

October 7, 2022

VIA ONLINE SUBMISSION

Christopher J. Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

RE: Request for Information (“RFI”) on Climate-Related Financial Risk

Dear Mr. Kirkpatrick:

Xpansiv Ltd. (“Xpansiv”)¹ welcomes the opportunity to provide comments on the Commodity Futures Trading Commission’s (the “Commission” or “CFTC”) efforts around climate-related financial risk and underlying commodities markets.²

Overview

Xpansiv commends the Commission’s aim to promote responsible innovation and avoid systemic financial risks, which will improve the level of transparency of climate risk and mitigation data while driving consistency in how such data is prepared, presented, audited, and used by markets. Xpansiv also generally supports and endorses the comments submitted in response to the Commission’s RFI by the CME Group, Inc.

Companies and financial markets increasingly demand that environmental risks and opportunities be transparent and priced into commerce and investments. Xpansiv applauds the various global efforts to effectuate rules for disclosing climate risks and impacts associated with doing business, including Scope 1, 2 and 3 emissions reporting and progress on net zero targets. Xpansiv also supports efforts to address other growing transition risks³ and encourages regulators to strive for harmonized disclosure requirements and metrics.

Xpansiv believes more—particularly more harmonized and more credible— environmental data needs to be rendered accessible, transparent, and transferable across current financial market modalities to adequately support near- and long-term business and investment decisions in a rapidly warming world.

¹ Xpansiv Ltd., formerly Xpansiv CBL Holding Group, represents a family of entities including CBL Markets (USA), LLC, CBL Markets Australia Pty Ltd., and Xpansiv Data Systems, Inc.

² The Commodity Futures Trading Commission, Request for Information on Climate Related Financial Risk, 87 Fed. Reg. 34856 (published June 8, 2022); as extended by The Commodity Futures Trading Commission, Request for Information on Climate Related Financial Risk, 87 Fed. Reg. 43501 (published July 21, 2022).

³ See, e.g., Securities and Exchange Commission, The Enhancement and Standardization of Climate-Related Disclosures for Investors, 87 FR 21334 (published April 2022); European Financial Reporting Advisory Group, European Sustainability Reporting Standards Exposure Drafts (published April 2022); International Sustainability Standards Board, Exposure Draft IFRS S2 Climate-related Disclosures (published March 2022).

As the Commission evaluates its role in the transition economy, Xpansiv urges it to maintain and reinforce its current, well-established approach to environmental commodities; apply the same approach to emerging digital environmental commodities as it does to underlying physical commodities; and continue to collaborate with other federal agencies and civil society to help incentivize greater transparency and scalability of climate action. It is on these bases that Xpansiv offers the following comments for the Commission’s consideration.

Introduction

Xpansiv is the leading market infrastructure platform in the growing voluntary carbon market (“VCM”), with over a third of global credits transacting across our networked platform. A majority of voluntary carbon units issued last year were on registries powered by APX, our wholly owned subsidiary. We are linked with all of the major registries and are building the infrastructure to scale a trusted, transparent, and credible market. We work with CME Group to provide deliverables underlying voluntary carbon futures contracts, and S&P Global Commodity Insights to provide benchmark carbon price reporting.

Recommendations

1. Voluntary Spot Carbon Market Transactions

Derivatives market participants have understood for years that the Commodity Exchange Act of 1936 (“CEA”) and the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) have left certain commodity transactions outside the Commission’s scope of regulation. Congress conferred upon the Commission “exclusive jurisdiction” over commodity futures and options thereon but generally left outside of the CFTC’s jurisdiction spot and forward transactions in which the parties intended to make or take delivery of a commodity.⁴

The CEA broadly defines the term “commodity” to encompass virtually all goods, services, and interests.⁵ The CFTC generally recognizes “environmental commodities,” including emissions allowances, carbon offsets, carbon credits and renewable energy certificates, as commodities akin to wheat and soybeans rather than “commodity interests,” such as futures or swaps.⁶ Agricultural and exempt commodities that can be physically delivered and consumed are nonfinancial commodities.⁷

Environmental commodities have been treated by the CFTC as intangible commodities that can be physically delivered and consumed—and therefore as commodities that qualify as nonfinancial commodities.⁸ In particular, environmental commodities may be physically delivered through ownership

⁴ Matthew F. Kluchenek, *The Status of Environmental Commodities Under the Commodity Exchange Act*, Harvard Business Law Review Online, 39 (2015).

⁵ 7 U.S.C. § 1a(9).

⁶ Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 Fed. Reg. 48208, 48256 (Aug. 13, 2012) (“Products Release”).

⁷ Products Release at 48232.

⁸ Retail Commodity Transactions Involving Certain Digital Assets, 85 Fed. Reg. 37734, 37741 (June 24, 2020); Products Release at 48233.

transfer and consumed by use in commerce or to satisfy the terms of voluntary net zero commitments or mandatory environmental programs.⁹

The Commission has also acknowledged that “market participants often engage in environmental commodity transactions in order to transfer ownership of the environmental commodity (and not solely price risk), so that the buyer can consume the commodity in order to comply with the terms of mandatory or voluntary environmental programs.”¹⁰ The settlement method for environmental commodities is “equivalent to that of physical commodities where ownership is transferred by delivering a warehouse receipt from the seller to the buyer, thereby indicating the presence in the warehouse of the contracted for commodity volume.”¹¹ Furthermore, “it is possible to manipulate the deliverable supply of an environmental commodity just as it is for a tangible commodity.”¹²

Sales of commodities on a “spot” or “cash” basis where the seller delivers the purchased commodity to the purchaser within a timeframe typical for sales of such commodities are generally outside the scope of the CFTC’s jurisdiction. Similarly, sales of commodities where delivery of the commodity is deferred for reasons of commercial convenience or necessity, known as “forwards,” are generally outside of the CFTC’s jurisdiction. However, the CFTC has the authority to police fraud and manipulation in transactions that involve any commodity irrespective of whether the transaction at issue constitutes a spot or forward.

In discussing environmental commodities, in the CFTC and SEC’s joint final rules defining certain terms in the Dodd-Frank Act, the Commission noted that it:

“Those two features—ownership transfer and consumption—distinguish such environmental commodity transactions from other types of intangible commodity transactions that cannot be delivered, such as temperatures and interest rates. The ownership transfer and consumption features render such environmental commodity transactions similar to tangible commodity transactions that clearly can be delivered, such as wheat and gold.

As a result, the CFTC found that ‘environmental commodities can be nonfinancial commodities that can be delivered through electronic settlement or contractual attestation. Therefore, an agreement, contract or transaction in an environmental commodity *may qualify for the forward exclusion from the swap definition if the transaction is intended to be physically settled.*’

Conversely, as described by an industry participant, to the extent that emissions allowances, carbon offsets/credits and RECs [renewable energy certificates] are not physically settled (*i.e.*, consumed), but traded in secondary market fashion like a stock or bond, the forward exclusion would likely not apply to the transaction. Moreover, the CFTC has stated that, if a contract were to include the right to unilaterally terminate an

⁹ Products Release at 48233.

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.*

agreement under a pre-arranged contractual provision permitting financial settlement, the forward exclusion would not apply.”¹³

In Xpansiv’s view, because the Commission and market participants have historically understood that spot transactions of environmental commodities are not subject to CFTC regulation, it may be beneficial for the Commission to consider releasing guidance clarifying how such commodities are treated—particularly the distinction between the physically-settled spot markets in carbon offsets and derivatives transactions (or security-based digital assets) that securitize, reference or correlate to an underlying physical environmental commodity. Such guidance will assist not only in derivative product innovation efforts, but also in bringing clarity to the regulatory treatment of intangible environmental commodities and digitized or tokenized environmental assets that physically settle.

As carbon markets scale and as financial markets in general shift toward improved collection and disclosure of climate-related corporate risk data, Xpansiv supports further guidance from the Commission on ways to monitor forward and futures transactions to prevent and address fraud and manipulation.

2. Digitized Environmental Assets

Digital assets—including native or primitive 1:1 tokens of environmental commodities—can offer myriad carbon accounting, market infrastructure and climate-related risk-mitigating benefits. Emerging market capabilities to “commoditize” or “unitize” environmental attributes as registered environmental commodities should be underpinned by an accessible and transparent network of measurement, reporting and verification (“MRV”) data that provides an audit trail to substantiate and keep a record of corporate environmental claims. That underlying data can help build trust and transparency in environmental commodities and accelerate corporate utilization of derivatives products to help manage defined climate-related risks.

As environmental commodity markets digitize, regulatory and governance regimes must also enable and enforce consistent treatment across emerging classes of digital assets, distinguishing digitized environmental commodities from opaque or unaccountable cryptocurrencies. A 1:1 layer of digitized (e.g., tokenized) environmental commodity, which is capable of physical delivery and settlement, is no different than any other spot environmental commodity from a regulatory treatment perspective. A layer 1 native token ecosystem, one that puts the standards bodies and government entities in charge of asset verification, then enables financial instruments to be tied or correlated to an auditable dataset substantiating environmental claims and identifying market participants trading in or retiring such claims.

That layer 1 ecosystem should be considered functionally and existentially distinct from security-based tokens or cryptocurrencies. There has been recent proliferation of new entrants in environmental markets that are attempting to utilize some form of security-backed tokenization model with and without permission from standards bodies. These recent efforts to offer tokenized trading units secured by underlying environmental commodities create new complexity with respect to regulatory oversight and accountability for related instruments—i.e., connected, subset, linked, or other related products that are backed by underlying traditional environmental assets. The private sector and regulators should cooperate to evaluate the best role for such digital assets in helping scale climate action, and build

¹³ *Id.* at 48,233–35.

approval, accountability and governance frameworks that appropriately define the various asset classes, prevent double counting of environmental claims, and protect and encourage enhanced reporting and transparent accountability.

3. Collaboration with Existing Efforts on Climate-Related Financial Risk

The private sector increasingly recognizes that climate-related business and financial risks are material to companies' overall health and economic value and should be rendered transparent and measurable. Private companies should be able to organize around a common set of climate-related risk accounting methodologies that share standardized sustainability and climate impact definitions, datapoint requirements, and derived risk or environmental claim formulae. Such methodologies will enable the data-driven insights and intelligence that are at the core of every macroeconomic, sector-based, and company-specific decarbonization pathway. The collection and disclosure of decision-useful environmental data—e.g., information related to governance, strategy, risk management and metrics and targets—is a necessary first step to address and price climate-related business and financial risks.

Other regulatory bodies—such as the Securities and Exchange Commission (“SEC”) in the United States and the European Financial Reporting Advisory Group (“EFRAG”) in the European Union—have recognized the relevance of such disclosures and have proposed rules to mandate them. Xpansiv generally supports the various efforts to achieve widespread climate-related risk disclosures to the extent they align with and build upon existing standards and best practices promulgated by, e.g., the Task Force on Climate-Related Financial Disclosures (“TCFD”), the Sustainability Accounting Standards Board (“SASB”), and the International Sustainability Standards Board (“ISSB”). Continued collaboration between the Commission’s market advisory committees is needed with such independent organizations, and across regulatory bodies, to harmonize the various classification systems and taxonomies to standardize the packaging and delivery of information and reportable data flows to investors, consumers, and governments.

We again thank the Commission for allowing us to provide feedback on the state of voluntary carbon markets as well as for its consideration of these comments. If you have any questions, please do not hesitate to reach out to Michael Goldstein at mgoldstein@xpansiv.com.

Sincerely,

Xpansiv