CDP EUROPE'S COMMENT ON THE EUROPEAN COMMISSION'S ROADMAP AGAINST DEFORESTATION AND FOREST DEGRADATION

Reducing the impact of products placed on the EU market

Background

CDP welcomes the European Commission's initiative aiming at minimising the EU's contribution to deforestation and forest degradation worldwide and promoting the consumption of products from deforestation-free supply chains in the EU, assessing and taking into account regulatory and non-regulatory policy options.

The single largest cause of deforestation and forests degradation globally is commercial agriculture. The production of agricultural commodities on which the CDP Forests questionnaire is focused, such as palm oil, beef, soy, timber, and pulp and paper, drives around 70% of tropical deforestation (2000–2010)[1]. Moreover, large-scale commercial agriculture accounts for about 40% of deforestation in the tropics and subtropics[2]. The supply-demand of key forest risk commodities also accounts for 10-15% of greenhouse gas emissions.

If tropical deforestation were a country, it would rank as the third largest emitter of greenhouse gases (GHGs). With the world´s forests containing more carbon than oil, gas and coal deposits, healthy forests play a critical role in combating climate change. Moreover, intact forests are vital as natural carbon sinks. Up to one third of the annual carbon mitigation needed to limit the temperature increase could be achieved by addressing deforestation and forest degradation.

CDP's disclosure process incentivizes companies to measure, manage and reduce their impacts on the environment throughout their entire supply chains. We track key performance indicators such as board level oversight, risk assessment, and corporate governance as well as implementation measures including certification, traceability and supplier engagement to provide critical data to investor shareholders and purchasing organizations and to highlight how companies are progressing in their efforts to halt deforestation. Despite the benefits disclosure offers, reporting on forests is still poor. **In 2019, 70% of more than 1.800 companies requested to provide this information to investors, shareholders or purchasing organizations failed to do so.** This lack of transparency should be of equal concern to consumers, who trust that known brands are acting to implement publicly made commitments yet have little access to information to assess their progress. Especially after it

[1] https://www.unenvironment.org/explore-topics/forests/why-do-forests-matter
[2] http://www.fao.org/publications/sofo/2016/en/

has been made clear that the 2020 commitments to banish deforestation from the supply chains will not be met by many of the major companies around the world[3].

With transparency being the basis for effective accountability, CDP provides a disclosure system where comparable data on the negative and positive impacts of companies on global forests as well the impact of global deforestation on these companies is collected and used by investors and policymaking to take better informed decisions. This is underpinned by the most frequently reported risks for companies when it comes to forests – which are reputational and market risks (50%). It is the type of risk reported by the largest number of companies (74%), which is not surprising, as most impacts associated with deforestation to date have been from reputational damage and more than half of all detrimental impacts (67%) experienced by disclosing companies were the result of reputational drivers. Other companies are willing to lead the way, with 98 companies reporting business opportunities valued at US$33.1 billion, half of which (48%) are highly likely or virtually certain to transpire, covering areas like increased brand value, improved climate change adaptation or driving demand for sustainable materials.

These figures show, that **the EU needs to set clear regulation and legally binding agreements to halt deforestation and forest degradation**, as companies may not comply with the needed ambition to meet the global climate goals voluntarily.

EU legal framework

CDP urges the European Commission to present an ambitious EU Action Plan against deforestation and forest degradation. Our input focusses on three areas of CDP expertise and insight.

Corporate disclosure and action

Strengthening the corporate reporting framework by specifying disclosure and due diligence requirements of corporates on deforestation, forests degradation risk and land-use change throughout their entire supply chains, notably considering the ongoing revision of the Non-Financial Reporting Directive.

Sustainable Finance

Integrating and specifying deforestation risk assessment in policy measures targeting investors and banks, notably considering the legislative and non-legislative measures of the EU Action Plan on Financing Sustainable Growth. CDP has provided concrete guidance on how companies, investors, local and national governments can use CDP's disclosure system to implement, and go beyond, the regulatory requirements of the Action Plan[4].

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[3] https://www.theguardian.com/environment/2020/jan/17/biggest-food-brands-failing-goals-to-banish-palm-oil-deforestation

[4] https://6fefcbb86e61af1b2fc4-c70d8ead6ced550b4d987d7c03fcdd1d.ssl.cf3.rackcdn.com/cms/reports/documents/000/004/725/original/CDP_and_the_EU_Action_Plan_on_Sustainable_Finance_spreads.pdf?1570438792

Public and private procurement

Encouraging better management of forest-related impacts by suppliers and act as a driver of positive action to halt deforestation in supply chains; and embed zero-deforestation criteria into procurement rules, notably into the planned legislation on green public procurement[5]

CDP data and insight

1. Corporate disclosure and action in 2019

Companies reported through CDP that typically, 15% of revenue is dependent on commodities driving deforestation.

Despite this revenue dependency and although deforestation is a main contributor to greenhouse gas emissions and driving climate change, a third (35%) of companies do not include forest-related issues in their risk assessment. But a great majority (81%) of organizations that conduct risk assessments, identify substantial risks, reporting up to US$48.2 billion in potential losses due to the impacts of deforestation in 2019. As over half of companies reporting risks (58%) did not report the potential financial impact, the figure is likely to be much greater.

Analysis of data reported through CDP in 2019 reveals that 126 European companies responded through CDP's forests questionnaire, looking at risks associated with key forest commodities. This included 92 responses on timber, 32 on cattle, 46 on palm oil, 32 on soy, and 11 on rubber. Only a small number of companies report on the risks and opportunities related to labelling and due diligence processes. However, last year a group of big corporations and NGOs have asked the European Commission for implementing mandatory reporting and due diligence processes to minimise the negative characteristics associated with cocoa production, including deforestation[6].

In 2019, 14 European companies also reported through CDP that greater enforcement of regulations would be a key measure that would improve their ability to manage deforestation risks. Other corporate responses suggested that increased transparency through increased regulation would address a key barrier to avoiding deforestation-risks, that there is a lack of proper labelling for deforestation-free commodities, or that due to the tight competition in the market some suppliers do not want to disclose detailed information on their sources unless there are specific legal requirements. Moreover, companies mention that more cooperation between regulatory authorities on the EU Timber Regulation is needed and they would like to

[5] https://ec.europa.eu/commission/presscorner/detail/en/speech_20_139
[6] https://www.voicenetwork.eu/wp-content/uploads/2019/12/Joint-position-paper-on-the-EUs-policy-and-regulatory-approach-to-cocoa.pdf

see the European Commission's Communication on stepping up action on deforestation translated into urgent concrete action.

Conclusions for Corporates:

- A record number of companies disclosed to CDP's Forests questionnaire in 2019. While these companies have taken an important first step in their journey towards managing deforestation risks, most will need to significantly accelerate their efforts to match the progress they are making on climate change, and to a lesser extent on water security.
- CDP's Forests A List 2019 features just eight companies this year, an increase of only one from 2018. However, six of these companies are European, showing again leadership from businesses in the region. In part, the Forests A List is smaller because the disclosure process for forests is much less established than for climate change, with fewer total respondents. However, this doesn't fully account for the discrepancy.

2. Sustainable finance

In 2019, over 500 investors and financial institutions, managing US$96 trillion in assets, put their names to the CDP Forests Disclosure Request. This figure has risen from 380 in 2017, and just 31 when the first information request was sent out in 2010.

Engagement with the issue has never been greater. A growing number of financial institutions have introduced policies that cover their investment in or lending to companies involved in forest-risk commodity supply chains. Rabobank's sustainability policy, for example, commits the Dutch bank to "strive to achieving zero net deforestation by preferably not engaging in transactions that are directly linked to deforestation activities". Some of these institutions are taking concrete action to remove deforestation risk from their portfolios. Many are engaging with companies to encourage them to improve their practices, often in behind-closed-door meetings.

Some are going further, choosing to decline investment to, or to divest from, companies that are causing or contributing to deforestation. In some cases, these decisions are made public. In its latest responsible investment report, Norges Bank Investment Management, which manages around US$1 trillion for Norway's Government Pension Fund Global, reported divestment from one soy and three palm oil companies, based on the long-term environmental and social risks they pose. Equally, investors are working collaboratively to encourage higher standards within commodity supply chains. Ninety-one institutions, managing US$6.7 trillion in assets, in mid-2018 called on the Roundtable for Sustainable Palm Oil (RSPO) to strengthen draft revisions to its sustainable palm oil standards. In November, the RSPO adopted strengthened standards.

Service providers are offering products that help investors avoid deforestation-related risks. Exchange operator Euronext has launched an equity index, the Euronext® CDP Environment France EW Decrement 5%, which includes the 40 France-listed companies which score highest based on their CDP disclosures, including on deforestation risks.

Financial institutions are also offering products to help channel finance towards sustainable forestry management and commodity production. For example, BNP Paribas has structured a

US$95 million sustainability bond on behalf of the Tropical Landscapes Financing Facility. The proceeds will help fund a sustainable natural rubber plantation on heavily degraded land in Indonesia, in a joint venture between tire maker Michelin of France and Indonesian conglomerate Barito Pacific Group.

Governments can use existing tools such as Climetrics, the first independent fund rating that provides a holistic assessment of a fund's climate-related risks and opportunities, covering a fund universe of over 15.000 funds and used by institutional and retail investors. The underlying methodology uses portfolio companies' performance across three interrelated themes: reducing GHG emissions, managing water resources and tackling deforestation

Conclusions for Investors:

- As a first step, seek to understand the extent and nature of their exposures to deforestation risk. CDP forests data offers essential insights in this regard.
- Explore the potential of investing in opportunities in deforestation-free commodity supply chains. These might include sustainable landscape bonds, green bonds or impact funds that target sustainable agriculture and forestry.
- Provide support for companies that invest in measures that will improve their ability to manage risks, particularly at the landscape and jurisdiction levels, through providing sustainable loans, project finance and equity.

3. Public and private procurement

Activities causing deforestation and forest degradation can often be hidden in complex supply chains, which is why it is important that public and private buyers engage with their suppliers. On one hand, major corporations have for decades outsourced their environmental impact to other companies - and often countries - in their value chain. But with supply chain emissions 5.5 times more than a company's direct operations, these large corporations are a powerful lever in the transition to a sustainable economy.

On the other hand, public procurement accounts for about 14% of European GDP, and public authorities' buying can play a key role in positive environmental action by driving suppliers to combat deforestation. And as the EU is responsible for 10% of worldwide deforestation associated with the production of goods or services between 1990 and 2008, it has the responsibility to step up the action in protecting and restoring the world's forests.

The projected rise in demand for agricultural products will increase the pressure on natural resources and further strain the remaining forests. However, companies responding to the CDP are not taking enough urgent action. Almost a quarter of the companies responding to CDP have yet to begin taking action to remove deforestation from respective commodities in their supply chains. But supply chains also need to be better managed. Nearly 30% of suppliers to companies that report to CDP have yet to begin removing deforestation from the products they sell.

Furthermore, there is a gap between upstream and downstream companies taking measures. For example, large-scale agribusinesses dominate zero-deforestation initiatives. However, CDP data shows that commitments to deforestation do not cascade down the supply chain as expected, with about one-third of all reporting companies not yet supporting their suppliers, such as local communities or smallholders, in this transition. In addition, there is a substantial gap in 2020 commitments made by companies closest to production and those that control land. Only 16% of these companies have a 2020 forest commitment in place, compared to 86% of companies with no control over land.

To improve the sustainability and resilience of their business, companies can become a CDP supply chain member and ask their suppliers to disclose through CDP's Supply Chain Program. The program began with just 19 members, largely from the retail and consumer goods sectors and headquartered in the USA and Europe. Today it brings together a diverse group of 125 major purchasing organizations from around the world, with an enormous US$3.2 trillion in combined procurement spend – an amount greater than the annual GDP of the United Kingdom[7].

There is huge power in this scale of procurement spend. But with great power comes great responsibility. And over the past 10 years we have seen a fundamental shift in expectations around business action on climate change and other environmental sustainability issues. The program launched in 2008, a time when many governments were acting far too slowly to address climate change; a fact emphasized by the disappointing final outcome from the landmark Copenhagen climate talks in 2009. Partly as a result of this, subnational actors – particularly large corporates, but also some large public sector organizations – have started to play an increasingly important role driving climate action internationally. In many cases they are moving considerably faster and further than governments have required.

However, European companies in agricultural commodity supply chains must be encouraged to disclose their impact and to establish and meet clear commitments to accelerate progress in deforestation-free supply chains. Although four-fifths (80%) of the responding companies have set quantitative targets related to increasing sustainable production or consumption of certain forest commodities, only 70% have come close to meeting the targets for third party certification, 56% have achieved the traceability targets and 38% have come close to meeting sustainable procurement standards.

Where regulations have not pushed companies to act in many parts of the world, clear signals from major purchasers have made a real difference. And as the consensus on the need to act has developed, coalescing around major campaign groups such as the We Mean Business coalition, with involvement from some the most significant players in the global economy. And this commitment to a sustainable, low carbon economic transition has helped to bolster international support for political change, helping secure the signing of the Paris Agreement in 2015.

[7] https://www.cdp.net/en/research/global-reports/global-supply-chain-report-2019

Within the CDP Supply Chain programme there are several government members who want to leverage the power of public procurement to drive action on climate change:

- Los Angeles Department of Water and Power
- California Department of General Services
- U.S. General Services Administration (GSA)
- Ministry of the Environment, Government of Japan

With consumer country governments turning their attention to commodity supply chains the needed action to protect the world's forest can be accelerated. Governments of seven European countries[8] – Denmark, France, Germany, Italy, the Netherlands, Norway and the United Kingdom – have signed the Amsterdam Declaration 'Towards Eliminating Deforestation from Agricultural Commodity Chains with European Countries'. It commits signatories to "support and help meet the private sector goal of eliminating deforestation from the production of agricultural commodities such as beef and leather, palm oil, paper and pulp, soy and other commodities such as cocoa and rubber by no later than 2020[9]." It specifically recognizes the role of the private sector in eliminating deforestation from global supply chains[10].

Conclusion for Public and Private Procurers:

- Encourage better management of forest-related impacts by suppliers of public and private procurement organizations and act as a driver of positive action to halt deforestation in supply chains.
- Embed sustainability criteria into procurement rules; Public authorities can use their purchasing power to influence suppliers to adopt more sustainable practices relating to their forest impact.

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For further information please contact CDP Europe's policy team

Nadya Dedikova
Public Affairs Officer
+32 2 880 04 43
nadya.dedikova@cdp.net

CDP Europe
EU Transparency Register No.: 050269010212-72
c/o Finance Watch
Rue Ducale 67 b3, 1000 Brussels, Belgium

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[8] https://mfvm.dk/fileadmin/user_upload/MFVM/Miljoe/Letter_to_European_Commissioners_on_Deforestation.pdf
[9] Dutch Ministry of Foreign Affairs (2017), Amsterdam Declaration 'Towards Eliminating Deforestation from Agricultural Commodity Chains with European Countries'.
[10] CDP (2018), Analysing European Public and Private Actions to Tackle Imported Deforestation