processes, not presented as an afterthought.

Risk Management

Under the TCFD framework, the risk-management section describes how the company identifies, assesses, and manages climate-related risks and how those processes are integrated into its overall risk-management system. Companies should outline:

- The methodologies or tools used to identify and prioritize risks, such as online risk assessment tools, financial prioritization, or internal control assessments.
- The criteria for materiality, or how the company decides whether a risk is financially significant enough to disclose.
- The processes for mitigation and adaptation, including how responsibilities are assigned and monitored.
- How climate-related risk information feeds into broader corporate risk assessments and financial reporting cycles.

CARB's intent is that climate risk management becomes part of standard business practice, on par with operational, financial, and legal risk oversight. This means that processes such as budgeting, capital investment, supply chain planning, and governance reporting should incorporate climate-related considerations alongside traditional financial and operational analyses. By embedding climate risk into these existing structures, companies can better anticipate how extreme weather events, regulatory changes, or market shifts might affect costs, revenues, and asset values over time.

For regulators and investors, this integration signals maturity: it shows that a company understands climate change not just as an external environmental factor, but as a core business risk, one that warrants the same attention, controls, and board-level oversight as any other financial or strategic risk.

Metrics and Targets

Finally, the metrics-and-targets section provides the quantitative indicators used to assess and monitor climate-related risks and progress toward mitigation goals.
While SB 261 does not prescribe specific metrics, it expects consistency with the metrics used under related frameworks like SB 253 or CDP reporting.

At a minimum, companies are expected to disclose:

- The metrics they use to evaluate material climate-related risks (for example, measures of physical risk exposure or transition-risk intensity).
- The targets or goals they have established to reduce those risks or strengthen resilience.

When possible, companies should explain how these metrics influence executive incentives, investment decisions, or financial projections, reinforcing that climate considerations are integrated into core performance management.
Beyond these minimum expectations, CARB and the TCFD recommend including more specific and quantitative indicators to enhance transparency and show how climate considerations are integrated into business performance. Examples include:

- Greenhouse gas emissions data (Scope 1 and 2, and Scope 3 where material).
- Risk exposure metrics, such as the percentage of assets located in high-risk regions or the proportion of operations covered by climate insurance.
- Performance indicators, such as energy intensity, renewable-energy use, or capital expenditures on resilience and adaptation.
- Progress against targets, including interim and long-term emissions-reduction goals.

Takeaways

An effective SB 261 report is not a checklist but a cohesive narrative. Governance informs strategy; strategy drives risk management; and metrics provide evidence of progress.
Companies should explicitly reference how these elements connect, for example, how board oversight shapes strategic resilience planning, or how data collected for emissions reporting informs financial-risk modeling.
This integrated approach demonstrates that the company understands climate risk as a systemic business issue rather than a compliance exercise, which is precisely the intent behind both the TCFD and SB 261 frameworks.

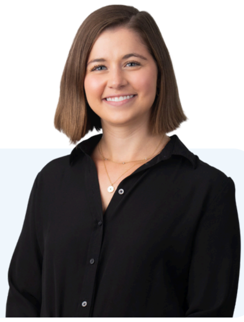
Why SB 261 Matters — Beyond Compliance

Beyond compliance, the most forward-looking organizations will treat SB 261 as an opportunity to integrate climate considerations into their broader enterprise risk management systems. Doing so not only strengthens resilience and transparency but also helps embed long-term sustainability into financial decision-making. A shift that regulators and investors increasingly expect. The law compels organizations to take a disciplined, forward-looking approach to climate risk management, encouraging them to understand how evolving environmental, market, and policy dynamics could affect their balance sheets, operations, and growth strategies. SB 261 can serve as a strategic planning tool rather than a compliance exercise. By systematically assessing both physical risks (such as extreme weather, heat stress, or supply chain disruption) and transition risks (including new regulations, carbon pricing, or shifting customer expectations), companies gain insights that directly inform capital investment, site planning, insurance coverage, and product strategy.

This process helps leadership identify which parts of the business are most exposed and where innovation or adaptation can create competitive advantage.

In short, while compliance may be the starting point, the true value of SB 261 lies in its ability to drive strategic foresight and organizational resilience. Executives who use this process to anticipate change, embed climate considerations into core planning, and align governance around long-term sustainability will not only meet regulatory expectations; they will lead in a marketplace that increasingly rewards transparency, preparedness, and trust.

Meet the authors



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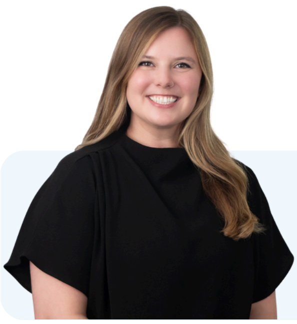

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