

**Before the Subcommittee on International Monetary Policy and Trade  
U.S. House of Representatives**

**Hearing on  
“The Costs and Consequences of Dodd-Frank Section 1502: Impacts on America and the  
Congo”**

**Statement of  
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Chairman of the Board of IPC – Association Connecting Electronics Industries**

**May 10, 2011**

Chairman Miller, Ranking Member McCarthy and Members of the Subcommittee, I am pleased to be here today to discuss the Security and Exchange Commission’s proposed rule on implementation of Section 1502 of the Dodd-Frank Act.

I am Steve Pudles, CEO of Spectral Response LLC, an employee-owned electronics manufacturing services (EMS) company located in Lawrenceville, Georgia. We employ 135 people at our 72,000 square feet facility and I’m proud to say that in 2008 we were Georgia’s manufacturer of the year in the medium company category. We provide a wide range of services for our customers from electronics assembly to product build to third party logistics. And our customers range from small start-ups to large publicly traded corporations.

I am here today as well in my capacity as the Chairman of the Board of IPC —Association Connecting Electronics Industries. The IPC is a U.S. headquartered global trade association, representing all facets of the electronic industry, including but not limited to companies that design, manufacture and assemble printed circuit boards. Contrary to common perception of electronics manufacturing, the majority of IPC’s members are small businesses. Printed circuit boards and electronic assemblies are vital to the operation of electronics products ranging from computers, cell phones, pacemakers, to sophisticated missile defense systems. IPC has more than 3,000 member companies of which 1,900 are located in the U.S.

The subject of this hearing is critically important to IPC members who collectively manufacture products that incorporate all four of the key metals refined from conflict minerals. Both Original Equipment Manufacturers (OEMs) and electronic manufacturing service (EMS) providers, such as my own company, use tin-based solder to attach components to printed circuit boards through soldering. These components include integrated circuits (chips), connectors, capacitors, batteries, etc., all of which contain one or more conflict minerals. Many printed circuit boards are finished with tin surface finishes. A number of printed circuit boards also contain gold plating for specific electrical connections.

At the outset of my testimony, I would like to recognize the good intentions of those members of Congress who authored Section 1502. By all accounts, the human rights situation in the Democratic Republic of Congo is grave. While Section 1502 has come under very legitimate scrutiny, I am grateful that my government struggles with the complexities of international conflict resolution and human rights crises.

IPC has been engaged in the conflict minerals issue for the last several years. IPC has worked with its members that supply electronic solder to encourage their suppliers --- the smelters --- to engage in conflict free sourcing. IPC is actively participating, along with its members, in the pilot implementation of the OECD due diligence guidance. IPC members are working to develop a due diligence guide for small businesses in the electronics manufacturing sector and are developing supply chain communication standards as well.

IPC supports the underlying goal of Section 1502; but quite frankly, I am concerned that the SEC's draft implementing regulations places great burdens on the private sector without having the intended positive effect on people in the DRC. In fact, there is mounting evidence of unintended negative consequences associated with companies' efforts to prepare for compliance with anticipated regulations.

I do not purport to be a subject matter expert on the issues that plague the DRC, but I can speak to the effects of the proposed regulations on companies like my own. In my testimony today, I would like to share with the Subcommittee how the draft rule is likely to impact my business and the electronics industry. Understanding the true costs and challenges of this regulation is an important aspect of finalizing reasonable requirements on the private sector.

Finally, I would like to encourage the SEC to implement the requirements of Section 1502 in a manner that supports the goals of the statute without unduly burdening U.S. manufacturing industries or causing unnecessary disruptions of the minerals trade, which is vital to the livelihood of the people of the DRC. To this end, I would like to offer my industry's views about sensible changes or additions to the proposed rule that could dramatically mitigate the costs while maintaining the spirit of Section 1502.

## **I. Costs of Implementation**

Members of the committee make no mistake, the regulations proposed by the SEC will impose a significant cost on my company and companies like mine. The irony, of course, is that my company is not an SEC issuer and so, in theory, we are not the subject of the regulations. In practice, however, the forthcoming regulations will impact us through the due diligence needs of our customers, over a quarter of which are SEC issuers.

Briefly, I would like to talk about these costs in the context of my company. Over the last several months my customers have asked me to begin auditing my supply base. Each of my customers has had a different due date for information and when I talk to peers at other companies; they are experiencing the same thing. Audit requests from customers are sweeping through the industry and the regulation has not even been released.

My company has 15,000 part numbers growing to 20,000 by the end of year. Determining the mineral content in all these parts is a herculean task not to mention the extensive auditing of my supply base with the hope they will be able to trace the raw material in their parts to a supplier and then to a smelter and then to the mine.

I expect that I will have to hire an audit company to perform the audit and I will have to hire additional staff to manage the audits. I will also have to buy a software program to collect the data ensuring that the data is compatible with both my suppliers and my customers.

A variety of cost analyses have been conducted on the proposed rule<sup>1,2,3,4</sup>. An independent analysis of the costs, conducted at the Payson Center for International Development at Tulane University Law School<sup>5</sup> at the request of Senator Durbin, estimated total costs of \$7.9 billion, over 100 times the estimate by the SEC.

More specifically, in the electronics industry, an IPC survey<sup>6</sup> of our members in the electronic interconnection portion of the electronics supply chain indicated median costs in excess of \$230,000 per year to comply with Dodd-Frank. This is a significant expenditure for companies in my industry which operate on very slim profit margins – industry average of 6.6% in 2011<sup>7</sup>.

PCB and EMS companies and their direct suppliers make up a small part of the entire electronics industry. In this group of industry segments alone, the estimated cost impact of due diligence is estimated at roughly 279 million dollars in the first year, with ongoing annual costs expected to be around 165 million dollars.

As a chief executive working hard to keep my company profitable in difficult economic times, I am troubled that the SEC's analysis on the impact of the regulation significantly underestimates the impact and cost to U.S. manufacturers. The SEC has underestimated the cost number of issuers affected by the rule, failed to account for all of the derivatives regulated under the proposed rule, underestimated the cost of compliance for affected issuers, and failed to consider the enormous burden on the supply chain. Just as we should not ignore the human rights violations in the DRC, we should not remain blind to the real costs of these regulations. By appreciating the burden to companies like mine, sensible changes can be made to the draft regulation.

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<sup>1</sup> Chris Bayer, Tulane University, "A Critical Analysis of the SEC and NAM Economic Impact Models and the Proposal of a 3<sup>rd</sup> Model in view of the Implementation of Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, October 17, 2011.

<sup>2</sup> IPC. "Results of an IPC Survey on the Impact of U.S. Conflict Minerals Reporting Requirements." February 2011.

<sup>3</sup> 75 Ref. Reg. 80966.

<sup>4</sup> National Association of Manufacturers (NAM). Comments submitted to the SEC. March 2, 2011.

<sup>5</sup> Chris Bayer, Tulane University, "A Critical Analysis of the SEC and NAM Economic Impact Models and the Proposal of a 3<sup>rd</sup> Model in view of the Implementation of Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, October 17, 2011.

<sup>6</sup> IPC. "Results of an IPC Survey on the Impact of U.S. Conflict Minerals Reporting Requirements." February 2011.

<sup>7</sup> IPC Global Quarterly EMS Statistical Program.

## II. Comments on the Proposed Regulations

The SEC has faced a challenging task in drafting regulations to implement Section 1502 of Dodd-Frank. At IPC, we do appreciate the extra time the SEC has taken to finalize a rule, and we are hopeful that this final rule will take into account the concerns the electronics industry has articulated since passage of Dodd-Frank.

The anticipated compliance burdens stemming from the draft regulations are, in a large part, related to a small number of provisions exacerbated by very short deadlines on the private sector. Accordingly, a few key regulatory provisions, when paired with sufficient implementation time, could greatly decrease the burdens associated with the regulations, while still meeting the underlying goals of Section 1502 of the Dodd-Frank legislation.

I'd like to use the remainder of my time to highlight a few of these key recommendations, which are further detailed in IPC's comments to the SEC.<sup>8</sup>

### A. Phase-in Implementation

The anticipation of the regulations has already resulted in a de-facto embargo on minerals from the DRC. Due to the absence of broad-scale tracking and traceability for minerals from the DRC, a number of companies have sought to avoid conflict associated minerals by altogether avoiding procurement of minerals from the region.

Congo's share of world tin sales dropped to 2 percent last year from about 4 percent in 2008, when it was the fifth-largest supplier, according to an article<sup>9</sup>. In North Kivu, home to the country's biggest tin mines, mineral sales have fallen more than 80 percent in the past three years, according to the mines' ministry statistics.<sup>10</sup> This has caused disruption in the minerals trade and is causing significant financial hardship to thousands that depend on the legitimate minerals trade for their livelihoods.

The most valuable change the SEC could make to its draft rule is the inclusion of a reasonable phase-in provision giving companies, like my own, a transition period to understand the final regulations and query our supply chains accordingly. Doing so would ensure that compliance with regulatory and customer requirements would be done effectively and efficiently. Additionally, a phased implementation of conflict minerals regulations will also better align regulatory requirements with developing traceability and transparency systems, thus reducing the unintended negative consequences of the regulations.

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<sup>8</sup> IPC Comments on SEC Proposed Rule on Conflict Minerals, 17 CFR Parts 229 and 249, [Release no. 34-63547; File No. S7-40-10], RIN 3235-AK48, IPC-Association Connecting Electronics Industries, March 2, 2011

<sup>9</sup> Bloomberg News. Congo Clashes Thwart Plans to Export Conflict-Free Minerals. May 2, 2012.

<sup>10</sup> Congo Clashes Thwart Plans to Export Conflict-Free Minerals, By Michael J. Kavanagh, Bloomberg, May 2, 2012

According to a United Nations report<sup>11</sup> the implementation of due diligence programs, specifically traceability systems in the DRC is severely lacking. For many mines and smelters the desire to implement due diligence measures is present but the necessary infrastructure to do so is non-existent. Certain non-conflict areas have been able to implement due diligence programs and as a result, these areas have seen improved governance, mineral production, and export of minerals. In addition, buyers for minerals that are not “bagged and tagged” have decreased, except for three smelters in China. According to a recent OECD report<sup>12</sup>, areas that have yet to implement due diligence measures continue to struggle. The UN report states:

“In areas where no traceability systems have been introduced, particularly the Kivus and Maniema, mineral production and exports have fallen. This has not only decreased conflict financing, but also weakened mining sector governance, with a greater proportion of trade becoming criminalized and with continued strong involvement by military and/or armed groups.”

IPC members are actively working to improve transparency and accountability within their supply chains. I want to commend our sister trade associations, ITRI, Electronic Industry Citizenship Coalition (EICC), Global e-Sustainability Initiative (GeSI) for their tireless efforts over the past several years in the DRC to certify legitimate minerals trade and establish smelter audit programs. At best, these programs could take another 1-2 years to be fully functional. Failure to establish a realistic, implementable time-line for required supply chain transparency will result in continuing significant, negative unintended consequences for those engaged in legitimate minerals trade. It is highly unlikely that a full scale-up of these programs will be possible in time to allow issuers to rely upon them in the year immediately following implementation of the regulations.

A phase-in of the regulations will allow industry and local governments to continue to make progress on due diligence measures that will benefit the region. During the phase-in period, IPC recommends that issuers be required to disclose to the SEC: 1) that specific conflict minerals are necessary to the functionality of a product manufactured by the issuer; 2) the company’s conflict minerals policy; 3) the company’s efforts to exercise due diligence on the conflict minerals used in their product. IPC recommends that during this phase-in period, companies that are unable to determine the source of their conflict minerals would not be required to complete a CMR, as the legislation requires such a measure only for companies whose conflict minerals did originate in the DRC or adjacent countries.

Implementation of this phase-in would provide for an orderly, cost-efficient transition that promotes the goals of the legislation without inflicting undue burdens and harm upon U.S.

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<sup>11</sup> United Nations Security Council. Letter dated 29 November 2011 from the Chair of the Security Council Committee established pursuant to resolution 1533 (2004) concerning the Democratic Republic of the Congo addressed to the President of the Security Council. December 2, 2011.  
[http://www.un.org/ga/search/view\\_doc.asp?symbol=S/2011/738](http://www.un.org/ga/search/view_doc.asp?symbol=S/2011/738).

<sup>12</sup> Upstream Implementation of the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas. May 2012.

issuers, their suppliers, and those engaged in the legitimate trade of conflict minerals from the DRC.

## **B. Indeterminate Category**

The SEC can also help mitigate the unintended consequence of a de facto ban by establishing a transitional category of conflict minerals of indeterminate source. This third category is envisioned to be of a short and temporary nature according to a schedule that will allow enough time for implementation of supply chain traceability in the DRC and adjacent countries. By providing a third category of conflict minerals for a transitional period approach, companies will not be encouraged to impose a de-facto ban on legitimate trade from the DRC in order to avoid identifying their products as supporting conflict in the DRC.

## **C. De-Minimis**

Manufacturers, including myself, will find it difficult to determine not only the presence of each mineral but the specific amount contained in each product. In my opinion, an effective regulation would focus on economically significant uses of conflict minerals. The SEC can accomplish this by instituting a de-minimis threshold. Establishing a de-minimis threshold would allow the SEC to focus on products containing a significant amount of conflict minerals in a manner that will change supply chain behavior. Should the SEC not wish to implement permanent de minimis standards, IPC recommends the use of de minimis standards for phasing-in the regulation. By focusing only on significant uses of conflict minerals first, the SEC would improve the efficiency of implementation and ease the compliance burden on some of the less significant users of conflict minerals, while maintaining consistency with the intent and goals of the rules.

## **D. Synchronized Reporting Schedule**

Although my company is not a SEC filer, many of my customers are. Therefore, in order to keep their business, I must comply with customer requests to provide the necessary information on the presence and source of conflict minerals in the products. I am not alone. Many electronics manufacturing companies are not SEC filers, leaving them in the same situation as me. The SEC can significantly reduce the substantial burden on the supply chain by implementing a single reporting date for all issuers. Requiring reports throughout the year, in concert with each issuer's annual report will require my company to constantly be replying to conflict minerals inquiries, posing a significant burden. Because my customers are likely to be on different reporting schedules, I will likely have to conduct due diligence and support third party audits repeatedly throughout the year. A single reporting date will allow for increased efficiency and thus lower costs, without reducing the effectiveness of the regulations.

## **E. Exemption for Recycled and Scrap Materials**

The electronics industry is committed to environmentally sensible practices and has been involved in a variety of efforts to further that objective. Many companies, including my suppliers, use recycled metals in order to reduce the amount of virgin materials required in the manufacturing process. It is imperative that the SEC does not diminish these efforts by adding significant regulatory burdens to the use of recycled or reclaimed conflict minerals. The final rule should include an alternative approach for recycled or scrap sources that is practical and does not overly burden recycled materials so as to discourage their use.

An issuer, or the supplier of an issuer, using a recycled material containing conflict minerals will not be able to provide any of the details required in a CMR. The traceability of the reclaimed metals is impossible to track due to the various forms of recycling and thousands of consolidators, reclaimers, and scrap dealers both foreign and domestic. Instead, issuers should have a reasonable basis for believing the material is recycled and maintain auditable records to support the determination. IPC believes that due diligence is the appropriate requirement for verifying recycled or reclaimed conflict minerals.

Use of recycled materials is a significant part of the metals trade and needed to decrease the demand for minerals from the conflict regions in the DRC or adjoining countries.

## **F. The SEC Should Provide Non-Binding Examples of Appropriate Due Diligence**

Given the varying circumstances affecting the broad range of companies impacted by this rule, the SEC should not prescribe specific due diligence requirements as it would impose significant burdens, especially to companies that are small businesses. The SEC should, however, provide assistance to companies by identifying examples of acceptable due diligence such as industry developed smelter validation audits, the bag and tag scheme being developed by ITRI, information or standards provided by the Department of State or other federal agencies, the OECD standards, and others. Provision of a list of acceptable standards and guidance will provide important assistance to companies without hampering their ability to comply in a manner that is both efficient and appropriate for their circumstances.

## **G. The SEC Should Clearly Define Covered Products.**

The electronics sector I represent typically assembles electronics for Original Equipment Manufacturers (OEMs) or name brands. Although many of these items contain conflict minerals, my company typically does not control selection of suppliers or material sources for the majority of products we manufacture. Further, this may put my company in the position where I do not have sufficient leverage over a supplier selected by an OEM, placing an excessive burden on my company. Issuers who purchase or assemble products from an approved supplier list controlled by their customers should be exempted from the proposed reporting requirements for those items they do not specify.

The SEC should not consider conflict minerals necessary to the production of a product if they are not contained in the product. The SEC should not consider conflict minerals necessary to the production of a product even if the tool or machine containing conflict minerals was manufactured for the purpose of producing the product. Such an approach would be much broader than intended by the legislation. Additionally, such an approach would be very difficult for the SEC to implement or enforce, given the difficulty of determining and verifying which equipment is designed for what production process. Finally, this reporting may be unnecessarily duplicative, as any issuer manufacturing tools or machinery would be required to comply with the proposal if conflict minerals are necessary for the functionality of the tool or machine.

### **III. Conclusion**

In conclusion, on behalf of my company and IPC's over 3,000 members, I urge the SEC to implement the requirements of Section 1502 in a manner that supports the goals of the statute without unduly burdening U.S. manufacturing industries or causing unnecessary disruptions of the legitimate minerals trade, which is vital to the livelihood of the people of the DRC.

Thank you for the opportunity to address you today.