Standards Board for
Alternative Investments Limited
7 Henrietta Street
London
WC2E 8PS
United Kingdom
www.sbai.org

Tel: +44 20 3405 9042

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The International Sustainability Standards Board (ISSB)
IFRS Foundation
Columbus Building, 7 Westferry Circus
London, E14 4HD
Submitted by Email: commentletters@ifrs.org

Re: April 2025, Exposure Draft Amendments to Greenhouse Gas Emissions Disclosures: Proposed Amendments to IFRS S2[1]

Dear Sir or Madam,

The Standards Board for Alternative Investments (SBAI) welcomes the opportunity to respond to the ISSB's Exposure Draft ED/2025/1 proposing targeted amendments to IFRS S2 Climate-related Disclosures. We commend the ISSB for its consultative approach and its continued efforts to enhance global comparability and standardisation of sustainability disclosures.

At the SBAI we are an active alliance of managers and investors dedicated to advancing responsible practices, partnership, and knowledge in the alternatives industry. At our core is a community that is committed to knowledge sharing, informed dialogue, and innovation. We set clear standards and actively promote responsible practice to normalise quality, fairness, and comparability to enhance decision-making. Together, our community of allocators and managers create real world solutions – in short, we solve for better.

The SBAI's *Alternative Investment Standards*[2] are supported globally by over 250 institutional investors and alternative investment managers – spanning a diverse range of strategies including hedge funds, macro, credit, systematic, and commodity-focused portfolios – collectively overseeing more than US$9 trillion in assets. The SBAI is an Affiliate Member of the International Organisation of Securities Commissions (IOSCO), and we support global efforts to facilitate fair and efficient markets, reduce systemic risk, and enable investors to make well-informed investment decisions.

We broadly support the intent of the Exposure Draft to reduce the implementation burden while preserving decision-useful information and encourage the adoption of ISSB standards. In particular, the targeted relief mechanisms are a welcome recognition of the complexity (and cost) faced by multi-jurisdictional preparers.

[1] https://www.ifrs.org/content/dam/ifrs/project/amendments-greenhouse-gas-s2/issb-ed-2025-1-greenhouse-gas-s2.pdf
[2] The Alternative Investment Standards ("Standards") address key areas of alternative investment practice including disclosure, valuation, risk management, fund governance, and shareholder conduct. Access here: https://www.sbai.org/standards.html

Response to Question 1: Measurement and Disclosure of Scope 3 Category 15 (Financed Emissions)

We recommend that the ISSB considers how different types of derivatives can matter in the context GHG-emission accounting, to ensure the chosen approach is fit for purpose and enables investors and other users of the data to make well-informed decisions regarding investment and risk-management.

While the SBAI agrees that the term 'derivatives' is very broad, covering a very wide spectrum of assets – some might indeed have no relevance GHG-emission accounting purposes (e.g., FX, commodities[3]) – the SBAI believes it is worthwhile assessing how certain derivative exposures do matter for GHG-emission accounting as consequence of both their underlying economic exposure as well as their impact on market price formation for their equivalent cash positions.

Specifically, before deciding about (optional) ex/inclusions of certain instruments in the measurement and disclosure, we believe the ISSB should:

- Understand the key considerations of different users and providers of the data, including institutional investors (i.e., the ultimate users/beneficiaries of the data) and investment managers (as providers of the information for investment funds) – versus banks and others, who act as both traders an holders of derivative instruments.
- Assess how decisions about ex/inclusion of data impact the reliability, consistency, and comparability of the reporting framework, including potential greenwashing risk.

The SBAI highlights that the <u>(optional) exclusion of derivatives as proposed by ISSB in paragraph 29A(a) stands in contradiction with the SBAI *Principles for GHG-Emission Accounting in Alternative Investment Strategies ("Principes")*</u>[4], which explicitly incorporates certain derivatives[5], thereby enabling investors to make well-informed investment decisions.

The conclusions of this report are the culmination of extensive effort by the SBAI's Responsible Investment Working Group (constituted by leading institutional investors and alternative asset managers globally) as well as peer organisations and standard-setters in this space. Likewise, they are consistent to separately developed guidance from other industry groups representing the ultimate users/beneficiaries of this data, including IIGCC[6] and MSCI[7]. We therefore affirm that derivatives should not be excluded from efforts to improve transparency.

Overview: SBAI Principles for GHG-Emission Accounting in Alternative Investment Strategies ("Principes")

- Developed through 2022/2023 to address shortcomings of existing GHG-emission accounting and reporting standards regarding derivative and short positions which gave rise to greenwashing concerns and undermined comparability.
- Seek to provide institutional investors and asset managers a consistent and comparable framework to enable well-informed decisions investment decisions regarding risk, market impact, etc.
- Recognise that economic exposure, irrespective of instrument type (e.g., cash or synthetic), contributes equally to influencing the cost of capital of underlying entities, and give rise to equivalent economic and risk exposure.
- Apply a symmetric, implementation-agnostic approach, using delta-adjusted attribution methods

[3] See Appendix 2

[4] SBAI Principles for GHG-Emission Accounting in Alternative Strategies (January 2024), access: https://www.sbai.org/resource/principles-for-ghg-emission-accounting-in-alternative-strategies.html

[5] Derivatives referenced in PCAF's Standard for financed emissions: listed and unlisted equity, corporate bonds and business loans, project finance, commercial real estate, mortgages, motor vehicle loans, and sovereign debt

[6] IIGCC Derivatives and Hedge Fund Guidance (February 2024), access: https://www.iigcc.org/resources/derivatives-and-hedge-funds

[7] MSCI ESG and Climate Reporting with Derivatives (January 2024), access: https://www.msci.com/research-and-insights/paper/esg-and-climate-reporting-with-derivatives

From an institutional investor perspective, there are many reasons and requirements for why exposure to derivatives matter in the context of GHG-emission accounting, including:

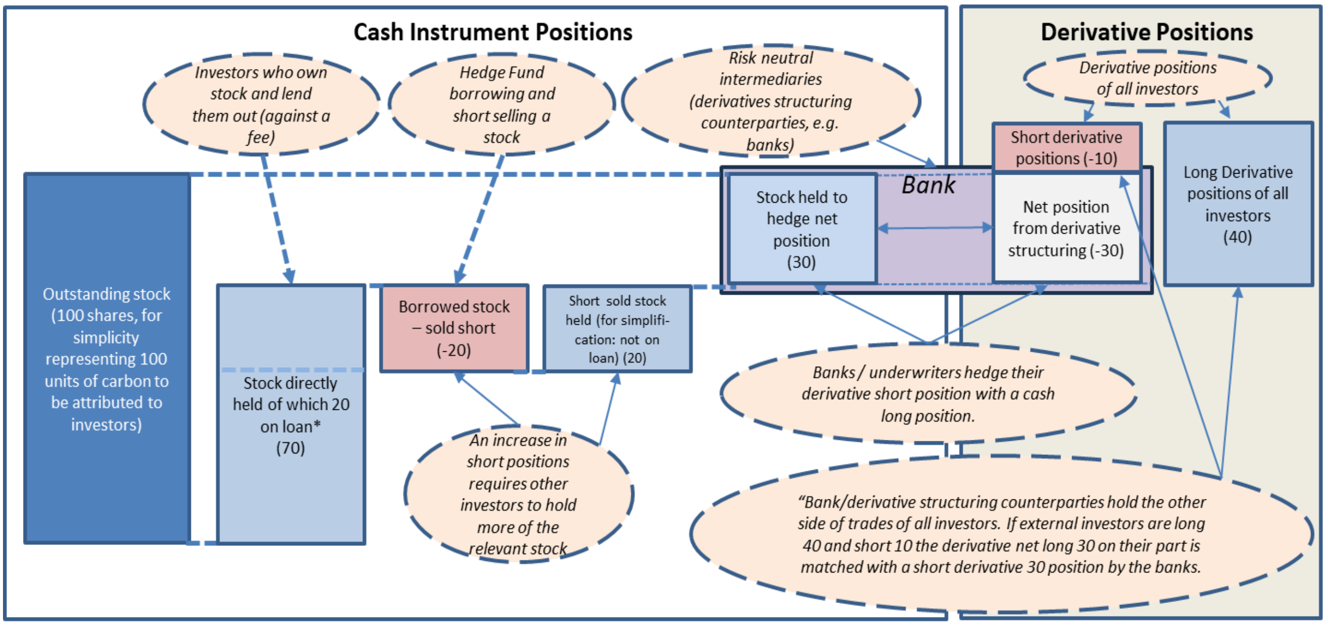
- Understanding risks in relation to GHG-emissions (which is a stated objective of ISSB), irrespective of whether these risk exposures arise via cash or synthetic holdings of equities/bonds
- Understanding true net risk, i.e., incorporating the impact of derivative hedges and short positions
- Understanding the impact on issuer cost of capital, given that derivatives and short positions matter in a manner equivalent to long or short cash positions (see appendix 1)
- Preventing greenwashing, for example by 'hiding' heavy emitters by structuring exposure synthetically with derivatives to artificially lower reported emissions (and inaccurately assess potential risk)

The SBAI would be delighted to meet with the ISSB team to discuss the extensive findings of our work, and how the ISSB efforts can be taken forward in a manner that provides investors with meaningful information about GHG-emissions. Please do not hesitate to contact us for further detail.

Yours sincerely,

Thomas Deinet
Executive Director
Standards Board for Alternative Investments (SBAI)

Appendix 1: Illustration of Long and Short Positions in Cash Instrument and Certain Derivatives



Short selling increases the supply of stocks, thereby increasing cost of capital for issuers

The net derivative exposure of all investors has real world impact on the demand for a stock, affecting cost of capital**

* Stock held on loan refers to the practice of loaning shares of stock (or other securities) to other investors against collateral. Institutional investors engaging in securities lending earn a borrowing fee, increasing their returns. It is common practice, helps financial markets keep functioning smoothly, enabling risk management as well as short selling. The lender remains exposed the fluctuations in value of the securities on loan. The security is returned on demand to the lender.

**if short derivative positions exceed long derivative positions, derivative structuring counterparties will have to hold short positions, thereby increasing the supply of stock in the market.

The illustration shows that the aggregate impact of short positions and derivatives matter, notably:

- Short positions require other investors to hold more of the underlying assets, increasing cost of capital (no different to "selling" an asset).
- Net derivative exposure of all investors, assuming the risk of certain underlying (e.g., corporate) economic activities, will need to be replicated in the market for the relevant cash instruments (e.g., equities) by the derivative counterparties (e.g., banks, which do not assume any of the risk). If, in aggregate, investors holding derivatives have a net long exposure, the derivative counterparties will need to hold this exposure in the market to remain market neutral. If investors hold a net short exposure, the derivative counterparties will need to replicate this exposure through short-selling.
- There is **symmetry** of impact of long and short positions (across all instruments) in how they influence future cost of capital.
- There is **equivalence** of impact, whether a position is held via cash instruments, or derivatives.

Appendix 2: Responsible Investment and GHG-Emission Accounting in Direct Commodity Investments

While we call for the inclusion of certain derivatives in reporting frameworks, not all derivatives should be accounted for – namely, commodities. Our analysis, published in our recent guidance on *Responsible Investment and GHG-Emission Accounting in Direct Commodity Investments*[8] concludes that as these instruments do not provide investment capital nor impact cost of capital, there is no credible mechanism for real-economy emissions impact. Inclusion of such exposures would introduce risks of greenwashing and data distortion as consequence of emission attribution to agentless products. We therefore support exclusion of commodity derivatives from financed emissions metrics.

[8] SBAI Responsible Investment and GHG-Emission Accounting in Direct Commodity Investments (May 2025), access: https://www.sbai.org/resource/responsible-investment-and-ghg-emission-accounting-in-direct-commodity-investments.html