

United States House of Representatives  
Committee on Financial Services  
2129 Rayburn House Office Building  
Washington, D.C. 20515

MEMORANDUM

**To:** Members of the Committee on Financial Services

**From:** FSC Majority Committee Staff

**Date:** May 16, 2013

**Subject:** May 21, 2013, Monetary Policy and Trade Subcommittee Hearing on “The Unintended Consequences of Dodd-Frank’s Conflict Minerals Provision”.

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The Subcommittee on Monetary Policy and Trade will hold a hearing on “The Unintended Consequences of Dodd-Frank’s Conflict Minerals Provision” at 2:00 p.m. on Tuesday, May 21, 2013, in Room 2128 of the Rayburn House Office Building. This will be a one-panel hearing with the following witnesses:

- David Aronson, Freelance Writer, Editor of [www.congoresources.org](http://www.congoresources.org)
- Mvemba Dizolele, Peter Duignan Distinguished Visiting Fellow, Hoover Institution
- Rick Goss, Senior Vice President of Environment and Sustainability, Information Technology Industry Council
- Sophia Pickles, Policy Advisor, Global Witness

### Background

Ever since it gained its independence in 1960, the Democratic Republic of the Congo (DRC) has been in a state of civil war. In 2000, the United Nations Group of Experts linked the Congolese civil war to the mineral trade. Tin, tantalum, tungsten, and gold—which are used to manufacture everyday goods such as pens, USB drives, buttons, and food containers—are mined in areas of the eastern DRC that the Congolese army and armed militias are fighting to control. The factions use proceeds from mineral sales to buy weapons. Some have argued that banning the use of minerals mined in or near the DRC or discouraging companies from using such minerals by “naming and shaming” them might deny rebel militias a source of funding and end the conflict.

Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111-203) is one such effort to discourage companies from using minerals mined in the DRC. Section 1502 requires the Securities and Exchange Commission (SEC) to promulgate rules for public companies requiring them to disclose their use of minerals that originated in the DRC, which Section 1502 defines to be “conflict minerals.” Public companies must comply with Section 1502’s disclosure requirements when these minerals are necessary to the functionality or production of a product. If companies cannot verify that the minerals they use did not originate in the DRC, Section 1502 requires them to (1) exercise due diligence on the source and chain of custody of these minerals; (2) hire an independent third party to audit the due diligence measures; and (3) report to the SEC on the due diligence measures they undertook and their auditor’s assessment of those measures.

Section 1502 was added to the Dodd-Frank Act during the House-Senate conference negotiations, without the benefit of a legislative hearing on the proposal. As a result, Congress did not examine how Section 1502 would be implemented, whether it would help end the conflict in the DRC, and what its effects would be on the DRC, the companies that use these minerals to manufacture goods used by consumers and other manufacturers, or the broader economy. Although bills similar to Section 1502 were introduced in previous Congresses, no legislative hearings were held on those bills and they were not marked up in Committee.<sup>1</sup>

Notwithstanding the lack of legislative history to guide it, the SEC has drafted regulations to implement Section 1502. Although Section 1502 requires that implementing regulations be finalized no later than April 15, 2011, the SEC did not issue a final rule until September 2012 because the subject matter was beyond the SEC's usual area of expertise.<sup>2</sup> SEC Chairman Mary Schapiro testified before Congress that it is unusual for the SEC to promulgate and enforce regulations under prescriptive laws that require specialized knowledge of the mineral trade in the DRC. The SEC received over 30,000 comment letters on its proposal to implement Section 1502.

### **The Consequences of Section 1502 on the DRC**

Some human rights groups and Congolese activists are concerned that Section 1502 may have unintended consequences that harm those who live in the DRC. To avoid triggering Section 1502's reporting requirements, most mineral procurement companies no longer purchase minerals from the DRC. Because there is no recognized system to verify that the sources of minerals from the DRC are conflict-free, efforts to ensure that these minerals do not enter supply chains have resulted in a *de facto* embargo against the DRC. Many believe that rather than ending the conflict, the embargo has instead further impoverished the people it was intended to help.<sup>3</sup>

According to the Extractive Industries Transparency Initiative, as many as 12.5 million Congolese—approximately 17 percent of the DRC's population—depend on mineral trading to make a living, and most of the money generated by mineral trading goes to artisanal miners, rather than soldiers and rebels. In a working paper issued by the Center for Global Development, Dr. Laura Seay, assistant professor of political science at

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<sup>1</sup> In 2009, legislation similar to Section 1502 was introduced in the House and Senate: Rep. Jim McDermott (D-WA) introduced H.R. 4128, the Conflict Minerals Trade Act, and Senators Sam Brownback (R-KS), Dick Durbin (D-IL), and Russ Feingold (D-WI) introduced S. 891, the Congo Conflict Minerals Act.

<sup>2</sup> The SEC's mission is to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation. The SEC has little or no experience in crafting trade sanctions or articulating and enforcing human rights policy, two areas which have not traditionally been within the purview of securities regulation.

<sup>3</sup> See, for example, Séverine Autesserre, "Dangerous Tales: Dominant Narratives on the Congo and their Unintended Consequences", *African Affairs* (Spring 2012), available at <http://afraf.oxfordjournals.org/content/early/2012/02/09/afraf.adr080.full.pdf+html>; Laura Seay, "What's Wrong with Dodd-Frank Section 1502: Conflict Minerals, Civilian Livelihoods, and the Unintended Consequences of Western Advocacy", *Center for Global Development Working Paper* (Jan. 5, 2012), available at [http://www.cgdev.org/sites/default/files/1425843\\_file\\_Seay\\_Dodd\\_Frank\\_FINAL.pdf](http://www.cgdev.org/sites/default/files/1425843_file_Seay_Dodd_Frank_FINAL.pdf); David Aronson, "How Congress Devastated Congo", *New York Times* (Aug. 7, 2011), available at <http://www.nytimes.com/2011/08/08/opinion/how-congress-devastated-congo.html>; and Hannah Levintova, "Boycott Minerals from Congo? Not So Fast," *Mother Jones* (Sep. 29, 2011), available at <http://www.motherjones.com/mojo/2011/09/congo-dodd-frank-conflict-minerals>.

Morehouse College, has reported that “despite ending most of the trade in Congolese conflict minerals,” the de facto embargo has “done little to improve the security situation or the daily lives of most Congolese.” Severine Autesserre, assistant professor of political science at Barnard College, has argued that Section 1502 and other international efforts have not only failed to achieve their intended results but that they “have exacerbated the problems that they aimed to combat.”

The non-profit organization Enough, one of Section 1502’s original proponents, has noted it did not intend for Section 1502 to result in an embargo. Nonetheless, the organization believes that the SEC should continue to implement Section 1502.

### **The Impact of Section 1502 on U.S. Companies**

Because conflict minerals are used to make a vast array of products, Section 1502 could affect nearly all of the 5,994 publicly-traded companies in the U.S. Privately held companies that supply minerals to public companies will also bear the cost of implementing Section 1502, because public companies will require them to account for the origin of minerals in the products they supply to public companies. One large U.S. food company, for example, claims to have over 100,000 secondary suppliers which sell products that may contain conflict minerals. Because that company must report to the SEC on its use of these minerals, its secondary suppliers will also have to account to that company on the origins of the minerals they use.

Companies that will be subject to Section 1502’s requirements report that compliance costs will be high. According to a Tulane University study<sup>4</sup> commissioned by Senator Dick Durbin (D-IL), the cost of implementing Section 1502 will be \$7.93 billion. The study focused on the costs to public companies and their first-tier suppliers. The study found that almost half of the total cost—\$3.4 billion—would be internal costs, and the rest—\$4.5 billion—would take the form of payments to third parties for services such as consulting, IT systems, and audits. The bulk of the costs—\$5.1 billion—would be borne by suppliers to public companies, including small and medium-sized businesses. The study estimates that implementing Section 1502 will cost public companies \$2.8 billion. The National Association of Manufacturers has estimated that the cost of implementing Section 1502 will be between \$9 and \$16 billion.

### **Section 1502 and Conflict in the DRC: Effective Human Rights Policy?**

Notwithstanding the unprecedented use of U.S. securities regulation as an instrument of human rights policy or its costs on manufacturers and consumers, it is not clear that an aggressive implementation of Section 1502 would help end the civil war in the DRC. The Enough Project and Global Witness—two global human rights organizations that advocated for Section 1502’s inclusion and that continue to support the law—have asserted that Section 1502’s costs are justified by the hope that it will end the conflict in the

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<sup>4</sup> Chris Bayer, “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 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act”, Tulane University: Payson Center for International Development. (Oct 17, 2011), available at [http://www.payson.tulane.edu/sites/default/files/3rd\\_Economic\\_Impact\\_Model-Conflict\\_Minerals.pdf](http://www.payson.tulane.edu/sites/default/files/3rd_Economic_Impact_Model-Conflict_Minerals.pdf)

eastern DRC. Yet it is not clear that Section 1502 can reduce the conflict in the DRC. A recent United Nations report noted that non-mineral natural resources continue to finance armed groups and criminal networks in the DRC. For that reason, Section 1502—no matter how robustly implemented—will not cut off funding to these groups.

Others are concerned that the proponents of Section 1502 have failed to adequately consider its effects on the Congolese, and they have raised concerns that Section 1502 will further immiserate hundreds of thousands of Congolese who depend on the mineral trade for their livelihoods. The Enough Project has responded to this criticism by claiming that it is the exporters of minerals who profit from the mineral trade, not the Congolese. Some academics dispute this claim, including Mvemba Dizolele of the Eastern Congo Initiative. They have concluded that if family members and dependents of miners who have lost this source of income are counted, the number of Congolese who have been harmed by Section 1502 likely climbs into the millions.