March 17, 2017

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: **Acting Chairman Piwowar's January 31, 2017 Statement on the Commission's Conflict Minerals Rule**

Dear Mr. Fields:

The Corporate Governance Coalition for Investor Value (the "Coalition") was formed in 2015 to provide a forum for the discussion of issues of common interest among its members to advocate for strong corporate governance policies and federal securities laws that promote long-term value creation for investors and the firms in which they invest. Coalition members represent American businesses of all sizes, from every industry sector and geographic region. These businesses produce the goods and services that drive the American economy, employing and creating opportunities for millions of Americans and serving the countless communities nationwide in which the Coalition believes that strong corporate governance policies are important to provide investors with a return on investment and businesses with the capital needed to grow and operate. The Coalition welcomes the opportunity to comment on the final rules issued by the Securities and Exchange Commission (the "SEC" or "Commission") under section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), concerning so-called conflict minerals.

The Coalition and its member companies believe that the decades-old human rights crisis in the Congo ("Congo" or the "DRC") needs to be resolved. However, we fundamentally believe that the disclosure mechanism envisioned by section 1502 is a tragically misguided approach that, according to a growing body of evidence, has very possibly made the crisis in the DRC worse, not better. The conflict minerals rule

has also imposed a significant burden upon the shareholders in public companies and contributed to the phenomenon of "information overload" at a time when there is broad agreement that SEC disclosures need to be modernized for the 21st Century. A major portion of the conflict minerals rule (which forced companies to disclose whether or not their products were "conflict-free") was also struck down by the courts as a violation of the First Amendment. Given these developments we believe that at a minimum, the Commission should consider the following modifications to the implementation of the rule:

- Form an interagency working group with the State Department to monitor the complex, technical, humanitarian, diplomatic, and geopolitical issues impacted by the rule.

- Provide that a reporting company is only subject to the rule to the extent it exercises a significant level of direct control over the manufacturing of its products.

- Implement safe harbor and *de minimis* standards.

- Provide a more definite statement that scrap and recycled sources are out of scope.

- Simplify required reporting on Form SD.

Discussion

The ostensible goal of section 1502 was to bring peace and stability to the Congo by cutting off the source of funding to violent militia groups and to provide public company investors with decision-useful information. Regrettably, section 1502 has failed to provide public company investors with information that is material to their decision-making and has directly led to a multitude of unintended and damaging consequences for the people of the Congo. It has also frustrated local efforts in the DRC to implement due diligence programs and increase transparency. These outcomes are consistent with the repeated warnings by Congolese experts about the dangers of the conflict minerals campaign, which was largely spearheaded by Western

activists with relatively little input from people who live and work every day in the DRC.

Impact of the Conflict Minerals Rule on the DRC and Surrounding Region

Instead of fostering benign transparency for the global supply chain, the conflict minerals rule has in fact created a de facto embargo on minerals sourced from the impacted region—an embargo that has not discriminated between "good" mines and "bad" mines. By incentivizing international buyers to purchase their minerals elsewhere, the rule has negatively impacted the livelihood of millions within the region. In an open letter to President Obama and then-SEC Chairman Mary Schapiro, 50 religious, civil society, and business letters in South Kivu Province, DRC wrote:

> We write to you in our capacity as representatives of the people of South Kivu Province in the Democratic Republic of Congo, in the hopes that you may be able to alleviate the unintended economic crisis that has befallen our people as a result of the recent passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act…
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> As you know, our country is already among the poorest in the world…in this environment; artisanal mining has emerged as one of our only economic lifelines, and has directly and indirectly provided millions of jobs. The abrupt cessation of this trade has devastating impacts on our people: 1. Millions of our artisanal miners have suddenly had their livelihood cut from under them. (Many of them continue to mine; finding small-scale buyers who are either buying on speculation or smuggling abroad, but at less than a half of what they were making before.) They find it increasingly difficult to pay school, health, or maternity fees. Some even report having difficulty providing food for their families. 2. …The world'[s] sudden refusal to buy these minerals means that the planes no longer service these [remote mining] communities; with nothing to trade, they are unable to provide themselves with such basic necessities as salt, sugar, oil, cloths, soap and so on. 3. Because artisanal mining was one of our only engines of economic growth, secondary economic impacts are being felt throughout the province. Even in our large towns, economic activity has

> diminished; construction slowed; trade in everything fallen. People with very little to begin with are now dealing with less." [1]

At the same time that the Congo and many of the bordering countries covered by section 1502 are experiencing substantial hardship due to decreased demand for minerals, they are bearing significant direct costs to comply with due diligence requirements. For example, in testimony before the U.S. House Committee on Financial Services, Subcommittee on Monetary Policy and Trade, then-Minister of State in charge of Mining with the Ministry of Natural Resources Government of the Republic of Rwanda stated that during the 2014-2015 fiscal year, the "the Ministry of Natural Resources – which has several departments beyond mining – had a budget of $19.8 million…[and] approximately $6.1 million was spent to comply with the diligence requirements…and still, because of Section 1502, our minerals were effectively excluded from the market.[2]

Moreover, the U.S. Government Accountability Office ("GAO") has reported that U.S. efforts have "failed to translate into significant improvements in security in 2015 in eastern DRC."[3] According to local stakeholders:

> Had these unfortunate consequences at least resulted in a significant reduction in the conflicts here, they might have proven worthwhile. But minerals are only one of numerous elements propelling these conflicts, and we have seen no reduction in the toll our people suffer from them. If anything, the law has forced the mineral trade further underground, complicating the various initiatives we and others have undertaken to increase its transparency.[4]

The GAO report also noted that "[t]he UN…reported that armed groups continue to generate significant revenue from the control, taxation, or looting of all of

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[1] Open Letter to President Obama and SEC Chairman Schapiro, from 50 religious, civil society and business leaders in South Kivu Province, DRC. (July 5, 2011) ("DRC Open Letter"). https://www.sec.gov/comments/s7-40-10/s74010-324.pdf. A list of signatories is provided on pages 4-6.

[2] Evode Imena, Minister of State In charge of Mining, Ministry of Natural Resource Government of the Republic of Rwanda, Testimony before the U.S. House Committee on Financial Services, Subcommittee on Monetary Policy and Trade, Dodd-Frank Five Years Later: What Have We Learned From Conflict Minerals Reporting?, at 8 (Nov. 17, 2015). Underscoring political instability in the region, former Minister Imena was recently arrested and faces official corruption charges. *See* Ivan R. Mugisha, Rwanda's Ex-Mining Minster Held for Nepotism, the East African (Jan. 30, 2017).

[3] GAO 2016 Report, *supra* note 1, at 1.

[4] DRC Open Letter, *supra* note 10.

the 'conflict minerals'—gold, tin, tantalum, and tungsten—despite the expansion of traceability and due diligence efforts to more mining sites in the DRC."[5] Other militias have responded by simply turning to different businesses in order to fund their activities. In other words, while the conflict minerals rule has caused immeasurable harm to innocent people, it has not in any meaningful way inhibited the ability of certain groups to perpetuate violence. According to the Pole Institute, a local research-based institute:

> The rise of the M23, but also other groups such as Raia Mutomboki and the large array of new Mai Mai militias, coincides with the downturn in mining in the Kivus – which itself is an unintended, but logical consequence of the new policies on Congolese mining being driven by international concern about ["]conflict minerals[."] Mining is not at the root of these new armed activities. It is the absence of mining that fuels conflict: by depriving the region of foreign earnings, by removing economic opportunities, by driving young people to seek a living through violence instead, by exacerbating competition between local stakeholders over ever scarcer revenues.[6]

The Washington Post also ran a front page story in 2014 that laid bare the devastating impact that the conflict minerals rule has had. The *Post* story, for example, included a story about a fourteen-year-old boy who joined a militia when his father could no longer make enough money from the tin mine where he was working. The article stated that "[the boy's] path to war involved not just the wrenching poverty and violence of eastern Congo but also an obscure measure passed by American lawmakers."[7]

Impact of the Conflict Minerals Rule on Public Companies and their Shareholders

In addition to the humanitarian impact of the conflict minerals rule, the mandated disclosure has failed to provide material information to investors. Even after conducting costly and burdensome due diligence efforts, most companies are

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[5] GAO 2016 Report, *supra* note 1, at 1.
[6] Dominic Johnson, Senior Analyst, Pole Institute, NO KIVU, NO CONFLICT? The misguided struggle against "conflict minerals" in the DRC, 9 (Apr. 2013).
[7] Sudarsan Raghavan, How a well-intentioned U.S. law left Congolese miners jobless, The Washington Post (Nov. 30, 2014).

still unable to determine the source of the conflict minerals in their products and whether the conflict minerals financed armed groups in the Congo. According to the GAO, "after an estimated 79 percent of the companies that filed a Form SD performed due diligence, an estimated 67 percent of them reported they were unable to confirm the source of the conflict minerals in their products, and about 97 percent of them reported that they could not determine whether the conflict minerals financed or benefited armed groups in the [DRC] and adjoining countries."[8] In fact, only a "small percentage—an estimated 3 percent—of companies that indicated they performed due diligence reported in 2015 that they were able to determine whether conflict minerals in some of their products financed or benefited armed groups."[9]

The Coalition's member companies have observed many of the same challenges in complying with the rule. Many companies' supply chains are complex and fragmented, with the reporting company frequently many tiers removed from the minerals supply chain for smelters or refiners that process metals found in its final products. Typically, there are many intervening third parties between the original sources of conflict minerals and the company. The company, therefore, must rely on its immediate suppliers, with whom it has business relationships, to provide information regarding the sourcing of necessary conflict minerals in the relevant products. The company's immediate suppliers, in turn, typically are downstream in the minerals supply chain and have similar challenges in achieving supply chain transparency.

Because many suppliers are privately held companies with no previous experience with SEC reporting, they often do not have the personnel or expertise to adequately research their supply chains. Coalition members have reported that often the information that flows up through their supply chain is inaccurate, and in some instances have included addresses for smelter locations located in a different continent, far away from the DRC. Often, suppliers are not responsive to requests for information and data. One member company of the Coalition reported that fully one-quarter of its supply chain companies did not submit responses to requests for information. In sum, accuracy and reliability of information received through this process are common shortcomings.

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[8] GAO 2016 Report, *supra* note 1, at summary.
[9] *Id.* at 21.

In regulated industries suppliers have often gone through lengthy, rigorous, and multi-level regulatory and quality assessments and approvals. In other cases, industry consolidation has led to only a limited universe of suppliers from which certain parts can be sourced. Thus, it can be very difficult to switch to another supplier if an existing supplier is not responsive to the company's conflict minerals program.

In order to make a good faith effort to comply with the conflict minerals rule, companies have had to dedicate enormous time and resources for compliance. Coalition member companies have reported having to dedicate hundreds of working-hours per year to the conflict minerals rule, which translates to enormous costs for shareholders. These are resources that could be dedicated to hiring or training other employees, or making long-term investments that benefit both the company and its investors.

One Coalition member company reported that non-recurring implementation costs totaled roughly $10 million, and that annual compliance costs will fall in the range of $1-2 million per year. That company reported having to severely update its supply chain operations, in particular by creating a new sequence of communications with thousands of suppliers in order to secure accurate information to help the company comply with the mandate. Another company estimated that their conflict minerals compliance efforts span over 7 months per year, and involve information collection spread across 300 suppliers. That company reported having up to 100 employees at any given time involved with the compliance efforts. These are costs that are ultimately borne by the shareholders and customers of public companies.

Recommendations

As many commentators have pointed out and as the Commission conceded in both the proposed and final conflict minerals rule, the subject matter of section 1502 is well beyond the scope of the Commission's historical expertise. We believe that the Commission should establish a standing interagency working group with the State Department to jointly examine the impact that the conflict minerals rule is having on the impacted region. The working group can investigate the issues involved with identification and the feasibility of supply chain authentication and propose refinements to the disclosure regime that will mitigate the lingering negative impact on persons living in the affected region, investors, business operations, the quality of disclosures, and consumer choice.

Additionally, Step One of the analysis under the final rule requires a reporting company that manufactures or contracts to manufacture products to determine whether conflict minerals are "necessary to the functionality or production" of any product manufactured or contracted to be manufactured by the reporting company. Many of the Coalition's member companies have struggled to determine whether conflict minerals are in fact "necessary to the functionality or production" of a given product in light of the broad construction of these terms and the lack of detailed guidance from the Commission or staff as to how these terms should be interpreted. This fundamental ambiguity in the final rule has created substantial uncertainty regarding the scope of the rule.

A company should only be subject to the disclosure rules to the extent it exercises a significant level of direct control over the manufacturing of its branded goods, including directly sourcing or procuring raw materials for the manufacture of those goods. Eliminating uncertainty and confusion about which companies will be subject to the rules and ensuring that only companies that directly control input materials and have the capacity to monitor the source of those materials will ensure the disclosure requirements reflect Congress's intent to create disclosure obligations for companies that are significantly and directly involved with conflict minerals.

Similarly, the reporting burden could also be improved by including safe harbor and *de minimis* standards in the rule. Safe harbor standards would enable companies distant in the supply chain that have little or no view to or control over the acquisition of the conflict minerals to comply by adopting defined contractual procurement practices, without also being subjected to undue and impractical audit or reporting requirements. Separately, without a *de minimis* standard, even trace elements of one of the conflict minerals could trigger disclosure obligations. For example, a catalyst used to manufacture another product should be viewed no differently than a physical tool used for the same purpose, which is generally excluded from coverage of the rule. But the SEC made the subject of catalysts even more confusing than it needed to be with the infamous footnote 236 to the final rule adopting release, which covers products made with a conflict-mineral catalyst if "traces" of the catalyst remain in the final product but not if the catalyst is fully "washed away." The problem with this position from an engineering standpoint is there is always a likelihood that at least some minute traces of a catalyst will unintentionally remain in a product manufactured with that catalyst, and footnote 236 provides no *de minimis* threshold. Accordingly, for a company taking a conservative approach, any product manufactured using a

conflict-mineral catalyst ends up being covered by the rule even though catalyst traces are not intended to be in the product and do not serve the functionality of the product.

Step Two of the final rule requires a reporting company that determines in Step One that a conflict mineral is necessary to the functionality or production of a product manufactured or contracted to be manufactured by the reporting company to conduct in good faith a reasonable country of origin inquiry (the so-called "RCOI") that is reasonably designed to determine whether the conflict mineral originated in a covered country or is from scrap or recycled sources. If the reporting company determines that its necessary conflict minerals did not originate in a covered country or did come from recycled or scrap sources, or if it has no reason to believe that the conflict minerals may have originated in a covered country, or if it reasonably believes that its conflict minerals did come from recycled or scrap sources, the company does not move on to Step Three and must disclose on Form SD its determination and briefly describe its RCOI. On the other hand, the reporting company must move on to Step Three if it knows that any of its necessary conflict minerals originated in a covered country and are not from recycled or scrap sources, or has reason to believe that its necessary conflict minerals may have originated in a covered country and has reason to believe that they may not be from recycled or scrap sources. Step Three, of course, contemplates an onerous due diligence process.

Putting aside the needless complexity of the core inquiry, the Coalition wishes to make two final recommendations. First, in light of significant difficulties our member companies report in tracking scrap and recycled raw materials, we urge the Commission to provide a more definite statement that scrap and recycled sources are out of scope if a reporting company reasonably believes they are included within a product otherwise subject to the rule. Second, and more fundamentally, the Commission should take action to cure the fundamental First Amendment defect inherent in the rule as written, which formed the basis for the D.C. Circuit's ruling on appeal. The most straightforward way to do so would be to permit a company that is unable to determine the country of origin after conducting an RCOI to provide a general description of those efforts in Form SD along with a statement that it has been unable to determine the country of origin. Under this approach, there would be no need to advance to Step Three of the analysis, nor would there be any need to seek an expensive audit. We are optimistic that these approaches would begin to unwind the de facto embargo on the region that now exists.

Conclusion

The Commission has an opportunity to begin correcting some of the fatal flaws embodied under the current rule, and we respectfully urge you to do so without delay. The Coalition thanks you for your consideration of these comments and is available to discuss them further with the Commissioners or staff at your convenience.

Sincerely,
U.S. Chamber of Commerce
American Petroleum Institute
The Center On Executive Compensation

cc: The Honorable Michael S. Piwowar
The Honorable Kara M. Stein