

Methodology for 2022 baseline review of financial institution action on deforestation

What information is reviewed to create the baseline of financial institutions in Race to Zero and GFANZ?

About the project:

Global Canopy is conducting a baseline review of financial institutions in the Race to Zero and GFANZ as well as others that have signed significant climate commitments on their exposure to and existing action on deforestation and associated human rights. The 2022 baseline review will be followed by full assessments using the Forest 500 methodology in 2023.

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About Global Canopy:

Global Canopy is an innovative environmental organisation that targets the market forces destroying tropical forests. Since 2001, we have been testing new approaches to tackling deforestation, and guiding companies, investors and governments worldwide to think differently about our planet's forests. See: www.globalcanopy.org

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INTRODUCTION

This methodology is used to conduct a baseline review of the financial institutions which are members of Race to Zero and/or the Glasgow Financial Alliance for Net Zero (GFANZ), or have signed other significant climate commitments. In June 2022, Race to Zero updated their leadership criteria for membership in Race To Zero (which includes GFANZ), which for financial institutions included the addition of action on deforestation. This was in recognition of the fact that eliminating deforestation and conversion of natural ecosystems is essential in achieving net-zero.

Acknowledging that deforestation has recently been added to the Race to Zero leadership criteria, this year, Global Canopy will be conducting a baseline review of the financial institutions included in the Race to Zero, GFANZ and those that have signed other significant climate commitments on their exposure and existing policies and action on deforestation and associated human rights. The financial institutions will not yet have had time to act on the updated criteria so this review will assess pre-existing action, and will create a baseline for tracking future progress.

Ahead of COP 27, we will publish an independent baseline analysis with the results of this review, sharing high-level insights on the current state of action on deforestation for financial institutions in Race to Zero and GFANZ, as well as others that have signed significant climate commitments.

The 2022 baseline review will be followed by full assessments using the Forest 500 methodology in 2023. As well as creating a baseline, the 2022 review will allow us to identify and highlight examples of existing positive action and engagement.

The below indicators are used to conduct this review. Existing policies and actions will be reviewed for the financial institutions with regards to palm oil, soy, cattle products (beef and leather) and timber products (timber and pulp and paper).

The baseline review considers only information which has been made **publicly available** on the financial institutions' websites. In all cases, only sources published publicly by the financial institution itself are accepted. Wherever possible financial institutions are reviewed in their **native language** to allow for subjectivities in language.

THE BASELINE REVIEW

What data is reviewed for financial institutions in this sample to gather a baseline?

The baseline review is based only on publicly available information. Any information publicly available on the financial institution's websites during the review period, scheduled to run in August and September 2022, is considered within the baseline review.

What is the methodology based on?

This methodology is adapted from a sub-set of indicators from the 2022 Forest 500 financial institution methodology. In 2022 the Forest 500 financial institution methodology was aligned with the [Finance Sector Roadmap](#), which provides detailed guidance on the best practice approach for financial institutions working to eliminate deforestation, conversion, and associated human rights abuses from their portfolios by 2025. The Finance Sector Roadmap was aligned with and endorsed by the the Accountability Framework Initiative¹, which outlines the fundamental best practice for companies operating in forest-risk supply chains.

What is reviewed in the baseline?

Financial institutions are reviewed against 12 indicators. Indicators 1-3 are reviewed once per financial institution, the remaining indicators (4-12) are reviewed once for each of the four highest-forest risk commodities² (cattle products, soy, palm oil, timber products). In addition, we will look at the exposure of the financial institutions reviewed. There is no scoring associated with this baseline review.

At what level will the financial institutions be reviewed?

Global Canopy will be conducting the baseline reviews of the financial institutions at the level at which they joined the Race to Zero, GFANZ, or the other significant climate commitment. For some financial institutions that means that multiple subsidiaries of the parent institution will be included.

How are certification schemes considered?

Indicator 4 refers to the use of 'credible' certification schemes. Credible schemes are defined as multi-stakeholder certification schemes that include civil society in decision-making and exclude the production of commodities from intact forest landscapes, high conservation value areas, primary forests, tropical natural forests, or similar. Global schemes considered credible are FSC and PEFC (for timber and pulp and paper), RTRS (for soy), RSPO, MSPO and Rainforest Alliance (for palm oil)

¹ The Accountability Framework initiative (AFi) is a collaborative initiative to accelerate progress and improve accountability for ethical supply chains in agriculture and forestry. The Common Methodology is a methodology for assessment of company progress towards deforestation-free supply chains. to support common and aligned approaches to assessing corporate performance by buyers, investors, financial institutions, and civil society.

² These four commodities drive over two-thirds of tropical deforestation.

THE METHODOLOGY

Indicators 1 to 3 are reviewed once per financial institution, while indicators 4-12 are reviewed for each commodity.

INDICATOR NUMBER	INDICATOR
1	Does the financial institution have an overarching commitment to remove or reduce the amount of deforestation and/or conversion of all natural ecosystems caused by clients/holdings in their portfolio, or a clear statement of intent to tackle deforestation/conversion?
Guidance	<i>Overarching commitments must be financial institution-wide (i.e. must apply to all financing). Conversion-free is understood as no conversion of natural ecosystems anywhere (also referred to as zero/zero gross conversion), deforestation-free is understood as no loss of natural forests anywhere (also referred to as zero/zero gross deforestation), while zero net deforestation is understood as a commitment to offset forest loss through forest restoration.</i>
Answer options	Conversion-free commitment or a deforestation-free commitment that explicitly includes all other natural ecosystems
	Deforestation-free commitment
	Zero net deforestation commitment
	No overarching commitment
2	Does the financial institution recognise deforestation, conversion, and associated human rights abuses as a business risk?
Guidance	<i>The financial institution recognises that deforestation, conversion, and associated human rights abuses pose a risk to the financial institution itself. Business risk can be recognised in multiple ways, including but not limited to financial, operational, competition, or reputational risk. This risk can be identified using terms including 'risk', 'threat', and 'impact', as well as through language acknowledging the potential future impact of deforestation on the financial institution, including those suggesting that the financial institution is adapting its financing activities to respond to environmental issues caused by deforestation.</i>
Answer options	Yes

	No
3	Is the financial institution involved in any collaborative finance sector initiatives or advocacy for legislation focused on deforestation?
Guidance	<i>To be captured in this indicator, the financial institutions must be involved in advocacy for legislation focused on deforestation, conversion, and associated human rights, and/or be involved in a collaborative finance-sector initiative focused on these topics.</i>
Answer options	Yes, involved in a collaborative finance sector initiative focused on deforestation
	Yes, involved in advocacy for legislation focused on deforestation
	No
4	Does the financial institution have a commodity-specific policy or explicitly states that their overarching policy applies to specific commodity supply chains?
Guidance	<p><i>The financial institution must have a policy that applies to their financing of clients/holdings in these supply chains, which sets standards that the clients/holdings should meet in order to receive, or continue to receive financing. Policies under this indicator are classified under these categories to enable differentiation among financial institutions on the level of ambition of policies falling under this indicator.</i></p> <p><i>Policies are categorised based on their strength.</i></p> <p><i>If a financial institution has multiple policies under this indicator, only the strongest policy is included in the baseline review. The financial institution must state the specific commodity by name. General statements will not be considered for this indicator.</i></p>
Answer options	Zero-gross conversion: <i>policy that prevents clearing or conversion of any native vegetation, beyond just forests</i>
	Zero-net conversion
	Zero-gross deforestation
	Zero-net deforestation
	Protects priority forests (<i>Primary/natural/intact forests or high conservation value forests</i>)
	Credible certification scheme
	Protects globally important landscapes (including UNESCO World Heritage Sites, RAMSAR wetlands, IUCN category 1-4 areas, protected areas)

	Sustainability policy: <i>commitments to produce or procure 'sustainably' or 'responsibly' produced commodities, or commitment to certification that is not listed as credible under this methodology.</i>
	No policy
5	Does the financial institution require the clients/holdings to test for the Free, Prior and Informed Consent of indigenous peoples and local communities prior to acquiring new interests in land or resources and prior to new developments or expansions, not proceeding with these operations unless consent has been given?
Guidance	<i>Use of the term FPIC (Free, Prior, Informed Consent) in reference to Indigenous people and local communities is required. The policy should apply to the specific commodity policy, or to the overall sustainability policy for the forest-risk commodities or for general lending and investment criteria.</i> <i>Policies in place for funds or bonds cannot be considered for this indicator.</i>
Answer options	Required
	Encouraged
	No policy
6	Does the financial institution have a policy that requires clients/holdings to ensure their business operations and supply chains meet key labour standards?
Guidance	<i>Key labour standards include those laid out in the United Nations (UN) Declaration of Human Rights, UN Guiding Principles on Business and Human Rights, IFC Performance Standard 2 and the ILO core conventions: ILO Convention 87 on Freedom of Association and Protection of the Right to Organize, ILO Convention 98 on the Right to Organize and Collective Bargaining, ILO Convention 29 on Forced Labor, ILO Convention 105 on the Abolition of Forced Labor, ILO Convention 138 on Minimum Age (of Employment), ILO Convention 182 on the Worst Forms of Child Labor, ILO Convention 100 on Equal Remuneration, ILO Convention 111 on Discrimination (Employment and Occupation), UN Convention on the Rights of the Child, Article 32.1 UN Convention on the Protection of the Rights of all Migrant Workers and Members of their Families.</i> <i>Policies in place for funds or bonds cannot be considered for this indicator.</i>
Answer options	Clients/holdings' entire supply chain - Required
	Clients/holdings' entire supply chain – Encouraged
	Clients/holdings' own operations – Required
	Clients/holdings' own operations – Encouraged
	No policy

7	Does the financial institution require the clients/holdings to respect the customary rights of Indigenous peoples to lands, resources, and territories, and refrain from land acquisition or development until any existing land conflicts have been resolved?
Guidance	<i>The financial institution should require, or encourage, the clients/holdings in its financial portfolio to refrain from any new land acquisition or new developments until any existing or potential land conflicts have been resolved.</i> <i>Policies in place for funds or bonds cannot be considered for this indicator.</i>
Answer options	Required
	Encouraged
	No policy
8	Does the financial institution require the client/holding to have a zero tolerance approach to violence and threats against Forest, Land and Human Rights Defenders?
Guidance	<i>In line with the Zero Tolerance Initiative, financial institutions should require clients/holdings to adopt a zero tolerance approach to violence and threats against Forest, Land and Human Rights Defenders.</i> <i>Policies in place for funds or bonds cannot be considered for this indicator.</i>
Answer options	Required
	Encouraged
	No policy
9	Does the financial institution apply the policy to all of their operations and financial services provided, or are there some exclusions?
Guidance	<i>Policies should apply to all financing, otherwise 'No' is recorded for this indicator. This can include policies which only apply to subsidiaries of the financial institution, certain types of financing (e.g. corporate lending, project finance, asset management, advisory services), financial deals regardless of value, and clients/holdings are certain stages of the supply chains.</i> <i>This indicator is assessed once for each indicator 4-8 for each commodity.</i>
Answer options	All financing
	No
10	Does the financial institution have a clear public process to identify policy non-compliant clients/holdings?
Guidance	<i>This indicator focuses on whether a financial institution has internal procedures to assess and monitor existing financial relationships with clients/holdings against their sustainability policies. Financial institutions can either specify details of a screening and monitoring process, or ad-hoc/less than annual audits.</i>

	<i>Financial institutions must have a deforestation policy in indicator 2.1 to be reviewed for this indicator.</i>
Answer options	Screening and monitoring process
	Ad-hoc audits
	No
11	Does the financial institution have a clear public process to engage with clients/holdings to manage non-compliance?
Guidance	<p><i>The financial institution should have a clear public process detailing how they will engage with clients/holdings in their financial portfolios who have been found to be non-compliant with either the financial institution's deforestation policy (indicator 2.1) or their own time-bound plan.</i></p> <p><i>The review will look at whether the financial institutions either engages with non-compliant clients/holdings with a clearly stated risk of redirecting finance within a set time-frame if progress is not made, or engages with non-compliant clients/holdings without a time-bound threat of redirecting finance.</i></p> <p><i>Financial institutions must have a deforestation policy in indicator 2.1 to be reviewed for this indicator.</i></p>
Answer options	Engage with non-compliant companies, with a time-bound threat of redirection of finance
	Engage with non-compliant companies, without a time-bound threat of redirection of finance
	No
12	Does the financial institution annually report the number or proportion of portfolio clients/holdings to which this policy applies, proportion which are compliant with their time-bound plans/in compliance with the financial institution's policy, and the number of companies/clients which have been engaged on deforestation-risk?
Guidance	<p><i>The financial institution should report progress against its policy. For example, how many clients/holdings assessed as part of their due diligence are classified as high/low risk or how many clients/holdings have been engaged on deforestation risks. This can be included in ESG reporting as long as the proportion compliant with the commodity or deforestation policy can be ascertained.</i></p> <p><i>Reporting must be from the last two reporting periods, either in 2020/2021, or 2021/2022. Financial institutions must report the following:</i></p> <ul style="list-style-type: none"> • <i>The number/proportion of portfolio clients/holdings covered by the deforestation policy</i> • <i>The number/proportion/outcome of portfolio clients/holdings which have been engaged with on deforestation-risk or compliance with the policy/time-bound plans</i> • <i>The number/proportion of portfolio clients/holdings compliant with the deforestation policy or their own timebound plans</i>

	<i>Financial institutions must have a deforestation policy in indicator 2.1 to be reviewed for this indicator.</i>
Answer options	Reports all three criteria
	Reports two criteria
	Reports one criteria
	No reporting



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