

The BEI & CGF's 'Soft Commodities' Compact: TECHNICAL GUIDANCE

as of December 2015

Introducing this Technical Guidance

This Technical Guidance has been developed by the BEI Compact Banks, convened and co-ordinated by the University of Cambridge Institute for Sustainability Leadership (CISL).

By adopting the BEI's 'Soft Commodities' Compact ('the Compact'), developed in partnership with the Consumer Goods Forum (CGF), Compact Banks pledge to help the CGF achieve zero net deforestation by 2020. The Compact is not intended to be prescriptive, but rather to lead the banking industry in developing market norms that align bank practice with the CGF's resolution on deforestation.

Individual Compact Banks are therefore expected to make their own decisions on if and how to incorporate the Compact's commitments into their own business practice. This is both pragmatic (because banks that adopt the Compact will offer different products and services, in different markets and have different internal procedures) and necessary from a Competition Law point of view.

Equally, the Compact is not intended to limit a bank's approach to supporting the CGF goal of zero net deforestation by 2020; all banks are free to go further, faster in line with their own business strategy and context.

The intended audience for this Technical Guidance includes Compact Banks themselves, banks that are considering adopting the Compact as well as other key stakeholders. It is a '**living document**' and will be updated periodically.

Key Terms

Some Key Terms in the Compact can be further clarified with reference to the details of the CGF's procurement guidelines. These are highlighted below. Where the CGF's procurement guidelines do not yield further clarity, Compact Banks are urged to make their own decisions on how to incorporate the Compact's commitments into their practices and communicate these accordingly.

It is noted that multi-stakeholder initiatives at a national level designed to support the implementation of the CGF's resolution offer a helpful opportunity for more specific 'National Interpretations' of the Compact to be defined.

In accordance with Competition Law, as with all of the BEI's activities, Compact Banks will undertake their own decisions on the manner in which this Technical Guidance will be embedded in within their own businesses.

‘Zero net deforestation’

The BEI follows the CGF’s explanation of ‘zero net deforestation’, itself derived from [WWF’s guidance](#):

- ‘Zero net deforestation’ can be distinguished from ‘zero deforestation’, which means no deforestation anywhere.
- ‘Zero net deforestation’ acknowledges that some forest loss could be offset by forest restoration. ‘Zero net deforestation’ is not synonymous with a total prohibition on forest clearing. Rather, it leaves room for change in the configuration of the land-use mosaic, provided the net quantity, quality and carbon density of forests is maintained. It recognises that, in some circumstances, conversion of forests in one site may contribute to the sustainable development and conservation of the wider landscape (eg reducing livestock grazing in a protected area may require conversion of forest areas in the buffer zone to provide farmland to local communities).
- However, ‘zero net deforestation’ is not achieved through the conversion of primary or natural forests into fast growing plantations. Such conversion would count as deforestation in assessing progress against the target.

Approaches to implementing a ‘zero net deforestation’ policy should prioritise avoiding the conversion of forests with a High Conservation Value (HCV)¹ or that are considered to be High Carbon Stocks (HCS)².

‘Corporate and investment banking customers’

- This term is intended to refer to commercial enterprises which make use of any of a bank’s corporate or investment banking services.
- It is not the intention of the BEI to prescribe parameters for the size of commercial enterprises that Compact Banks consider to be in scope. Rather, just as CGF companies are urged to conduct their own materiality assessments in determining the applicability of the CGF resolution to their own supply chains, Compact Banks are urged to consider this threshold explicitly when setting their own processes and procedures and make clear their approach in their public communications.

‘Significant’

- It is not the intention of the BEI to prescribe how individual banks should judge whether or not a customer’s operations include ‘significant’ production or processing of palm oil, timber products or soy in markets at high risk of tropical deforestation. Rather, just as CGF companies are urged to conduct their own materiality assessments in determining the applicability of the CGF resolution to their own supply chains, Compact Banks are urged to consider this key term explicitly when setting their own processes and procedures and make clear their approach in their public communications.

¹ Please see <http://www.hcvnetwork.org/> for a working definition of HCV

² While efforts to agree one methodology, with multi-stakeholder backing, for identifying HCS forests continue, this is aspirational. As an example, please see <http://www.greenpeace.org/international/global/international/briefings/forests/2013/HCS-Briefing-2013.pdf> for a working definition of HCS

- Best practice approaches include:
 - Conducting materiality assessments with key stakeholders; and/or
 - Establishing ‘no go’ criteria such as illegality, conversion of forests with a High Conservation Value or that are considered High Carbon Stocks or violation of the rights of workers or local people; and/or
 - Setting thresholds according to company size, which in turn may vary according to markets of operation.

‘High risk of tropical deforestation’

- This term is intended to refer to a risk-based approach to ensuring that the greatest attention is paid to those parts of the world where the production of palm oil, timber products and soy is most closely associated with deforestation.
- The CGF has published the following commodity-specific guidance for identifying high risk geographies, based on a combination of the presence of tropical forests, risk of commodity-driven deforestation, presence of HCV areas and input from producers, civil society and other experts. The CGF keeps these views under regular review and its current published set of high priority geographies can be accessed via its Sustainable Commodity Procurement Guidelines [here](#).
 - Oil palm plantations are almost always in the same areas as humid tropical forests, so all production regions are considered high priority.
 - Countries where production of timber products should be *verified* for low risk of contributing to deforestation include Indonesia, Malaysia, China, Thailand and Colombia while countries where production processes should be *monitored* for potential contribution to deforestation include Myanmar, Vietnam, Papua New Guinea, Cambodia, Democratic Republic of Congo, Cameroon and Ghana.
 - Forests, savannah, and grasslands (which can be a High Carbon Stock) in South America are currently at greatest risk from soy production. The primary focus for CGF members is therefore the Amazon, the Cerrado, the Atlantic Forest, the Gran Chaco, and the Chiquitano.

Role of certification standards

- As the Compact notes, there is a range of mechanisms available to banks that allows them, increasingly, to reduce the likelihood that they are financing the production or processing of palm oil, timber products and soy that contributes to deforestation and they are in a constant state of evolution and improvement.
- The certification standards identified in the Compact are those that were initially identified by the CGF and BEI as the minimum means of verification in assessing whether a company is at low risk of contributing to net deforestation and are therefore seen as sufficient means of verification that a company is aligned with the goal of zero net deforestation.
- Working with a range of expert stakeholders, the CGF has assessed that other means of verification are already equivalent to these standards in terms of operational strength and environmental and social integrity. Further commodity-specific details are found [here](#).

- Equally, the CGF has recognised that some groups have developed criteria and indicators for third-party verification of practices that go beyond existing certification standards. Examples include RSPO Next and the Palm Oil Innovation Group (POIG).
- These will be monitored for applicability as they achieve both critical mass and greater commercial traction.
- Individual Compact Banks are urged to make clear the minimum requirements they have of their customers in their public communications of their own positions on the Compact.

Implementation Guidance

The following guidance is offered to support implementation by individual Compact Banks of the section of the Compact that relates to ‘Raising Industry-wide Banking Standards’. It is noted that there will be a need for individual Compact Banks to prioritise their actions according to their own business contexts. A step-wise approach is therefore suggested. Individual bank action will vary depending on the internal policies and procedures that have already been established by a given bank.

1. Set and communicate the bank’s own approach to supporting the Soft Commodities Compact

The BEI recommends that banks consider incorporating the following into the details that they publish:

- The nature of the bank’s exposure to each relevant soft commodity, e.g. types of banking service and/or markets where exposure is the greatest, subject to commercial restrictions.
- The bank’s interpretation of key terms central to the Compact’s scope.
- Details of minimum requirements the bank has set for customers in relevant soft commodity sectors, including key dates or timeframes.
- The bank’s approach to non-compliance with its policies.
- The bank’s intentions with respect to reporting on its progress in implementing its policy, including frequency of reporting (e.g. annually), approach to disaggregated disclosure of customer performance (subject to their consent) and role of independent verification.
- The bank’s products which it has deployed that are intended to support the transformation of businesses in relevant soft commodity supply chains away from driving deforestation. Such reporting should make clear the intended impact and the rationale for how that impact will be achieved (noting that impact reporting itself can be much more complex) and the take-up rate (including as a proportion of relevant portfolios).

2. Confirm that the bank’s customers have a time-bound plan to achieve compliance with the bank’s approach to supporting the Soft Commodities Compact by 2020

- In order to maximise consistency, customers should be encouraged to make their plans transparent and public so that all banks are working off the same information, which can be independently verified.

- Where a bank is requiring third-party certification to verify compliance and membership of the certifying body requires members to have time-bound plans in place for all of their operations (e.g. RSPO), membership of certification bodies may be used as a proxy to help achieve this confirmation.
- If the certifying body does not have such requirements in place (e.g. FSC), direct engagement may be required to achieve this confirmation.
- When looking at their customers' collective performance, Compact Banks should choose the most appropriate metric according to their own business model. For instance, some banks may choose to base their calculations on the absolute number of customers with a time-bound plan, as a percentage of the bank's total number of customers in each relevant soft commodity supply chain. Others may choose to focus on their total credit exposure to customers with a time-bound plan, as a percentage of their total credit exposure to relevant soft commodity supply chains.
- It is recommended that banks accompany communications of such figures with narrative reporting to explain their approach to customers that do not have a time-bound plan.

3. Confirm that the bank's customers' production or processing operations are compliant with the bank's approach to supporting the Soft Commodities Compact

- In order to maximise consistency, customers should be encouraged to make this information transparent and public so that all banks can work off a standard dataset and have their calculations independently verified as appropriate, rather than assembling data themselves through their client relationship channels.
- Some certification bodies are already putting in place systems to facilitate this level of transparency and the metric used varies both on the position of a company in a commodity supply chain and on the type of commodity supply chain itself:
 - For instance, as part of their Annual Communication on Progress (ACOP), palm oil producers that are RSPO members are required to report the total acreage of their landbank and the total acreage that is certified already; mill owners are required to report the total number of mills they own and the total number that are certified. Banks are recommended to follow this lead.
- Systems like this can be developed by a range of actors, not just certification bodies. If they are robust, independently verified and fully utilised, they offer banks a standardised and transparent means by which to calculate aggregate figures. For example, a bank can calculate the total acreage of all of its palm oil producer customers' production operations and then report the total acreage that is certified as a percentage. Where such systems do not already exist, Compact Banks may wish to work together and with other relevant stakeholders to establish them.

Key Performance Indicators (KPIs)

The following guidance offers Key Performance Indicators (KPIs) for Compact Banks to help them to inform their stakeholders on the progress of their implementation of the section of the Soft Commodities Compact that relates to 'Raising Industry-wide Banking Standards'. They are intended to be useful and practical based on in-depth

consultation with banks and a range of other stakeholders. However, they will continue to be subject to modification based on the implementation experience of Compact Banks.

CISL will collate links to the information that Compact Banks disclose on the BEI website so that the BEI's stakeholders can access such information more easily, but the BEI will not prescribe a standardised reporting format.

KPI 1: Bank has published details of its approach to supporting the Soft Commodities Compact

KPI 2: Percentage of the bank's customers in each relevant soft commodity supply chain with all of their operations covered by a time-bound plan to achieve compliance with the bank's approach to supporting the Soft Commodities Compact by 2020

KPI 3: Percentage of the bank's customers' production or processing operations in each relevant soft commodity supply chain that have been verified as being compliant with the bank's approach to supporting the Soft Commodities Compact

KPIs 2 and 3 will have most value when they are tracked and reported over time, as this will go some way to demonstrating the positive impact of the bank's policies and engagement with its customers.

If the nature of a bank's business is such that it does not develop relationships with customers beyond one-off transactions, or if a bank's approach to supporting the Soft Commodities Compact is sufficiently mature that it considers itself to already be fully compliant, it may consider reporting on the number of relationships or transactions that it has terminated or refused in each relevant supply chain in a given period due to non-compliance with the bank's approach to supporting the Soft Commodities Compact. This is not the sort of positive impact that the BEI aspires to promote, but in such circumstances it can nevertheless be an indicator of the existence of a bank's approach to supporting the Soft Commodities Compact. Such reporting should include narrative reporting to contextualise the numbers reported in relation to the bank's overall exposure and to explain the nature of non-compliance and actions taken to try to address it. It should be noted that if a bank does not report on this metric, it should not be interpreted as a lack of action on its part.

Additional BEI Progress Indicators

Over and above individual Compact Bank KPIs, the BEI will integrate the following indicators of progress into the ongoing public communication of its efforts to deepen the impact of the Soft Commodities Compact, but will not consider them as Key Performance Indicators in their own right:

a) Compact Banks' combined market share

To ensure consistency and ease of verification, the BEI will track Compact Banks' combined market share. This figure will necessarily only give an approximate indication of the significance of the Compact Banks with respect to the financing of the production and processing of particular soft commodities.

b) BEI activities to reinforce market norms in line with the goal of zero net deforestation by 2020

The BEI foresees at least four means by which the Soft Commodities Compact can serve to reinforce market norms in line with the goal of zero net deforestation by 2020 and intends to communicate its goals and activities under these four headings:

- a) Strengthening the leadership of existing Compact Banks
- b) Growing the group of banks that choose to adopt the Soft Commodities Compact
- c) Improving the 'means of verification' available to banks to verify their customers' alignment with the zero net deforestation goal
- d) Supporting the development of new financing solutions that support the transformation of businesses in relevant soft commodity supply chains away from driving deforestation

Governance

It is not the intention either of the BEI as a leadership group of banks, or of CISL as host of the Secretariat for the group, to police or audit individual Compact Bank's progress towards the Compact's goal of aligning banking services with the CGF resolution to help achieve zero net deforestation by 2020. Indeed, efforts to increase transparency around progress Compact Banks are making to implement the Compact are intended to signal Compact Banks' willingness to work with all of their own relevant stakeholders to improve their individual performance.

However, if a Compact Bank is not felt to be working in support of the BEI's mission (either through lack of participation, insufficient support of the BEI's objectives, or promoting views inimical to its mission), the Chair of the BEI, supported by CISL, will seek to resolve the issue through constructive dialogue. If this is not successful, reference to the bank's adoption of the Compact will be removed from BEI communications with the agreement of at least two thirds of BEI members.