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Comments on mineral auditing

Based on my experience from 1997-99 and again 2003-6 managing the tantalum raw material procurement activities for Cabot Corporation, a publicly traded US corporation with stock traded on the New York Stock Exchange, I believe the proposed regulatory guidelines offered to the SEC by the Enough Project represent a readily achievable standard for SEC-regulated corporations. The following notes offer some details on the metals processing industries for those metals covered by Dodd-Frank and support, from an industry insider's perspective, for the practicality of the Enough project proposals.

1. Smelters and ore processing

The metals identified in the Finance Bill, tungsten, tin, tantalum and gold (3TG), are typically found in ores either as metal particles or as metal compounds (oxides being the most common form, for example tin oxide). The ores are processed at the smelters to extract the economically valuable metal from the ore, with the residue disposed of as waste.

Ore processing to recover the economically valuable metal from its host ore is a chemical process. The two most common techniques are:

(a) True smelting, in which the ore is mixed with other materials (for example coal) and heated, to separate the metal from the ore. Tin is recovered in this manner, as is some tantalum and some gold;

(b) Acid based chemical processing, in which the ore is dissolved in acid and the desired metals then separated from the resulting liquid. Tungsten, most tantalum, and many gold ores are processed in this manner.

In either case, it is important for the processors ("smelters") to understand the chemical composition of the ore. Trace elements in the ore, other than the economically important metals, can have a significant impact of the cost and efficiency of the smelter's operation. So, when ores are purchased, the buyer always requires the ore to have been sampled in advance of a purchase by a credible,

independent third party assaying company. This assay information then forms a part of the sale and purchase negotiation, and will be evaluated in every case by the buyer prior to any purchase agreement being reached.

2. Identifying potential conflict ores

In most mining operations, some processing of the mined ore takes place at the mine site, to remove waste material and increase the value of the ore to be sold to buyers. This is the case at large integrated mines and also in many artisanal mining operations such as in the Congo. So, it can be challenging to trace an ore back to a specific mine unless the mine is large and well characterised in its geology. Such characterisation occurs only in large mining operations with the financial resources to conduct the necessary work.

Nevertheless, the ore produced by artisanal miners still reflects to some degree the geology of the region where it was produced. For example, the term "coltan" is short for columbo-tantalite, and is generally applied to ores from the conflict regions of the Congo and to some Burundian and Rwandese ores that are of course produced in areas directly adjacent to the Congo. The term arises from the fact that ores in this part of Africa typically (though not always) contain comparable amounts of tantalum and niobium (also known as columbium, hence the term coltan).

Ore smelters necessarily have a good understanding of where their ores originate. This is partly because of the characteristic qualities of ores from specific parts of the world, but also from:

- knowledge of which trading companies are active in which parts of the world
- knowledge of the production capacities of the various ore producing regions
- knowledge of global import/export trade data
- and general industry knowledge (customer communications, equipment purchases, press releases, and so on)

So, identifying suspicious material is straightforward for participants in these metal markets at the smelter level. For example, the emergence in recent years of Dubai and Uganda as major sources of gold production, according to official statistics, may be interesting to the casual observer but, to those in these industries, is a clear signal that material is being smuggled from elsewhere and relabeled. The same story is true of an upsurge in tantalum production from Rwanda, again indicating smuggling from the Congo.

3. Auditing suppliers

The main consumers of 3TG metals include the electronics, aerospace and automotive industries. In each of these industries, OEMs and their suppliers have developed extensive and highly detailed information systems designed to enable quality problems to be traced quickly and efficiently to their root causes. These

quality systems are pervasive and extend back through supply chains to the smelters. Such tracing is necessary since the functionality provided by smelters in the form of the metal products they produce is frequently critical to end user product quality.

So, the systems needed to trace supplies of 3TG products back to smelters already exist. These data systems are data rich and can be interrogated through a computer terminal, hence the data needed for audits of 3TG products can be found quickly and at low cost. Putting in place a robust audit process does not require lengthy preparation, nor does it create an undue burden on suppliers.

4. Industry wide approaches

The electronics industry, through the Electronics Industry Citizenship Coalition (EICC) and Global e-Sustainability Initiative (GeSI) organisations, has designed and is implementing an audit process designed to audit all 3TG smelters, with a target completion date of 2011. The audit process further streamlines the compliance process for SEC-regulated firms because:

(a) By creating a robust common process, small firms can participate immediately as they can ride on the coat-tails of industry leaders;

(b) By inviting other industries to make use of the audit results, the electronics industry is helping other industries benefit from the highly developed quality systems within the electronics supply chain; and

(c) By creating a single audit for each smelter, repeated annually, the burden on smelters is kept to a manageable level and the incentives for smelters to participate are increased, expanding the scope and value of the programme.

The EICC and GeSI organisations have committed to publishing the results of their audits. So, firms affected by the legislation and accompanying SEC regulation need simply to trace their 3TG supplies back to their smelter suppliers, and then compare with the results of the EICC/GeSI audits. Provided these audits are properly conducted, all SEC-regulated firms should be able easily, and by their first reporting period required by law, to understand and disclose the extent to which they are using conflict minerals.

5. The importance of audit disclosure

The human rights catastrophe in the Congo caught the attention of major consumers of 3TG metals in the early 2000s. The initial industry response was for OEMs to ask suppliers to self-certify that they were not using conflict minerals. The failure of self certification over the last decade is beyond dispute, and clearly some firms were either unwilling to look at their ore supplies, or else were deliberately dishonest, when they furnished customers with certification letters. The only way to prevent

such dishonesty is to insist on a transparent, independently audited process, and the SEC's regulations can only meet the requirements of law if they demand transparency.

So, while in my view the EICC/GeSI audit process is a robust process, it will only be effective as a tool to support the goals of Dodd-Frank is the SEC insists upon clear public statements by firms regulated by the SEC of their audit process and a comprehensive listing of all their 3TG smelters.

6. The value of the OECD guidelines

While the US is taking a leadership role in addressing the exploitation of 3TG conflict minerals, other regions of the world are also developing regulations and legislation. The OECD guidelines, having been developed by a multi-stakeholder group including substantial input from corporations, are both an effective framework and the basis for an efficient set of regulations. The main industries consuming 3TG metals are global, and creating regulations at significant variance to OECD guidelines is likely to create additional administrative burdens for companies, with a disproportionate weight on smaller firms that are less able to comply with multiple disclosure requirements. For the benefit of all SEC-regulated firms, and more particularly to help manage the compliance load on smaller companies, the SEC would do well to follow the OECD guidelines in formalising its regulations on conflict minerals.