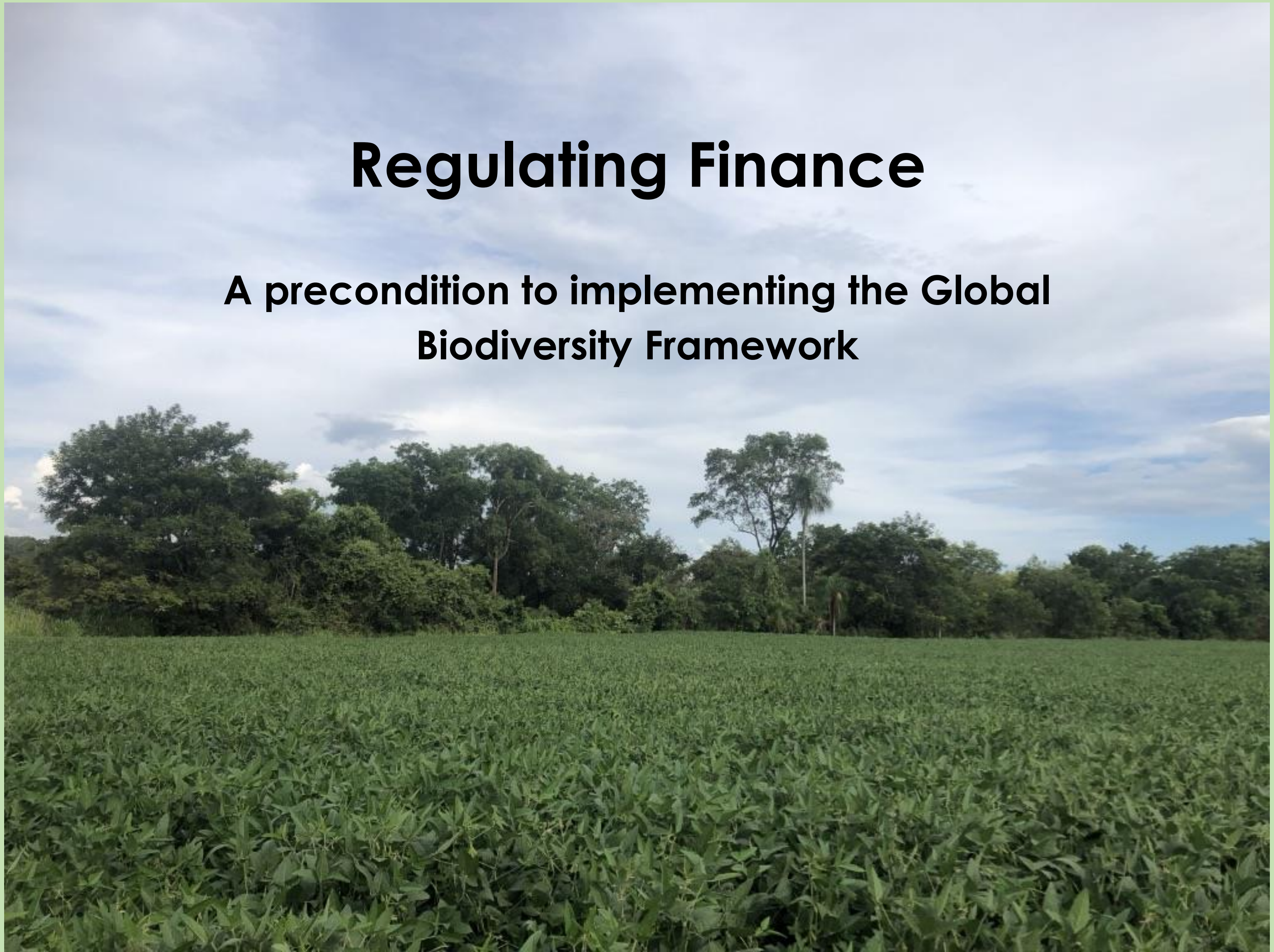
Regulating Finance

And the need to move beyond "mainstreaming"


Mainstreaming = Integrating Biodiversity into Business as Usual
Alignment = Adapting Business as Usual to the Scientific and Social Requirements of Biodiversity

New briefing paper highlights need to regulate finance and shy away from voluntary approaches



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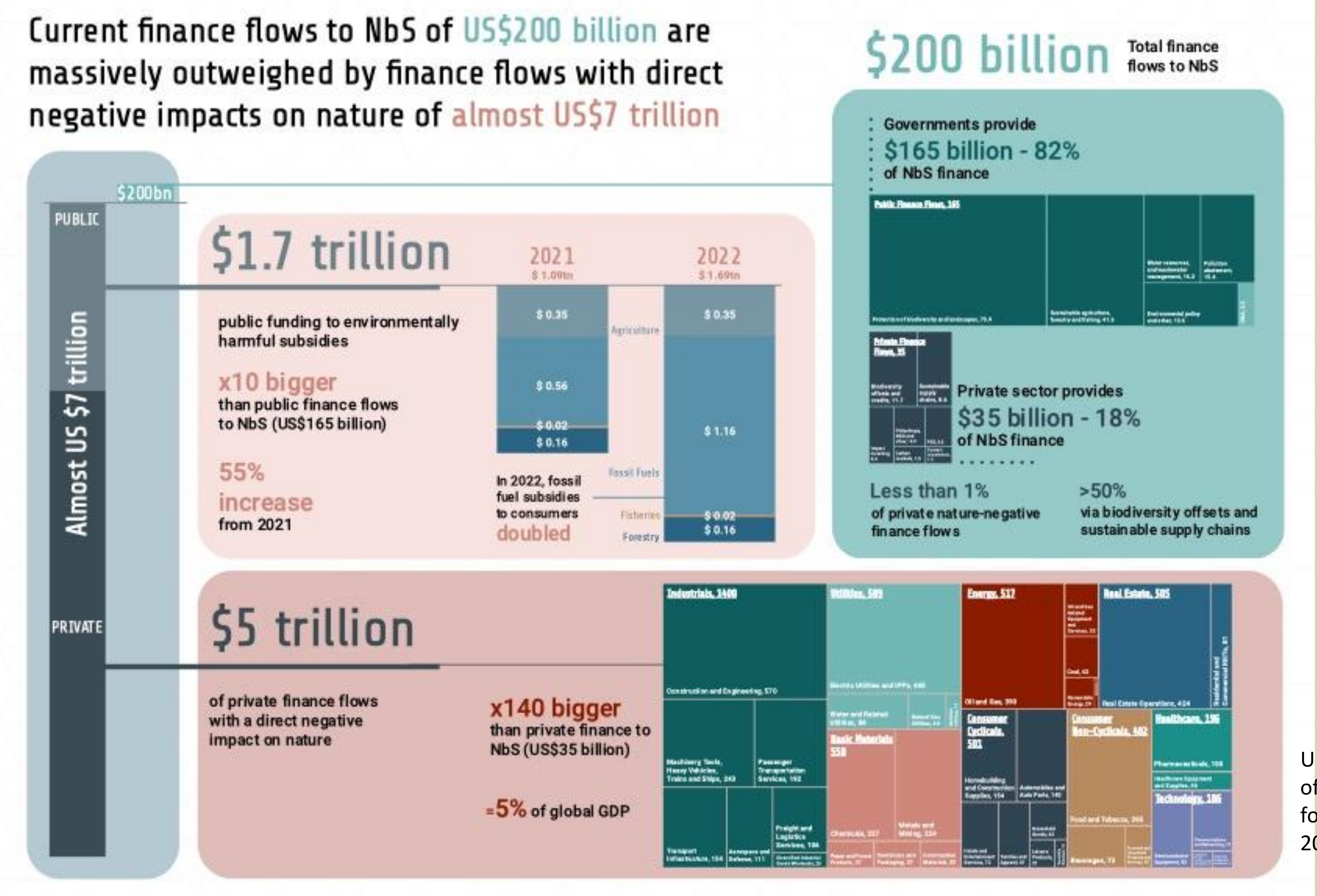


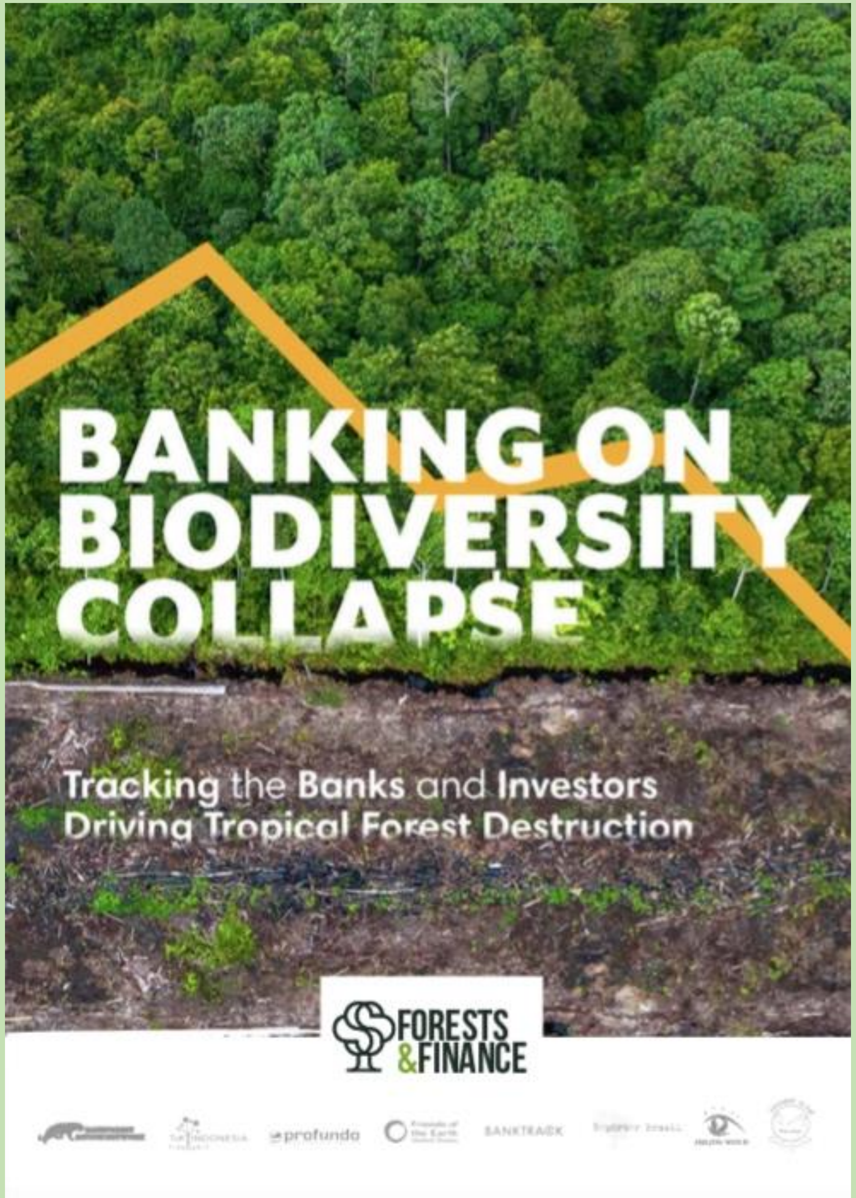
UNEP, State of Finance for Nature, 2023

In the GBF and its resource mobilization strategy, Governments commited:

- To progressively align all financial flows with the GBF (GBF Target 14)
- To take legal, administrative or policy measures to ensure that financial institutions transparently disclose their impacts on biodiversity ... in order to progressively reduce negative impacts (GBF target 15)
- To identify and eliminate subsidies and other perverse incentives that might trigger biodiversity loss (GBF target 18)
- To update their National Biodiversity Strategies and Action Plans (NBSAPs) before the 16th Conference of the Parties in October 2024 so as to align them with these and other GBF targets – this means concrete commitments that will realistically lead to the achievement of these targets by 2030 should be incorporated.

Without regulating private finance, the GBF cannot and will not be implemented

- The 2023 Banking on Biodiversity Collapse report revealed that at least $307 billion in credit had been directed to the main tropical forest-risk sectors from 2016 to September 2023.
- The March 2024 Bankrolling Ecosystem Destruction report estimated that over 1 trillion USD in global credit went to major corporate groups involved in so-called ecosystem risk sectors, including agricultural commodities associated with deforestation risks; sectors using large inputs of such commodities to produce animal feed; sectors consuming large quantities of this feed; and timber and wood pulp, since 2015.
- The Deforestation Dividends report concluded that between 2016 and 2020, financial institutions earned 1.54 billion USD in revenue from a portfolio of 20 deforestation-risk agro-industrial companies.
- The Banking on Climate Chaos report shows that 60 of the world's largest banks poured over USD 6.9 trillion into the fossil fuel industry over the past 8 years, driving climate chaos, biodiversity loss and deadly local community impacts.



Corporate-led, Voluntary Approaches: Recipes for Failure that Undermine the GBF

- Taskforce on Nature-related Finance Disclosures (TNFD) provides voluntary reporting guidelines whereas GBF target 15 calls for addressing impacts.
- It mainly requires disclosure of information that is financially “material", which means risks will only be reported if they might impact on the financial interests of -potential- investors in the company - unless national laws require otherwise.
- A 2021 World Bank report highlighted that low and middle low income countries will suffer 10 to 15 times larger economic impacts from biodiversity loss than high income countries. Indigenous Peoples, women, and local communities that depend on biodiversity for their livelihoods are the first to suffer from biodiversity loss.
- The wealthy companies causing the harm are often the last to suffer from the impacts of the damage they cause.
- TNFD also allows investors to determine freely which data they want to disclose and through which methodology such data are gathered, which virtually ensures that these data will not be consistent, comparable or even independently verifiable.
- TNFD does not oblige companies to disclose where they are operating or buying from, which makes it impossible for local communities, or local or national authorities to verify whether a certain company or bank is linked to the biodiversity loss in their area.
- Companies are not even obliged to report if they are facing serious complaints over biodiversity destruction or human rights violations.

Other corporate-led voluntary schemes have proven to be ineffective as well

- An analysis of the forest-risk policies of more than 100 financial institutions concluded that despite some marginal improvements since 2016 "vague language, unclear timeframes, and other loopholes persisted, leading to continued facilitation of human rights violations and deforestation." (BOBC, 2023)
- the "Soft Commodities Compact" revealed an overall failure to reach its targets. The 12 banks that signed up to this compact actually increased their investments in forest-risk companies during the 6-year duration of the compact and they were not even able to comply with the commitment that all their clients were to join voluntary sustainability certification schemes.
- Analysis found critical gaps in the Roundtable on Sustainable Palm Oil certification scheme
- The Forest Stewardship Council has been found to have had "minimal impact on tropical deforestation" in general,
- Independent audits of the Round Table on Responsible Soy concluded that certified companies "show a failure to achieve any social or environmental benefit".

A legally binding Convention requires legally binding regulations and commitments at the national level.

Some initial steps are being taken:

- The French Duty of Vigilance Law requires that large multinational corporations, including financial institutions, operating in France establish a plan covering all their international activities that "includes reasonable due diligence measures to identify risks and prevent serious violations of human rights and fundamental freedoms, the health and safety of people and the environment, resulting from the activities of the company and those of the companies it controls." Most critically, it also allows communities to seek remedy for harms.
- The EU has introduced mandatory sustainability reporting for certain undertakings, including banks and insurance companies from 2025 onwards.

Other non yet legally binding or incomplete but hopefully soon to be strengthened initiatives include:

- China has adopted Green Finance Guidelines for the Banking and Insurance Industries, which instruct banks and insurance companies to strictly restrict financing industries that face significant environmental and social risks. It is hoped the key provisions will be incorporated in the revised Chinese Law on Commercial Banking.
- The Government of Brazil has decided to exclude industrial livestock activities from its sustainable sovereign bonds
- Malaysia already adopted a Value-based Intermediation Financing and Investment Impact Assessment Framework in November 2019.
- In 2022 Indonesia introduced a Green Taxonomy to expedite financing for sustainable sectors.
- The EU is currently reviewing its Corporate Sustainability Due Diligence Directive to possibly include a wider scope of activities including finance
- The European Commission is preparing an impact assessment on the need to provide for specific legal obligations for financial institutions under the EU Regulation on Deforestation-free Products so that EU banks and other investors will no longer be able to invest in forest-risk commodities (that will subsequently be banned from entering the EU market).

Identification and redirection of the most perverse incentives by 2025 is a lithmus test whether countries are taking the GBF seriously

For example, annually:

- The EU provides more than 6 billion Euro in biomass subsidies
- The UK provides 1.5 billion USD in biomass subsidies
- South Korea provides 400 million in biomass subsidies

Despite a rapidly growing body of evidence that wood-based bioenergy does not only cause more greenhouse gas emissions that coal, but also is a key driver of deforestation, forest degradation and biodiversity loss in general, including through replacement of natural ecosystems by monoculture wood plantations

Recommendations

- Establish strong **legally binding social and environmental standards** that financial institutions must comply with.
- Require **strong due diligence** by financial institutions for all their financial services including across client company groups
- Require financial institutions to have contract and client **on-boarding requirements** on biodiversity and human rights risks, including repercussions for non-compliance
- Require financial institutions to **disclose** the name of the project and company (or company group) they are financing, including financial intermediaries, their full impacts on biodiversity with methods that allow data to be publicly and independently verified, and scrutinized and complaints they face about their biodiversity and human rights impacts
- Require financial institutions to adopt **holistic transition plans**, with clear metrics and targets, that address biodiversity, climate and social impacts with a systemic approach;
- Clearly **establish the responsibility** of financial institutions for their contribution to adverse impacts through financing or investing in companies that cause harms
- Establish mechanisms **to hold financial institutions accountable** for the adverse impacts they have caused or contributed to in their financing and investment.

Only by moving beyond mainstreaming and putting in place the national regulatory framework that ensures alignment of all public and private financial flows with the GBF, and genuine incentive reform, resources can be mobilized to implement the GBF.

Moreover, we need to redirect incentives to support a genuinely gender-just, rights-based and equitable transition to sustainable livelihoods that are in harmony with nature

For more information see: www.forestandfinance.org