

Why EU action to tackle deforestation should not let finance off the hook

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Introduction

Last summer's devastating Amazon fires and the more recent Australian fires are a stark reminder of the immediate threats facing the world's forests.

In 2018, the tropics lost 12 million hectares of tree cover, of which 3.6 million hectares of primary rainforest disappeared, an area the size of Belgium.¹

These forests are crucial for the global climate and biodiversity. Current voluntary commitments from business, including banks, to tackle deforestation have failed to deliver the change in behaviour needed to halt this disastrous environmental destruction.

The EU is a key player in global deforestation as highlighted by European Commission research², which showed that the EU imported and consumed 10% of the global production of crops and livestock products associated with deforestation over the period 1990-2008.

The European Commission (EC)'s Communication "*Stepping up EU Action to Protect and Restore the World's Forests*", published on 23rd July 2019 is a welcome step in the fight against global deforestation. It sets out options for reducing the impact of the EU on global deforestation.³

A broad agreement has since emerged across the EU institutions that action, including regulatory measures, are now required to ensure that the EU's supply

chains do not contribute to deforestation. This could potentially include mandatory due diligence with companies required to check their supply chains for deforestation risks.⁴

There is growing awareness of the role of finance in fuelling deforestation. Analysis of the data from a recent *Global Witness* investigation into the financing of six agribusiness companies linked to forest destruction in the climate critical forests of the Amazon, Congo Basin and Papua New Guinea, found that **EU-based financial institutions were one of the main sources of funds and had backed these companies to the tune of €7 billion between 2013 and 2019.**⁵

The EC communication acknowledges the role of the financial sector in forest destruction. Action is now needed to take forward regulatory measures and ensure that any legislation on EU supply chains does not exclude finance.

The case for EU legislation on mandatory due diligence

After a decade of commitments⁶ to achieve 'zero net deforestation by 2020' in key forest-risk commodities, companies and financial institutions are still far from realising this goal, with some signatories

now admitting they will miss the 2020 target.⁷

Meanwhile, the world's largest financial institutions continue to sink vast sums into companies either levelling forests themselves or via other companies, often in blatant violation of their own deforestation policies and public commitments.⁸

It is against this backdrop that organisations and the corporate sector are calling for legislation requiring companies to undertake checks on their supply chains and financing to identify, prevent, mitigate and report on risks of deforestation, environmental harm and related human rights abuses.⁹

Due diligence is an established business practice routinely undertaken for commercial and legal risks. The OECD has already developed internationally agreed guidance on how these checks should be done for environmental harms and human rights abuses.¹⁰

Mandatory due diligence, which legally requires companies to undertake checks, is a feature of legislation across a range of sectors, including conflict minerals, timber and investments. As set out in a recent Global Witness briefing published jointly with Client Earth¹¹, there are lessons to learn from its use in these other sectors, including the importance of a rigorous enforcement regime.

The introduction of new rules requiring due diligence would level the playing field to ensure that businesses who disregard the impact of their operations on the environment and human rights, do not

undercut others already assessing and mitigating these risks.

Given its forward-looking function in identifying potential risks and adverse impacts, mandatory due diligence could help ensure that no company or financial institution pursues profits linked to deforestation¹² but instead chooses to invest in sustainable activities and supply chains that will endure and thrive as the economy shifts to adapt to new realities in a climate crisis age.




The EU's €7 billion backing to companies linked to deforestation

In September 2019, Global Witness published a new investigation, *Money to Burn*¹³, which examined the financing of six global agribusinesses groups¹⁴ most implicated in deforestation in the world's three largest tropical rainforests in the Amazon, Congo Basin and Papua New Guinea to produce palm oil, beef and rubber.

➤ Analysis of the data used in the investigation reveals that **EU-based financial institutions were the biggest provider of international finance, after Brazil, for companies directly or indirectly involved in deforestation. They provided a staggering €7 billion between 2013 and 2019¹⁵ (as shown in Table 2). This included financing from EU registered banks like Santander and Deutsche Bank.**

➤ This highlights the crucial role played by EU based financiers and the need for the EU to ensure any legislation tackling the EU's global deforestation footprint does not let finance off the hook.









Table 1 – Breakdown by EU Member State of financial support between January 2013 and March 2019 from financial institutions based in those Member States to the six agribusinesses named in *Money to Burn* implicated in deforestation. Amounts are given in € EUR.

| Country | | Amount (€, millions) ▼ |
|-------------|---|------------------------|
| Spain |  | 1,942.59 |
| France |  | 1,926.43 |
| Netherlands |  | 1,760.95 |
| Germany |  | 1,205.18 |
| Italy |  | 356.61 |
| Cyprus |  | 164.36 |
| Sweden |  | 20.45 |
| Denmark |  | 4.25 |
| Belgium |  | 0.38 |

Source: Profundo •



Table 2 – Breakdown by financial jurisdiction of financial support between January 2013 and March 2019 to the six agribusinesses groups named in *Money to Burn* implicated in deforestation. Amounts are given in € EUR.

| Countries | | Amount (€, millions) ▼ |
|-------------|---|------------------------|
| Brazil |  | 7,856.08 |
| EU |  | 7,381.44 |
| UK |  | 5,890.01 |
| US |  | 5,188.25 |
| Singapore |  | 4,560.14 |
| Australia |  | 2,986.14 |
| Japan |  | 2,620.45 |
| Others* | | 2,269.69 |
| Switzerland |  | 1,310.07 |

*‘Others’ are: Bermuda, South Korea, India, China, United Arab Emirates, Malaysia, Canada, Africa, Dubai, Egypt, Gabon, Norway, Liechtenstein, South Africa, Mexico, Taiwan, Chile, Andorra, Global

Source: Profundo •



Why finance shouldn't be excluded from due diligence obligations

Over the last decade, the digital disruption and influence of technology has made it much easier for policy-makers, researchers, media, NGOs and analysts to track financing linked to deforestation and identify the role that EU finance plays as an integral part of the agribusiness supply chain.¹⁶

Concurrently, a growing number of international and national institutions have clarified that finance should not be exempt from corporate responsibility commitments and standards.

Finance is included under the United Nations Guiding Principles on Business and Human Rights and the OECD Guidelines on Responsible Business Conduct.¹⁷ The Dutch Banking Sector Agreement has also articulated the due diligence responsibilities of banks in relation to forest-risk commodities such as palm oil and land-related human rights abuses.¹⁸ Voluntary initiatives in forest-risk commodities including the Soft Commodities Compact and Roundtable on Sustainable Palm Oil also include financial institutions among their membership.¹⁹

The growing shift to ensure that all relevant corporate entities are covered under a due diligence approach is reflected in France's 2017 *Duty of*

Vigilance law, which applies to all large French companies, including banks.²⁰

The distinction between 'finance' and other types of company is not always clear. For example, agribusiness firms can provide credit services or third-party financial services to farmers and an investment firm may fully own and operate an agribusiness enterprise.²¹

If due diligence legislation excludes finance it could feasibly result in one arm of a company being prevented from undertaking harmful practices that drive deforestation while a separate arm of the company is able to finance, and profit from, these same activities.

Therefore, any new EU regulation on deforestation risk must include financial institutions within its scope to avoid the risk of setting double standards for different sectors and sending the message that deforestation risk is acceptable for certain sectors e.g. finance, but not for others e.g. supply chains linked to agriculture.

Given the role of both investment and consumption in driving deforestation, it is essential that EU action covers both in order to effectively mitigate the overall risk.

How to ensure coherency with other EU policies

The July 2019 EC Communication highlighted that, "*it is of paramount importance to redirect the important flows of private finance in the agricultural sector*

[...] towards activities that are deforestation-free.”

Existing EU policy instruments and others under development, including those under the European Commission action plan on financing sustainable growth²², may help to provide some guidance for the financial sector in assessing and reporting environmental risks. However, they will not on their own redirect finance away from activities and companies associated with deforestation. We believe that this will only occur through a coherent approach that places the same due diligence obligations on supply chains and banks.

The EU Regulation on Disclosures Relating to Sustainable Investments and Sustainability Risks (DSR Regulation)²³ introduces obligations on how investors integrate Environmental Social and Governance (ESG) factors and assess and mitigate risks²⁴, as well as requiring the disclosure of impacts of investments and publication of due diligence policies. However, it has limited detail on the requirements for the due diligence policy and as yet has no details of sustainability risks. The absence of these crucial details means it is unlikely to be effective in relation to deforestation risks.

The upcoming EU taxonomy²⁵ will articulate the standard for products branded as green finance and provide an important benchmark on forest-related due diligence. However, green finance is only a very small portion of global financial markets and as long as the

taxonomy applies only to green finance products, it will not prevent companies exposed to deforestation from finding financing from EU based financial institutions for their activities.

The current revision of Non-Financial Reporting Directive (NFRD)²⁶ is expected to provide further guidance on how a company should report on its aggregate exposure to a range of environmental, social and governance risks. While general corporate reporting standards can help standardise information at a broad level they lack the detail needed to generate meaningful information on specific risks and risk management processes. The NFRD also does not require due diligence in line with international standards, nor contain any requirement that companies refrain from financing activities that contribute to harmful outcomes.

These developments show that due diligence for financial institutions on sustainability risks is becoming an accepted approach by financial institutions and policy makers. However, they are likely to prove ineffective when it comes to requiring financial institutions to identify and mitigate deforestation risks and are even less likely to redirect private finance away from deforestation. This is due to issues outlined above, including: limited scope; reliance on very limited reporting; inadequate detail on due diligence processes, or no requirement for due diligence; and lack of detail on deforestation risks.

Global Witness has investigated and exposed the role that EU based investors and their subsidiaries have played in bankrolling companies causing social and environmental harm, including destruction of primary forests. As we set out in our report *Indecent Exposure*²⁷, in many cases investors failure to identify environmental, social and governance risks in their investment chains before they were publicly exposed. In some cases, investors did not withdraw their investments even when this evidence came to light.

It is therefore crucial that finance is not exempt from any forthcoming legislation addressing the EU's global deforestation footprint.

Conclusion

In October 2018, the Intergovernmental Panel on Climate Change (IPCC) report stressed that action to stop deforestation and forest degradation, and to restore forests, is critical to avoid global temperature rise beyond 1.5 degrees.²⁸

The EU, as a major key player in the global markets of commodities linked to deforestation, has an important role to play to stop the destruction of our world's carbon rich forests.

Climate change and preserving natural resources are a major concern for European citizens, as the 2019 YouGov Poll showed an overwhelming 87 per cent of EU citizens expressed support for new laws to combat deforestation.²⁹

In order to achieve EU's climate and sustainable objectives and hence contribute to the halt of global deforestation, the EU should set obligations for companies including banks where we have seen a failure of voluntary initiatives.

EU action to require companies, including banks, to take responsibility for their impacts on the environment and human rights is essential if the EU is to tackle its own role in the climate and deforestation crisis.

www.globalwitness.org

¹World Resource Institute, <https://www.wri.org/blog/2019/04/world-lost-belgium-sized-area-primary-rainforests-last-year>, 25 April 2019

²European Commission, The impact of EU consumption on deforestation https://ec.europa.eu/environment/forests/impact_deforestation.htm, 2013.

³European Commission, Stepping Up EU Action to protect and restore world's forests https://ec.europa.eu/info/sites/info/files/communication-eu-action-protect-restore-forests_en.pdf, 23 July 2019

⁴ European Council conclusions on the Communication on stepping up EU action to protect and restore the world's forests, <https://www.consilium.europa.eu/media/41860/st15151-en19.pdf>, 16 December 2019;

European Parliament resolution on the European Green Deal https://www.europarl.europa.eu/doceo/document/TA-9-2020-0005_EN.pdf, 15 January 2020; European Commission Communication on The European Green Deal,

https://ec.europa.eu/info/sites/info/files/european-green-deal-communication_en.pdf , 11 December 2019

⁵ See data included in: Global Witness, Money to Burn

<https://www.globalwitness.org/en/campaigns/forests/money-to-burn-how-iconic-banks-and-investors-fund-the-destruction-of-the-worlds-largest-rainforests/> , 23 September 2019

⁶ This includes commitments made under the 2014 Soft Commodities Compact, which includes bank signatories - Banking Environment Initiative (BEI) and Consumer Goods Forum (CGF)'s 'Soft Commodities' Compact

<https://www.cisl.cam.ac.uk/business-action/sustainable-finance/banking-environment-initiative/programme/sustainable-agri-supply-chains/soft-commodities> Accessed 28 January 2020.

⁷ Financial Times, Cargill warns goal of halting deforestation will be missed, [ft.com/content/a67df690-8def-11e9-a1c1-51bf8f989972](https://www.ft.com/content/a67df690-8def-11e9-a1c1-51bf8f989972) 13 June 2019

⁸ Global Witness, Money to Burn, <https://www.globalwitness.org/en/campaigns/forests/money-to-burn-how-iconic-banks-and-investors-fund-the-destruction-of-the-worlds-largest-rainforests/> September 2019, 23 September 2019

⁹ Euractiv, *EU-wide approach to due diligence needed to regulate cacao sector, manufacturers and NGOs say*, 2 December 2019

<https://www.euractiv.com/section/agriculture-food/news/eu-wide-approach-to-due-diligence-needed-to-regulate-cacao-sector-manufacturers-and-ngos-say/>

Global Witness et al, Protecting Forests, Ecosystems and Human Rights: a case for EU action, October 2019

https://www.fern.org/fileadmin/uploads/fern/Documents/2019/Briefing_-_Protecting_forests___human_rights_-_a_case_for_EU_action.pdf

¹⁰ OECD, Responsible Business Conduct for Institutional Investors: Key Considerations for Due Diligence under the OECD Guidelines for Multinational Enterprises

<https://mneguidelines.oecd.org/RBC-for-Institutional-Investors.pdf> , 2017

¹¹ Global Witness and ClientEarth, Strengthening Corporate Responsibility: the Case for Mandatory Due Diligence in the EU to Protect People and the Planet

<https://www.globalwitness.org/en/campaigns/forests/strengthening-corporate-responsibility/> , July 2019

¹² Ibid, July 2019

¹³ Global Witness commissioned Profundo to look into databases of loans, investments and other types of financing kept by Bloomberg, Thomson Reuters Eikon, Orbis and others, along with company reports and websites. This helped to build up a picture of how these companies finance their operations. It has been impossible to determine which specific ground-level activities this money financed - but found that such funding was critical to agribusinesses' expansion. Global Witness, Money to Burn

<https://www.globalwitness.org/en/campaigns/forests/money-to-burn-how-iconic-banks-and-investors-fund-the-destruction-of-the-worlds-largest-rainforests/> , September 2019

¹⁴ These six agribusinesses are JBS S.A., Marfrig Global, Minerva Foods, Halcyon Agri Corp, the Olam Group and Rimbunan Hijau Group.

¹⁵ The total figure includes the following EU member states: Spain, France, Netherlands, Germany, Italy, Cyprus, Sweden, Denmark, Belgium, and Finland.

¹⁶ Oxfam International, 'Consent is Everybody's Business: Why banks need to act on Free, Prior and Informed Consent'. August 2019.

<https://policy-practice.oxfam.org.uk/publications/consent-is-everybodys-business-why-banks-need-to-act-on-free-prior-and-informed-620854> p.25 Accessed 28 January 2020.

¹⁷ See 'Friends of the Earth v. Rabobank'.

https://complaints.oecdwatch.org/cases/Case_330 Accessed 28 January 2020.

Also see Office of the UN High Commissioner for Human Rights 'OHCHR response to request from BankTrack for advice regarding the application of the UN Guiding Principles on Business and Human Rights in the context of the banking sector'. 12 June 2017.

<https://www.ohchr.org/Documents/Issues/Business/InterpretationGuidingPrinciples.pdf>

Also, John Ruggie 'Comments on the Thun Group of Banks Discussion Paper on the Implications of

UN Guiding Principles 13 & 17 in Corporate and Investment Banking Context. 21 February 2017. https://www.ihrb.org/uploads/submissions/John_Ruggie_Comments_Thun_Banks_Feb_2017.pdf
See:
https://complaints.oecdwatch.org/cases/Case_543 Accessed 28 January 2020.

¹⁸ Dutch Banking Sector Agreement. 'DBA's analysis of severe human rights issues in the palm oil value chain and follow-up actions'. IMVO value chain working group report. August 2019. <https://www.imvoconvenanten.nl/-/media/imvo/files/banking/2019-palm-oil.pdf?la=en&hash=443DAB72E7CDF2E5F54B51820405C4CD> Accessed 28 January 2020.

¹⁹ Banking Environment Initiative (BEI) and Consumer Goods Forum (CGF)'s 'Soft Commodities' Compact <https://www.cisl.cam.ac.uk/business-action/sustainable-finance/banking-environment-initiative/programme/sustainable-agri-supply-chains/soft-commodities> Accessed 28 January 2020.

Roundtable on Sustainable Palm Oil. 'Members'. <https://rspo.org/members/all> Accessed 28 January 2020.

²⁰ Legifrance.gouv.fr, 2017. "LOI n° 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et des entreprises donneuses d'ordre." Accessed 22/1/20 at <https://www.legifrance.gouv.fr/affichTexte.do?cidTexte=JORFTEXT000034290626&categorieLien=id>

²¹ Oxfam. 'Cereal Secrets: The world's largest grain traders and global agriculture'. Oxfam Research Report. August 2012. https://www-cdn.oxfam.org/s3fs-public/file_attachments/rr-cereal-secrets-grain-traders-agriculture-30082012-en_4.pdf Accessed 28 January 2020.

²² European Commission action plan on financing sustainable growth https://ec.europa.eu/info/publications/180308-action-plan-sustainable-growth_en Accessed on 31 January 2020

²³ European Union, Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R2088&from=EN>

²⁴ Global Witness, EU's Regulation on Investor Disclosure on sustainability risks and due diligence <https://www.globalwitness.org/fr/campaigns/european-union-brussels-global-witness-eu/eu-investor-disclosure-regulation/>, December 2019

²⁵ Global Witness, <https://www.globalwitness.org/en-gb/campaigns/european-union-brussels-global-witness-eu/political-agreement-eu-taxonomy-welcome-first-step-stronger-action-needed-tackle-financing-climate-breakdown/>, 9 December 2019; and European Parliament approved text [https://www.europarl.europa.eu/RegData/committees/econ/inag/2020/01-16/CJ36_AG\(2020\)646809_EN.pdf](https://www.europarl.europa.eu/RegData/committees/econ/inag/2020/01-16/CJ36_AG(2020)646809_EN.pdf), 16 January 2020

²⁶ European Union, Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en, 22 October 2014

²⁷ Global Witness, Indecent Exposure <https://www.globalwitness.org/en/campaigns/land-deals/indecent-exposure/>, September 2018

²⁸ Intergovernmental Panel on Climate Change (IPCC), Global Warming of 1.5°C, Summary for Policymakers https://report.ipcc.ch/sr15/pdf/sr15_spm_final.pdf, 2018

²⁹ Fern, EIA, Greenpeace, WWF, YouGov Poll <https://www.fern.org/news-resources/press-release-87-per-cent-of-europeans-support-new-laws-to-combat-global-deforestation-new-poll-shows-1963/> 21 May 2019