global witness

20 August 2012

Implementing the Conflict Minerals Provision

The cost of business as usual

The cost to U.S. industry of implementing Section 1502 of the Dodd Frank Act has been hotly debated since the bill was signed into law in July 2010. The law seeks to cut off the flow of funds to armed groups in the eastern Democratic Republic of Congo (DRC) by requiring companies to carry out due diligence on their supply chains to determine whether their products contain conflict minerals. Some industry bodies have been working to derail the regulations, claiming that it is too burdensome and costly for American companies to trace their supply chains. However, independent research into the costs of implementation has shown that the figures put forward by some industry players are seriously flawed. Moreover, the material costs of doing due diligence need to be considered in the context of the massive human costs of the continued conflict.

Business as usual costs lives

For over a decade the trade in minerals has fuelled a war in DRC that has cost over 5.4 million lives. The country's natural resource wealth is not the root cause of the violence, but competition over the lucrative minerals trade in its eastern Kivu provinces has become an incentive for all warring parties to continue fighting. The metals mined in eastern DRC enter global markets and make their way into products such as mobile phones, cars, airplanes and jewellery. Meanwhile the population in Congo's east bear the brunt of a conflict characterised by murder, pillage, mass rape and displacement.

Some sections of U.S. industry have already made substantial efforts to clean up their supply chains. However, others have resisted changing the way they do business. Global Witness recognises that there are costs associated with cleaning up supply chains, but the alternative – whereby multi-billion dollar American brands can continue to source raw materials in a way that exposes Congolese citizens to rape, murder, enslavement and impoverishment – is morally indefensible. Consumer awareness of this issue has risen substantially and companies that refuse to face up to their responsibilities risk serious damage to their reputations.

Industry delay tactics

The Securities and Exchange Commission (SEC) is 16 months late in publishing rules to accompany Section 1502, a delay caused in part by strong industry pushback against the regulation. The Chamber of Commerce has indicated that it will consider legal action against the SEC if the rules for Section 1502 do not 'show any benefits to investors, increase efficiencies for the marketplace or capital formation.'[1] This thinly disguised threat appeared to alarm the SEC and paralysed the rule-making process for over a year. This in turn has had negative consequences for the minerals trade in eastern Congo. A key finding of a U.S. Government Accountability Office report published in June assessing the effectiveness of Section 1502 concluded that 'in part because of the delay in the rule's issuance, many companies [...] are reluctant to participate in or support the global and in-region initiatives currently being developed or implemented because they are uncertain whether or not the initiatives will align with the anticipated rule'.[2]

Exaggerated implementation costs

Industry lobby groups the Chamber of Commerce and the National Association of Manufacturers (NAM) have claimed that it is too burdensome and costly for American companies to trace their supply chains.[3]

---

[1] Reuters, 'SEC to hold round-table on conflict minerals', 29 September 2011.

[2] United States Government Accountability Office, 'Conflict Minerals Disclosure Rule – SEC's Actions and Stakeholder-developed Initiatives', July 2012: http://www.gao.gov/assets/600/592458.pdf.

[3] See submissions by the Chamber of Commerce to the SEC, available at www.sec.gov.

However, independent analysis of the estimates put forward by some of these lobbyists finds that they are seriously flawed. One example is the National Association of Manufacturers' oft-cited claim that companies will have to pay US$1.2 to US$25 million in one-time compliance costs. Assent, a company that provides compliance software, notes in a submission to the SEC that NAM's estimate assumes even small businesses will have to pay $1 million dollars for software, when the most expensive programmes cost less than this amount. Assent actually provides this type of software free for small businesses. Claigan Environmental, a consultancy firm with expertise in supply chain management, found that NAM's estimate exaggerates the number of affected companies, grossly overstates the costs of compliance software and draws conclusions based on out of date information. Based on analysis of the compliance processes already put in place by dozens of companies, Claigan estimated one-time compliance costs to be between US$21,000 and US$813,000.[4]

Benefits to business of responsible, conflict-free supply chains

Putting in place due diligence systems will carry a cost, but in most cases this will decrease over time and will bring other business benefits to companies such as improved risk management and better supply chain performance.[5] Global Witness commissioned Green Research, a U.S. consultancy firm focused on corporate sustainability, to carry out an independent analysis that outlined some of the advantages of increased transparency and a better understanding of supply chains. Green Research spoke with over twenty companies that will have to comply with this legislation and reported a number of potential benefits:

- A few responsible companies have been working to ensure that their products do not fund conflict. With the passage of this law, other companies that were formerly taking no action will be required to comply, thus leveling the playing field for industry leaders.
- Complying with new laws offers the opportunity for innovation. The development of the 'Solutions for Hope Project' by Motorola and AVX, is groundbreaking in that it set up a closed pipe supply chain to source tantalum from the DRC. This has positioned AVX to be a provider of a new product line of conflict free components.
- A number of companies noted that increased understanding of their supply chains has the potential to lead to better risk management and improved supply chain management.[6]
- As one leading manufacturer of data storage devices put it, 'if we had to spend a whole lot of money on this, it means we've not been managing our supply chain correctly anyway.'[7]

Making U.S. taxpayers' money count

So far, much of the debate within the U.S. has centred on the financial costs to U.S. firms of taking responsibility for their use of conflict minerals. Far less attention has been given to how the activities of unscrupulous businesses are costing American taxpayers money. According USAID, the United States has contributed approximately $950 million dollars since 2008 in assistance to the DRC, for programmes relating to military education and training, peacekeeping operations, humanitarian assistance, health programmes, and conflict mitigation and reconciliation.[8] Publicly-funded U.S. development assistance to the DRC that aims to strengthen stability and security in the country risks being undermined by companies that are funding conflict through their purchases, however. As long as weak supply chain management by American and other companies drives the war economy in eastern Congo, U.S. taxpayers will continue contributing to international efforts to mitigate the appalling humanitarian consequences.

[4] Green Research, 'The Costs and Benefits of Dodd Frank Section 1502: A Company Level Perspective', January 2012, page 15, available at www.sec.gov/comments/s7-40-10/s74010-470.pdf; correspondence with Claigan Environmental, August 2012.
[5] Green Research, 'The Costs and Benefits of Dodd Frank Section 1502: A Company Level Perspective', January 2012.
[6] Ibid.
[7] Ibid.
[8] USAID Factsheet: http://www.usaid.gov/locations/sub-saharan_africa/countries/drcongo/drc_fs.pdf.