Davis Polk

California enacts anti-greenwashing requirements for climate-related claims and carbon markets

October 24, 2023 | Client Update | 8-minute read

Governor Newsom has signed the Voluntary Carbon Market Disclosures Act, a law intended to combat "greenwashing" by requiring disclosure on net zero, carbon neutrality and emissions reduction claims, as well as voluntary carbon offsets purchased, used, marketed or sold in California. The VCMDA, which becomes effective January 2024, applies to public and private companies that operate and make claims or purchase or use VCOs in California, or that sell or market VCOs in California.

On October 7, 2023, California Governor Gavin Newsom signed AB-1305, the Voluntary Carbon Market Disclosures Act (VCMDA).[1] The VCMDA is intended to address "greenwashing" by requiring detailed disclosure of the methodology for tracking and verifying claims made within California by entities operating within California regarding net zero, carbon neutrality or emissions reductions, as well as disclosure regarding voluntary carbon offsets (VCOs) purchased, used, marketed or sold within California. The VCMDA will become effective on January 1, 2024 and will require any covered disclosures to be updated at least annually. Violations of the VCMDA are subject to a civil penalty up to $2,500 per day per violation, not to exceed $500,000.

As discussed further below, as with the climate disclosure laws analyzed in our recent client update, key terms regarding the scope of the VCMDA are undefined (in particular, what it means to operate or make a claim within California). For example, given the nature of internet communications, it is unclear whether certain provisions of the VCMDA may be construed to apply to a company that operates in California and makes claims anywhere in the world regarding net zero or carbon neutrality as long as someone within California reads those claims via a company's website or other online communications. As with California's other recent climate disclosure laws, all companies that make or plan to make these types of claims or that market or sell such VCOs should assume that this law will be interpreted broadly. These companies should carefully review the VCMDA and consider preparing the required disclosures in advance of the VCMDA's January 1, 2024 effective date.

1. Overview of the VCMDA's requirements

The table below outlines the VCMDA's key requirements, which apply to three types of activities: certain types of net zero, carbon neutrality or emissions reduction claims; purchase or use of VCOs while making similar claims; and the marketing or selling of VCOs. As described in the table below, these requirements apply to entities that have some degree of connection to California (e.g., entities operating and making claims or purchasing or using VCOs within California, or selling or marketing VCOs within California).

Activities	Entities covered	Website disclosures required
VCMDA Section 44475.2 Making claims: - regarding achievement of net zero emissions - that an entity or product is carbon neutral - implying an entity or product does not add net carbon dioxide (CO2) or greenhouse gases (GHGs) to the climate - implying that an entity or product has made significant reductions to its CO2 or GHG emissions	Entities that operate within California and make claims within California	How these claims were determined to be accurate or accomplished How interim progress toward any goals described in these claims is measured Whether there is independent third-party verification of these claims or related data Disclosure may include, but not be limited to, any third-party verification of GHG emissions, and any science-based targets for the entity's emissions reduction pathway (and any related sector methodology or third-party verification)
VCMDA Section 44475.1 Purchasing/using VCOs *and* making any of the following types of claims: - regarding the achievement of net zero emissions - that an entity or product is carbon neutral - implying an entity or product does not add net CO2 or GHGs to the climate - implying that an entity or product has made significant reductions to its CO2 or GHG emissions	Entities that operate within California and purchase/use VCOs sold within California	Name of the entity selling the offset and the registry/program Project ID number Project name Offset project type and site location Protocol used to estimate emissions reduction or benefits Whether there is independent third-party verification of these claims or related data
VCMDA Section 44475 Marketing or selling VCOs	Business entities marketing or selling VCOs within California	Details regarding the carbon offset project, including protocols, location, timelines, project type, conformance to existing standards, durability, existence of verification and annual emissions reduced or carbon removed Details regarding accountability measures for projects that are not completed or don't meet projected reductions or removals Data and methods needed to independently reproduce and verify the number of reduction or removal credits issued by the project

2. Impact and key considerations

- **Broad applicability**. Similar to S.B. 253 and S.B. 261, also signed by Governor Newsom on October 7, 2023, the VCMDA could potentially have an impact beyond the border of California; however, key terms relating to the scope of its provisions are unclear. Notably, the concepts of "operating within" California and "making claims within" California are not defined in the VCMDA. In addition, the VCMDA applies to U.S. and foreign public and private companies, and unlike S.B. 253 and 261, it does not have minimum revenue requirements.

  Given the lack of defined terms, and the nature of internet communications, the requirements of Sections 44475.1 and 44475.2 of the VCMDA may be construed to apply even to a small company that has minimal operations in California if the company's claims are read by people within the state. Further, if a company markets or sells VCOs to people within California, that company will be subject to Section 44475 of the rule even if it has no other California operations. Section 4475.2 in particular is very broad in the types of climate-related claims governed by the disclosure requirement: not only does it cover "net zero" and "carbon neutral" claims, it also covers any claim that a company or product does not add net GHG emissions to the climate or has achieved "significant" GHG reductions. This language may be construed to cover just about any statement a company typically makes regarding its climate change policies or practices. These statements have proliferated in recent years, and appear regularly in company websites, advertising and marketing materials, sustainability reports, product labels and SEC filings.

  As such, any company that operates in California, regardless of size, and that makes or plans to make statements regarding net zero or carbon neutrality or otherwise relating to GHG reduction policies or practices, or purchases or uses VCOs in California (as well as companies that sell or market VCOs within California), should closely review the VCMDA and consider taking steps to comply.
- **Interaction with similar requirements and standards in other jurisdictions**. Regulators and lawmakers in the United States and around the world have increased their focus on climate-related disclosures and VCOs. For example, the SEC's proposed climate change disclosure rule includes provisions requiring disclosure of climate-related targets and goals, including data indicating progress toward the goals and disclosure of the use of carbon offsets and renewable energy credits. The VCMDA overlaps with and in some respects goes further than the SEC's proposed rule, including by potentially requiring disclosure surrounding claims of past emissions reductions. In addition, the "Green Guides" issued by the U.S. Federal Trade Commission (which were last revised in 2012 but are currently being updated) provide guidance to businesses regarding how to avoid making environmental claims that might mislead consumers and expose businesses to liability. Outside the United States, the European Union and the United Kingdom are developing rules and guidance that are intended to regulate and require evidence of certain environmental claims, including those related to carbon neutrality and climate friendliness.

  Further, as described in the table above, while the VCMDA requires detailed disclosures regarding VCOs, the VCMDA does not make reference to existing standards commonly used in the VCO industry, such as the Voluntary Carbon Markets Integrity Initiative's Claims Code of Practice and the Integrity Council for the Voluntary Carbon Market's Core Carbon Principles.[2] It remains to be seen how these standards will inform the implementation and enforcement of the VCMDA.

3. Next steps for companies

Given the VCMDA's imminent January 1, 2024 effective date, companies that expect to be subject to the VCMDA should begin taking steps to identify, clarify and substantiate any existing or planned net zero, carbon neutrality or emissions reduction disclosures, as well as gather data regarding VCOs. Such steps could include:

- **Identifying any existing or in-progress climate claims** on websites, product labels, sustainability reports, SEC filings and similar locations, and collecting (or generating) sufficient supporting information to meet the VCMDA's disclosure requirements. In addition, while the VCMDA does not require third-party verification of climate claims, it does require disclosure of the existence of any such verification and suggests that such verification could be a best practice, in particular for any quantitative claims.
- **Performing further due diligence into VCOs** purchased or used in California, if necessary, to support the VCMDA's specific disclosure requirements in this area. In addition, companies that market or sell VCOs in California should expect to receive an increase in requests for data from their customers stemming from the VCMDA.

These steps can be considered best practices to help prevent negative press and claims of greenwashing and related litigation more generally.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

Emily Roberts
+1 650 752 2085
emily.roberts@davispolk.com

Stephen A. Byeff
+1 212 450 4715
stephen.byeff@davispolk.com

David A. Zilberberg
+1 212 450 4688
david.zilberberg@davispolk.com

Michael Comstock
+1 212 450 4374
michael.comstock@davispolk.com

Timothy J. Sullivan
+1 212 450 4108
timothy.sullivan@davispolk.com

1 On the same day, Governor Newsom signed S.B. 253 and S.B. 261, which are discussed in our prior client update. Governor Newsom vetoed a fourth climate-related bill, the Voluntary Carbon Offsets Business Regulation Act (SB 390), which proposed standards intended to ensure the quantifiability and durability of carbon credits. It is possible that a version of SB 390 could be re-proposed by the California legislature in the future.

2 The Claims Code of Practice, which was finalized in June 2023, provides guidance and steps for companies to help ensure they credibly use carbon credits as part of their climate commitments. The Core Carbon Principles, which were finalized in March 2023, are meant to create consistent and standardized guidelines to help ensure that carbon credits in the voluntary market are "high-integrity."