NATIONAL ASSOCIATION OF Manufacturers

July 26, 2011

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File Number S7-40-10

Dear Ms. Murphy:

Attached is a concept paper explaining the views of the National Association of Manufacturers regarding a phase-in period of the Conflict Minerals rule. Please ensure that copies of this paper are received by the appropriate individuals in the SEC.

Thank you.

Sincerely,

Franklin J. Vargo

National Association of Manufacturers
Conflict Minerals Phase-in Concept
June 24, 2011

Introduction

Several government officials have asked what would occur during a phase-in of the Conflict Minerals Rule. The National Association of Manufacturers' members have consistently stated that companies would begin reporting to the SEC in accordance with the schedule in the legislation. All issuers subject to the law would provide the required disclosure of their use of conflict minerals the first full year the regulation is in effect and would report on due diligence actions as required.

However, because complex supply chains do not have traceability of conflict minerals built in, the NAM believes that a phase-in of the disclosure is warranted. We believe a phase-in is not prohibited by the law and would result in a practical, effective, and pragmatic implementation of the rule. It would also recognize that the needed reporting and information infrastructure on the ground in the Democratic Republic of the Congo and capacity to provide fully validated supply chains for affected minerals does not yet exist. In fact, the Department of State Conflict Minerals Map has not been kept up to date, which makes it practically impossible for issuers to comply in a meaningful way with the proposed rule. The OECD has recognized that:

> "Internal control mechanisms based on tracing minerals in a company's possession are generally unfeasible after smelting, with refined metals entering the consumer market as small parts of various components in end products. By virtue of these practical difficulties, downstream companies should establish internal controls over their immediate suppliers and may coordinate efforts through industry-wide initiatives to build leverage over sub-suppliers, overcome practical challenges and effectively discharge the due diligence recommendations contained in this Guidance."

Without flexibility, there is a very real danger that issuers may simply prohibit sourcing from the region entirely. This would not only defeat the goals of the legislation but it would significantly undermine the United States' and the entire international community's diplomatic efforts in the region.

It is important to understand the complexity of a modern supply chain in order to understand why a phase-in is critical to achieve the intent of the legislation and for companies to be able to reasonably comply with it. Supply chains are made up of layers known as tiers. At the top of the chain is the manufacturer of or party contracting to manufacture the final product. These top tier parties will generally have privity of contract only with Tier 1 suppliers. Tier 1 suppliers will have their own suppliers (Tier 2 suppliers) and so on. Supply chains can often be many Tiers deep. Manufacturers and those contracting to manufacture will generally be able to exercise control only over Tier 1 suppliers, with whom they are in privity of contract which experience shows diminishes substantially as one moves further down the supply chain to the raw materials producers.[1] Moreover, even with respect to Tier 1 suppliers, manufacturers will

[1] Thus, for example, the United Kingdom Ministry of Justice *Guidance* interpreting the UK Bribery Act of 2010 acknowledges: "Where a supply chain involves several entities or a project is to be performed by a prime contractor with a series of subcontractors, an organization is likely only to exercise control over its

only be able to negotiate new conditions and commitments as existing contracts or other agreements are renewed or new ones are entered into. In addition, many of the companies in Tiers could be small businesses and/or non-public companies located anywhere in the world (with the communication and cultural issues that go with that fact) without the infrastructure, resources, and capability to meaningfully comply. Many of these companies are not familiar with SEC reporting or the penalties carried for non-compliant filers.

Tracing minerals through the supply chain back to origin will be very challenging. The supply chain from mining to final product could follow the path as shown below for a metallic catalyst.

1. Mining
2. Negociant
3. Comptoir
4. Trader
5. Ore beneficiation (concentration of ore constituents by physical separation processes)
6. Smelting (extraction of metal from ore via multiple chemical reactions)
7. Refining (purification of crude metal)
8. Metal (tin or gold) is sold to company A, which makes the metallic catalyst
9. Catalyst is sold to Company B, which uses it to manufacture a polymeric coating (note that catalyst is not incorporated into the polymer chain, but is reclaimed for future use)
10. Company C purchases the coating and uses it to coat a part
11. Part is sold to Company D, which uses it to make a larger part
12. Larger part is sold to Company E, which uses it to make an assembly
13. Assembly is sold to Company F, an auto company, which uses it in manufacturing a car

Because of the complexity of the supply chain and the lack of reliable information about the source of these minerals[2], in the phase-in period we envision that companies would develop internal compliance programs, due diligence procedures and reasonable inquiry approaches perhaps drawing from common industry approaches to conflict minerals due diligence, adapted appropriately to company- and industry-sector circumstances.

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relationship with its contractual counterparty…The principal way in which commercial organizations may decide to approach bribery risks which arise as a result of a supply chain is by employing the types of anti-bribery procedures referred to elsewhere in this guidance (e.g., risk-based due diligence and the use of anti-bribery terms and conditions) in the relationship with their contractual counterparty, and by requesting that counterparty to adopt a similar approach with the next party in the chain." *Id.* at 16 (March 2011).

[2] The Electronic Industry Citizenship Coalition and the Global e-Sustainability Initiative, the leading industry and non-governmental organizations working on supply chain due diligence for conflict minerals, have only just completed the first list of "conflict free smelters" and it represents tantalum smelters only; lists covering smelters processing tin, tungsten, and gold are planned for later this year. See: http://eicc.info/documents/PR%20Extractives%20CFS%20Tantalum%20List%20FINAL.pdf

Possible Phase-in Approach

A rational and reasonable phase-in could be structured in the following manner:

First Year:

- Adopt and clearly communicate to first-tier suppliers the company policy or similar corporate statement or industry position for the supply chain of the minerals originating from conflict-affected and high-risk areas. The policy or similar corporate statement should incorporate the standards against which due diligence is to be conducted, consistent with appropriate standards and/or common industry approaches, adapted appropriately to company and industry sector circumstances. (Examples of company efforts underway to inform their suppliers can be provided.) Companies should:

- Publish the policy or similar corporate statement or industry position on the use of conflict minerals on the corporate website.

- Implement a process to identify whether tin, tantalum, tungsten or gold are used in company products or processes.

- Where practicable, begin the process to develop a chain of custody or a traceability system for purchased tin, tantalum, tungsten and gold by contacting first-tier suppliers. This process of establishing a chain of custody or traceability system may be implemented through participation in industry-driven programs (including smelter certification processes), national or international standards organizations, and/or through contract flow-down provisions or other written commitments.

Year Two:

- Strengthen company engagement with suppliers. A supply chain policy or similar corporate statement should be incorporated into contracts, purchase orders, and/or other means/agreements with first-tier suppliers, as contracts or other agreements are entered into or renewed. As part of this, ask first-tier suppliers to 1) push the new policies upstream to their suppliers, and 2) adopt contract provisions, purchase orders, specifications or use other means to encourage their suppliers to transmit information downstream from smelters/refiners.

- As practicable, follow up with first-tier suppliers that have not responded to requests for information. Conduct the reasonable country of origin inquiry, and due diligence based on the results of that reasonable country of origin inquiry.

- Assess risks of adverse impacts in light of the standards of the supply chain policy or similar corporate statement.

- Obtain reasonably reliable representations from processing facilities or first-tier suppliers.

- Publish the results of these efforts on the corporate website.

Year Three:

- Devise and adopt a risk management plan, including a description of policies and procedures to address non-conformance with the policy or similar corporate statement.

- As required, obtain independent third party audits of the Conflict Minerals report if directly sourcing from the DRC or adjoining countries.

- Implement a risk-based program that uses company control processes or common industry approaches to evaluate information provided by first-tier suppliers.

- In addition, as reflected in NAM comments, as infrastructure and capacity to trace mine source becomes operational for specific minerals, manufacturers will trace and report the origin of the conflict minerals more consistently and reliably.

The proposed phase-in schedule is consistent with the statutory requirements. All issuers will be held accountable for the information they provide to the SEC. If they knowingly or willfully provide false information, the issuer would be subject to SEC penalties. Our phase-in proposal is also consistent with the requirements of the law. Sec. 1502 (b) requires companies:

> "to disclose annually whether conflict minerals that are necessary… did originate in the Democratic Republic of the Congo…and in cases in which such conflict minerals did originate [to] submit to the Commissioner a report..."

Such language only requires and creates an affirmative obligation to disclose and submit a conflict minerals report if the issuer knows that the minerals in its products originated in the DRC or adjoining countries. If the issuer does not have actual knowledge that the minerals originated from the DRC, the authorizing statute creates no further obligation for the issuer.

This position is further supported by the legislative history of Sec. 1502 of the Dodd-Frank Act. During the conference on the Dodd-Frank Act, the Senate offered changes to the House of Representatives Offer on Section 1502 dated June 23, 2010 (attached as addendum A to our comments) which specifically amended the Section 1502 and "clarified that only companies that source from the DRC and adjoining countries need to file anything with the SEC" by removing "or did not" from the statutory language. This change created an affirmative obligation only if the minerals in an issuer's product(s) originated in the DRC or adjoining countries. "Did not" was purposefully removed by the Senate to narrowly tailor the disclosure and reporting requirements to apply to only issuers who have actual knowledge that the minerals in their products originated from the DRC or adjoining countries.

This approach to disclosure is appropriate given the varying levels of capacity and infrastructure available for each mineral/metal to provide data on origin. Gold, in particular, needs substantially more time and study to determine how to trace the origin and provide transparency. According to experts working on the bagging and tagging schemes and smelter validations, once a scheme is operational it takes, at a minimum, nine months for the issuers to receive information from suppliers on the origin. The proposed phased-in approach is based on this information.

Manufacturers subject to the new requirements place a high value on corporate compliance. Providing false information and knowingly misleading the SEC will have significant

negative repercussions for issuers and subject them to penalties under the law. Checks exist to prevent a company from failing to make reasonable inquiries to determine if conflict minerals originated in the DRC or adjoining countries. Given today's regulatory environment, the threat of an SEC enforcement action as well as the other potential penalties is a strong deterrent to companies that do not comply with the requirements.