

Conflict minerals in the electronics supply chain

Introduction

Compared with conflict diamonds, conflict minerals have received little publicity. But the business world – and the U.S. in particular – is now keenly aware of the issue. In August 2012, the Securities and Exchange Commission (SEC) approved implementation rules relating to Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank). This requires companies of all sizes who have issued securities in the U.S. to declare if their products contain conflict minerals.

This paper outlines the issues surrounding conflict minerals, looks at the impact of the recent U.S. rule and considers the electronics industry's response to the problem.

What are conflict minerals?

Conflict minerals are mined in the eastern region of Democratic Republic of Congo (DRC), a country with huge and valuable natural resources.



Photo: Mark Craemer

The minerals themselves are:

Gold: the biggest source of the conflict mineral trade. Gold is an excellent electricity conductor and is generally resistant to corrosion, making it useful in electronics. Because small quantities have a high value, it is particularly easy to smuggle

- **Tungsten:** this is mined as wolframite. Tungsten is a dense metal used in a wide range of products, from consumer goods such as light bulbs, televisions and mobile phones, to Formula 1 cars and bullets.
- **Tantalum:** this is mined as columbite-tantalite (coltan). Once it is refined, it becomes a heat-resistant powder that can hold a high electric charge. It is a vital ingredient for capacitors, which are used in a vast number of devices such as mobile phones, laptop computers and other electronic equipment.
- **Tin:** this is mined as cassiterite, which is a tin oxide. Tin is used as a solder for circuit boards.

Together, tungsten, tantalum and tin are known as the '3 Ts'

Official Report on Producer Countries

Gold and the 3 Ts are also mined in many other countries around the world. The table below shows the major producers of these minerals.

Major producers of gold and the 3Ts

Estimated 2011 mine production, in metric tonnes

	<u>Gold</u>	<u>Tin</u>	<u>Tantalum</u>	<u>Tungsten</u>
Australia	270	8,000	80	
Bolivia		20,700		
Brazil	55	12,000	180	
Canada	110		25	2,000
China	355	110,000		60,000
DRC (Kinshasa)		5,700		
Ghana	100			
Indonesia	100	51,000		
Mexico	85			
Mozambique			120	
Papua New Guinea	70			
Peru	150	34,600		
Rwanda			110	
Russia	200			3,100
South Africa	190			
USA	237			W
Uzbekistan	90			
Vietnam		6,000		
Other countries	688	5,000	275	6,900
	<u>2,700</u>	<u>253,000</u>	<u>790</u>	<u>72,000</u>

Notes:

Source: U.S. Geological Survey, Mineral Commodity Summaries, January 2012

US mining of tungsten has been withheld to protect company proprietary data

The situation in DRC

DRC was ravaged by war in the late 1990s and early 2000s. In total, the war claimed more than five million lives, many from starvation and disease. Although the war was declared

over in 2003, the eastern side of the country has remained unstable ever since.



This violent and conflict-torn region contains many of the country's mineral mines, the majority of which are controlled by armed groups. Conflict minerals are the primary source of financing for these groups. The money they make from selling these minerals is used both for personal enrichment and to perpetuate the conflict. The trade is reportedly worth hundreds of millions of dollars each year.

The groups include government troops (known as the FARDC), who are often former militia members. Their involvement with mines contravenes DRC law but is prevalent nonetheless. Rebel groups such as the Democratic Forces for the Liberation of Rwanda (the FDLR) are also prominent. The FDLR is led by instigators of the 1994 Rwandan genocide.

A group known as the M23 launched a new rebellion against the DRC government in April 2012. The core of this group formerly belonged to another rebel group called the *Congrès National pour la Défense du Peuple* (CNDP). The M23 takes its name from the date that the CNDP signed a peace treaty with the DRC government – March 23, 2009. Human rights groups such as Amnesty International have documented numerous abuses attributed to the M23's fighters. Territory targeted by the M23 includes a mineral-rich area traditionally controlled by the CNDP. While the extent of the M23's control over these mines and trading routes is unclear, the CNDP had a track record of illicit control of eastern DRC's minerals trade. The M23 seized the city of Goma on 20 November 2012, before withdrawing in early December. It has since failed to attend peace talks with the DRC government.

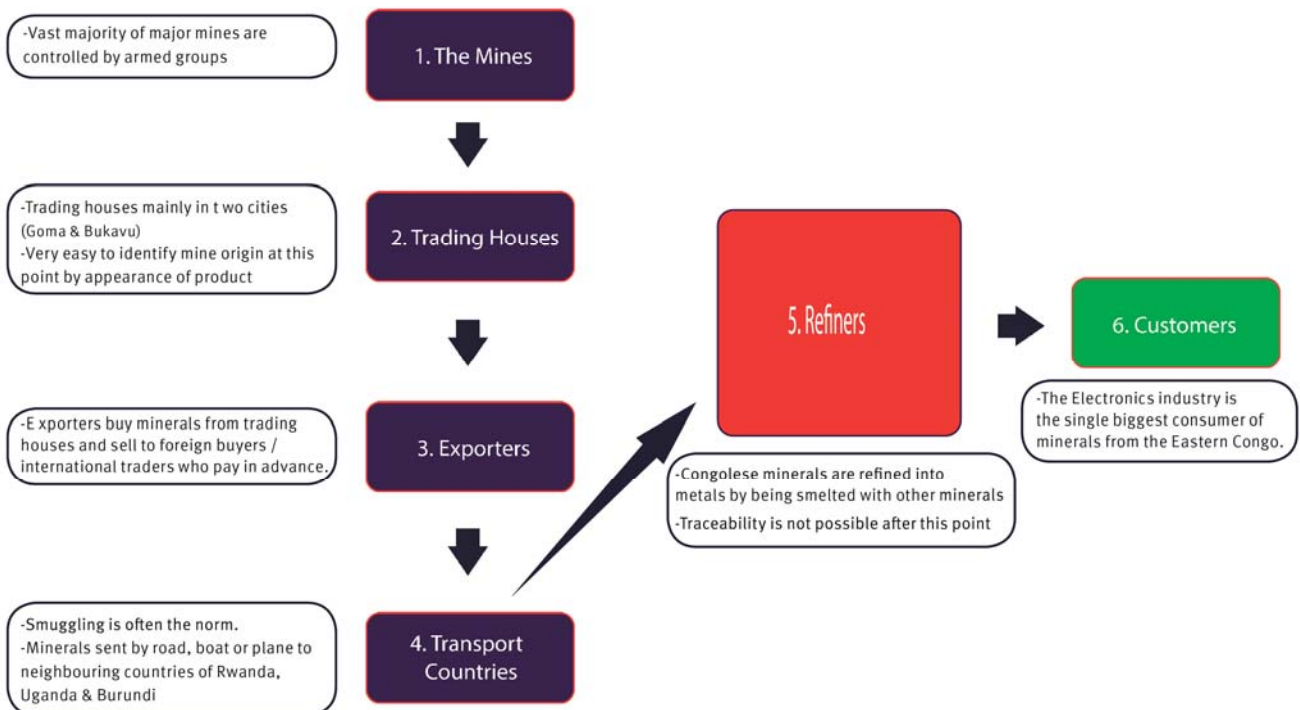
The conflict in eastern DRC has had appalling consequences for people in the region. All sides in the conflict attack civilians and commit serious human rights abuses, including murder, torture, forced labour in the mines and forced recruitment into the armed groups themselves. Hundreds of thousands of people have been displaced from their homes. Rape is widely used as a means of terrorising the population and DRC has been described as the worst country in the world in which to be female. Children also suffer significantly. It is estimated that child labourers make up around 30% of the mining workforce. Conditions in the mines are often extremely dangerous.



Photos: Mark Craemer

The conflict minerals supply chain

The diagram below shows how conflict minerals make their way from the militia-controlled mines to the electronic products that we buy every day.



At the early stages of the supply chain, it is relatively easy to identify which mine a mineral has come from, simply by its appearance. However, many trading houses and exporters fail to question the source of the minerals they are offered, or rely on verbal assurances. The absence of checks makes it simple for armed groups to sell their conflict minerals.

Almost none of the conflict minerals are officially exported from DRC. The minerals are mainly smuggled into neighbouring countries such as Rwanda, Uganda and Burundi. With their real origins obscured, the minerals are then exported to Asia, Europe, the Middle East and the U.S. and smelted with other minerals from all over the world. Once conflict minerals have passed through a refiner, it is impossible to determine where they have come from.

The electronics industry is the biggest single consumer of minerals from eastern DRC. However, other industries such as aerospace, automobiles, industrial machinery and jewellery can also have conflict minerals in their supply chain.

The impact of Dodd-Frank

Not surprisingly given the scale of the problem, governments, companies and campaign groups are seeking ways to address the issue of conflict minerals. The Dodd-Frank Act in the U.S. is an important aspect of this.

Dodd-Frank is a wide-ranging act, aimed at regulating the U.S. financial sector. It was developed in response to the global financial crisis and brings the most significant changes

to U.S. financial regulation since the aftermath of the 1930s Depression. The act was signed into law by President Obama in July 2010. In response to Dodd-Frank, U.S. regulators have produced hundreds of new rules to implement it.

Title XV of Dodd-Frank contains several specialised disclosure provisions for companies. Of particular note here is Section 1502, which relates to disclosures surrounding conflict minerals. The SEC issued the final rule relating to Section 1502 on 22 August 2012. The rule became effective on 13 November 2012 and companies must comply with it for the calendar year beginning 1 January 2013, with the first reports due by 31 May 2014.

Who does the rule apply to?

It is important to understand which companies are affected by Section 1502. According to the wording of the final rule:

“... the final rule applies to any issuer that files reports with the Commission under Section 13(a) or Section 15(d) of the Exchange Act, including domestic companies, foreign private issuers, and smaller reporting companies.”

In essence, this means that the rule applies to companies that have publicly issued equity or debt securities in the U.S. and who therefore have reporting obligations under the Exchange Act, as noted above. There is no exemption for foreign issuers or smaller companies. However, the rule does not apply to private companies or individuals, who do not have reporting obligations to the SEC.

What does the rule require?

The rule is long and complex but its key points can be summarised as follows:

- Companies that use conflict minerals (i.e. gold and the 3 Ts) “that are necessary to the functionality or production of a product” manufactured by the company must disclose annually whether any of those minerals originated in the DRC or an adjoining country.
- If the company’s conflict minerals originated in those countries, the company must submit a report to the SEC that includes a description of the measures it took to exercise due diligence on the minerals’ source and chain of custody.
- The measures taken to exercise due diligence must include an independent private sector audit of the report. The company submitting the report must identify the auditor and certify the audit.
- In addition, the report must include a description of the products manufactured or contracted to be manufactured that are not “DRC conflict free,” the facilities used to process the conflict minerals, the country of origin of the conflict minerals, and the

efforts to determine the mine or location of origin. The information disclosed by the company must also be made available to the public on the company's website.

The electronics industry's response

Many electronics companies are making solid progress in removing conflict minerals from their supply chains. A report from campaign group Enough in August 2012 ("Taking Conflict Out of Consumer Gadgets") stated that the majority of leading electronics companies had "moved ahead in addressing conflict minerals in their supply chains" since the organisation's previous report in December 2010. The report picked out Intel, Motorola Solutions, HP and Apple as "pioneers of progress".

"These leading companies have developed conflict minerals programs that have paved the way for other companies to follow. These include a smelter auditing program and an aid project for lagging smelters, direct sourcing and aid projects to help Congo develop a clean minerals trade, and tracing projects to dig deeply into their supply chains to identify precise numbers of smelters."

Enough, "Taking Conflict Our of Consumer Gadgets"

Members of the Electronics Industry Citizenship Coalition (EICC) and Global e-Sustainability Initiative (GeSI), including Intel, Dell, HP, Motorola Solutions, Microsoft, Xerox and AT&T, have engaged in developing wide-ranging schemes to implement Section 1502. These firms, alongside companies such as General Electric, Ford, Honda and Boeing, are also participants in the due diligence implementation programme hosted by the Organisation for Economic Cooperation and Development.

Intel was one of the first companies to conduct numerous smelter reviews which laid the foundations for the EICC and GeSI to develop and implement a process for independent third-party smelter audits. As of May 2012, 11 smelters were compliant and this number continues to increase.

However, the report notes that all companies have further to go to achieve "conflict free" supply chains and some major manufacturers are still lagging a long way behind.

A challenge to the SEC's rules

While individual companies have made progress towards complying with the SEC's new rule, not everyone has welcomed it. On 22 October 2012, the U.S. Chamber of Commerce, the National Manufacturers Association (NAM) and the Business Roundtable filed a lawsuit seeking to 'set aside in whole or in part' the SEC's final rule governing conflict minerals. As a result, it is currently unclear whether the new rule will come into effect as planned.

In a joint statement, the U.S. Chamber of Commerce and NAM said that the 'final conflict mineral rule imposes an unworkable, overly broad and burdensome system that will undermine jobs and growth and may not achieve Congress's overall objectives'. According to

the Wall Street Journal, the SEC estimates that the upfront cost for U.S. and foreign companies to comply with the legislation is in the region of \$3 to \$4 billion, with an additional cost of \$200 million annually. No individual company has publicly opposed the rule or come out in support of the lawsuit but many household names are members of these organisations.

Summary

Notwithstanding the current lawsuit and the effect it might have on the SEC's rule, there is no doubt that companies are increasingly looking to obtain assurance about conflict minerals in their supply chains. Many of SerCom's clients have therefore contacted us to find out more about our approach to the issue.

SerCom has a code of conduct, which was formally approved by our board of directors in June 2012. Conflict minerals are specified within the code. We require all the suppliers that we source to comply with the code and its metrics. We are committed to ensuring that we meet the highest standards of social responsibility, both across our company and within our supply base.



Photo: Mark Craemer