NATIONAL ASSOCIATION OF Manufacturers

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Testimony

of Franklin Vargo
Vice President
International Economic Affairs
National Association of Manufacturers

before the House Committee on Financial Services
Subcommittee on International Monetary Policy and Trade

on "The Costs and Consequences of Dodd-Frank Section 1502:
Impacts on America and the Congo"

May 10, 2012

COMMENTS OF FRANKLIN VARGO

BEFORE THE

House Committee on Financial Services
Subcommittee on International Monetary Policy and Trade

MAY 10, 2012

Mr. Chairman, Members of the Committee: Good morning. I am Frank Vargo, Vice President for International Economic Affairs at the National Association of Manufacturers (NAM). I am pleased to appear before this subcommittee to discuss the Securities and Exchange Commission's (SEC) implementation of Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), and its implications for America's manufacturers.

The NAM is the nation's largest industrial trade association, representing small and large manufacturers in every industrial sector and in all 50 states. Its membership includes both large multinational corporations and small and medium-sized manufacturers. Our members depend heavily on the global supply chain to compete within the U.S. marketplace and abroad. NAM members have a strong track record of working with the U.S. government to improve supply chain transparency and compliance practices.

Let me emphasize that the NAM supports the underlying goal of Sec. 1502 to address the atrocities occurring in the Democratic Republic of Congo (DRC) and adjoining countries and is working with other stakeholders to address the problem. We need, however, practical implementation rules that will achieve the objectives of the act while not unduly burdening the manufacturing process in the United States.

Generally speaking, Section 1502 requires companies subject to SEC reporting whose manufactured goods contain any gold, tantalum, tin, or tungsten to report annually to the SEC as to whether those minerals "did originate" from the DRC or adjoining countries. In cases in which such conflict minerals did originate in those countries, SEC registrants must submit a report that includes a description of the measures they took to exercise due diligence on the source and "chain of custody" of such minerals. Such a report must include an independent private-sector audit. In addition, the report must include a description of the products manufactured or contracted to be manufactured that are <u>not</u> 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 with the greatest possible specificity.

These requirements pose a potentially huge financial and reporting burden on America's manufacturers, given the breadth of use of these four metals throughout the manufacturing process and the depth, complexity, and constantly evolving nature of modern supply chains. The requirements also potentially affect many tens of thousands of small and medium-sized companies not subject to SEC reporting because they will, in turn, be asked by their large customers to provide the due diligence that will be required by the rule.

The NAM and our members recognize the importance of preventing the use of conflict minerals from the DRC and adjoining countries. We believe, though, that the SEC's regulations can implement the law in a manner consistent with the goals of the legislation without unduly burdening industry and harming American competitiveness.

The final SEC rule that would implement Sec. 1502 needs to be consistent with the realities of global supply chains, and acknowledge the practical limitations that issuers face in attempting to influence the behavior of other parties in supply chains that stretch from downstream users across multiple tiers of suppliers to refiners/smelters and mines.

We believe that modifications to the Proposed Rule are needed to accomplish that end. I would like to note that we appreciate the care with which the SEC has been proceeding, evincing an understanding of the consequences of getting the rule wrong. We have availed ourselves of the various opportunities for input that the SEC has provided the NAM and individual member companies, and deeply hope the final rule is one that provides the practical flexibility we believe is necessary.

In my statement today, I would like to call the Subcommittee's attention to three key points: (1) the need for a phase-in period that includes a category of "indeterminate origin," (2) the need for flexibility in determining due diligence, and (3) the huge cost of complying with this rule, particularly if sufficient flexibility is not provided.

1. The Need for A Phase-in Period with an "Indeterminate Category"

The SEC acknowledged in its draft proposal that standards of reasonableness for origin inquiries and due diligence will evolve over time as reporting and monitoring infrastructure becomes more robust. However, the Proposed Rule does not take adequate account of the extreme limitations that currently exist on the ability to submit meaningful reports and to exercise effective due diligence.

The reporting requirements in the Proposed Rule would become effective immediately, though such important elements of due diligence as the conflict-free smelter program are still evolving, and available information about each of the four metals varies widely. These limitations make it impossible for most manufacturers – especially large companies with diversified product lines – to file meaningful and informative information with the SEC. This disconnect between the proposed effective date of the new requirements and creation of the necessary infrastructure to facilitate compliance with the requirements necessitates a phase-in period.

The NAM and our member companies are grateful that Chairman Schapiro's most recent testimony expressly acknowledged the need for a transition period to allow the many industry, national, and international compliance initiatives that are getting under way to mature to the point where they can assist companies to make meaningful disclosure and to have a real and positive impact on the humanitarian crisis in Central Africa.

Industry and company efforts are underway to attempt to identify and reduce or eliminate DRC conflict minerals in their products. Some companies with very short supply chains are having some success, but they are few in number. Industry groups also have efforts underway. NAM members are participating in numerous international, public-private, and industry-led initiatives to drive change abroad and stop the trade in conflict minerals from the DRC and adjoining countries, including industry-wide smelter certification programs and working to create the needed infrastructure on the ground and around the world to facilitate compliance with the Proposed Rule.

The NAM is working closely with our member companies to increase pressure on conflicted-affected suppliers. In addition, NAM staff have participated in many forums sponsored by sector-specific efforts and international organizations in order to support efforts designed to influence a positive outcome for the region.

Determined efforts are underway, but they have not yet matured. Perhaps furthest along is the Electronic Industry Citizenship Coalition – Global e-Sustainability Initiative (EICC-GeSI). Considerable effort is going into the initiative, with many companies and industries looking it to see if its methodologies can be adapted to their needs. A major part of the EICC-GeSI effort is the smelter certification program to identify smelters that are free of DRC conflict minerals. However, to date, it appears they have been able to certify only 11 of the hundreds of smelters and gold refiners in the world supply chain – all of them tantalum smelters.

EICC-GeSI asked Resolve, an independent non-profit organization, to attempt to "trace" a small sample of electronics supply chains back to the mine and, in a smaller number of cases, to conduct a parallel effort to "track" a subset of these supply chains from the mine downstream. The results of their research – less than a 25 percent response rate from suppliers after six months of intensive effort, despite a limited number of supply chains in a single industry with many common suppliers – attests to the challenges confronting registrants attempting to establish a full map of their supply chain. In its report, Resolve concluded, "This means that today, while end-use companies have the potential to establish and have confidence in sources for some percentage of the metals in their products, they cannot assert 100 percent sourcing certainty about individual metals…. Movement is likely to come in a step-wise manner."

Similarly, the State Department conflict minerals map called for by Section 1502 was so heavily conditioned by its authors as to be virtually useless for due diligence. In its report, the State Department said, "Given the… limitations on the data available, this map does not provide sufficient information to serve as a substitute for information gathered by companies in order to exercise effective due diligence on their supply chains."

The Public-Private Alliance for Responsible Minerals Trade (PPA) is a new, joint initiative with U.S. State Department, the Agency for International Development, non-governmental organizations, and companies and industry organizations to support supply chain solutions to conflict minerals challenges in the DRC. However, it is just getting started, and has not yet let contracts seeking efforts to develop validated, certified, and traceable mines and supply chain routes in the DRC and adjoining countries in order to encourage legitimate mining in the region.

The Organization for Economic Cooperation and Development (OECD) Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High Risk Areas (the "OECD Guidelines") published last year is being tested for feasibility in two pilot projects (which include the participation of NAM members from diverse industry sectors), one of which is just being completed and one of which is just getting underway.

All these efforts are laudable and to be encouraged, but their lack of results so far should not be a reason to penalize companies that, despite their best efforts with what information exists, cannot know the origin of the metals in their products. Moreover, it must be emphasized that even when fully mature these various compliance resources will not enable large manufacturers of complex end products to trace or track the conflict minerals in their supply chains back to the smelter or refiner of origin, much less back to the mine. Modern supply chains are simply too deep, complex, and variable to permit such an exercise in the vast majority of cases. What they can do, when mature, is to enable companies to develop reasonable confidence that they are not sourcing from conflict-affected mines, and collectively to mobilize sufficient pressure across multiple industry segments to dramatically constrict conflict funding.

Accordingly, a phased-in approach is needed. The phased-in approach does not exempt or delay an issuer's requirements to report under the statute. In our proposal to the SEC, every issuer subject to the regulation would undertake, within the imperfect information infrastructure, to disclose to the SEC what information they have been able to develop regarding the use of conflict minerals and the efforts each is taking to increase transparency and stop the use of conflict minerals from the region for the first full fiscal year the regulation is in effect.

During the phase-in period, companies would adopt and clearly communicate to first-tier suppliers the company policy or similar corporate statement for the supply chain of the minerals originating from conflict-affected and high-risk areas. The policy or similar corporate statement should incorporate the standards against which due diligence is to be conducted, consistent with appropriate standards and/or common industry approaches, adapted to company and industry sector circumstances.

Where practicable, companies would begin a process to develop reasonable assurance that they are not sourcing tin, tantalum, tungsten and gold from conflict mines by contacting first-tier suppliers. This process may be implemented through participation in industry-driven programs, national or international standards organizations, and/or through contract flow-down provisions or other written commitments.

As part of this, companies would ask first-tier suppliers to 1) push the new policies upstream to their suppliers, and 2) adopt contract provisions, purchase orders, specifications or use other means to encourage their suppliers to transmit information downstream from smelters/refiners. Thus even within the phase-in period the objectives of the Act would be substantially advanced, without penalizing companies.

For the phase-in period, the SEC should create a temporary third category, "indeterminate origin," for products manufactured or produced with minerals for which issuers, despite their best efforts, are unable in the first years of their programs to determine origin. At least for the first years, issuers should not be required to file a Conflict Minerals Report (CMR) for such minerals. Requiring issuers to submit a CMR and/or identify their products as "not DRC conflict free" when the issuer has not been able to determine the origin after making reasonable inquiry would significantly harm global brands, place U.S. companies at a competitive disadvantage, and damage investor relations even though the issuer has in a place a policy prohibiting the use of conflict minerals from the DRC or adjoining countries in its supply chain that are not otherwise validated as conflict-free. Users of the indeterminate origin category would have to follow SEC-mandated steps in the phase-in period along the lines discussed above.

We recognize there is a concern that an indeterminate category could provide an excuse to ignore obligations under the law. However, the vast majority of issuers subject to the new requirements place a high value on corporate compliance, and will not be "bad actors." Providing false information and knowingly misleading the SEC will have significant negative repercussions for issuers and subject them to penalties under the law. Plenty of checks exist to prevent a company from making reckless inquiries to determine if conflict minerals originated in the DRC or adjoining countries. Given today's regulatory environment, the threat of an SEC enforcement action is a strong deterrent to companies that do not comply with the requirements.

2. The Need for Flexible Due Diligence

The SEC's Final Rule needs to create a flexible due diligence standard that recognizes no two supply chains are identical. The SEC should provide guidance to issuers on what would constitute reliable due diligence, but not mandate a specific set of requirements. Given the diversity of issuers and products affected, issuers should be permitted to develop due diligence plans that are consistent with their supply chains and information available from recognized government sources.

This is consistent with work with the international community to develop global supply chain solutions. Such flexibility is also consistent with other areas of law regarding supply chains and human rights issues. An issuer should be able to create a due diligence program aligned with reliance on reasonable representations from suppliers or a supplier declaration approach and smelter compliance to determine the origin of conflict minerals.

The Commission's Final Rule needs to have a "reasonable country of origin" threshold determination. It is important to understand that perfect certainty with respect to the origin of all conflict minerals in a modern supply chain is unattainable at virtually any price. Rather, the rule needs to reflect the understanding that registrants can comply with the letter and spirit of the Act by making a reasonable, risk-based, good-faith determination based on the totality of their circumstances. Such a determination could rest on such factors as the existence of flow-down clauses in the company's supplier contracts, company policies and use of consensus best practices, and participation in industry-wide, public-private, or international initiatives.

Such approaches are routinely used to achieve other vital government and social objectives, including protection of customer safety and health, quality assurance, environmental protection, and protection of national security and classified technology.

Equally important, due diligence over the source and chain of custody should not be defined to require: (1) that an issuer identify all parties between the mine (or even the smelter or refiner) and its 1st tier suppliers, or (2) that the issuer determine all the materials used in every manufactured item. While some manufacturers with short supply chains, small numbers of product types, and comparatively simple products may ultimately be able to trace metals in their products back to the smelter/refiner or perhaps even the mine of origin, the reality is that no manufacturer of complex end-products can map conflict minerals through the thousands of suppliers in its supply chain back to the smelter/refiner, much less the mine, or achieve a "chain of custody" that would enable it to know with certainty the origin of the conflict minerals in each of the millions of piece parts in its end-products.

Such companies have many tiers of suppliers, with thousands of companies in their supply chains. The Global Research Center for Strategic Supply Management at Arizona State University reports that the average large company has 7,000 suppliers. Many NAM members have 15,000 or more companies in their supply chains, and one company reported that through all its tiers its supply chain has 100,000 companies.

Moreover, NAM member companies' supply chains are not static. They are constantly changing as companies continuously seek new suppliers with better products or more competitive prices or delivery terms. Companies also seek multiple suppliers so as to avoid a situation in which a supply interruption from a single supplier can force a plant shut-down.

The OECD Guidelines recognize the complexity and fluidity of supply chains and the limited leverage end-product manufacturers have on remote tiers of their supply chains. The Guidelines state, "Control mechanisms based on tracing minerals in a company's possession are generally unfeasible after smelting, with refined metals entering the consumer market as small parts of various components in end products. By virtue of these practical difficulties, downstream companies should establish internal controls *over their immediate suppliers* and may coordinate efforts through industry-wide initiatives to build leverage over sub-suppliers, overcome practical challenges and effectively discharge the due diligence recommendations contained in this Guidance."

As noted, some manufacturers may be able to achieve such visibility due to the nature of their supply chains and products, but requiring such tracing or tracking for all manufacturers is not necessary to accomplish the humanitarian purposes of the Act and would impose needless and extraordinary costs on many industry segments. Issuers should have the flexibility to work with direct suppliers to push requirements to use conflict free minerals/metals upstream. The SEC should acknowledge that a risk-based program or use of a risk-based supply chain approach for entities in the supply chain is acceptable in place of a product-based or materials declaration approach.

Compliance with internationally recognized standards or guidance should be considered as a key factor in determining whether an issuer has exercised reasonable due diligence. In particular, compliance with the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-affected and High-Risk Areas (the "OECD Guidelines") should be stipulated as a "safe harbor," and be sufficient to meet the requirements of Section 1502.

It is important that the Commission ensure its compliance regime is consistent with the OECD Guidelines. Nothing in the Guidelines is inconsistent with any requirement of Section 1502. The Department of State in seeking to provide guidance to commercial entities seeking to exercise due diligence has endorsed the Guidelines, as have the affected governments in the region and dozens of other countries. Although important aspects of their implementation are a work in progress, they clearly now represent and will continue to represent consensus best practices agreed by the stakeholders.

However, although we believe that adherence to the OECD Guidelines should be evidence of reliability, this framework is newly entering an implementation phase and subject to changes based upon initial implementation efforts. Moreover, the Guidelines may not be appropriate for all issuers. Accordingly, the SEC should treat all accepted international, national, or industry compliance schemes as acceptable means of complying with Section 1502.and should not be the only international standard that is acceptable. Moreover, the Guidelines may not be appropriate for all issuers.

Audits of conflict mineral reports could be the single largest component of ongoing compliance expenses under the Proposed Rule. Clarity and flexibility are both needed as to the appropriate standard and the type of audit required. Any required audit (after the initial phase-in period) should examine a company's due diligence compliance program and procedures, rather than a materials-based outcome approach verifying whether the company was able to trace the minerals in its products back to the smelter.

3. The rule is expected to cost the U.S. industry $9-16 Billion to Implement

The NAM believes that the Proposed Rule is a significant rulemaking and will cost U.S. industry between $9-16 billion to implement. This is a far higher cost than the SEC's estimate of $71 million – more than 100 times higher. As such, we believe the SEC's analysis of the impact of the regulation greatly underestimates the impact on and cost to U.S. manufacturers.

The NAM's detailed estimate is available on our website and on the SEC's as well. Without going into too much detail in my statement today, some of the difficulties with the SEC estimate are that it estimated only 20 percent of the 5,994 issuers would be affected (evidently because the DRC supplies only 20 percent of global tantalum), underestimated the cost of CMR audits by a factor of four, and applied its estimates only to issuers, making no estimate of the cost of compliance for the thousands of companies in the supply chain – most of whom are not issuers.

The NAM estimated that the average large company has 2,000 companies in its supply chain – a conservative estimate, given that the Global Research Center for Strategic Supply Management at Arizona State University concluded the average large company has 7,000 suppliers.

While the new reporting mandate only applies to companies required to report to the SEC, we expect these requirements will flow through the entire supply chain. The regulation, if insufficiently flexible, could effectively force suppliers not subject to SEC reporting to maintain extensive records of their source materials, costing them thousands of dollars to establish and maintain these records. In its October 25, 2011, letter to the SEC, the Small Business Administration's Office of Advocacy said, "Because the SEC does not take into account the complexity of supply chains and the number of small businesses that are part of those supply chains, the SEC has underestimated the number of small businesses that would be impacted by the Proposed Rule."

The NAM's estimate is corroborated by an October 2011 Tulane University study, which using an independent model in conjunction with the consulting, IT and auditing communities, concluded the cost would be $7.9 billion.

A further report, done by Claigan Environmental, estimated the cost at $800 million. However, as related to the SEC by the NAM's and IPC's analysis of that report, it appears seriously understated. The principal reason for the underestimate is their belief that virtually all companies can use the EICC-GeSI template to comply with the Final Rule. The template is being developed by and for electronics firms that have simpler supply chains and are closer to the smelters than diversified manufacturers. In discussion with NAM member companies, most large companies say they would be unable to use the simple EICC-GeSI template, which is based on an Excel spreadsheet. Companies with thousands of suppliers through many tiers, and hundreds of thousands, if not millions, of parts would need a much more robust system to trace and track minerals, should the SEC require them to do so. Anecdotal evidence supplied by NAM member companies based on their own discussions with external auditors and consultants suggest that audit costs alone for a large company could exceed Claigan's estimates by orders of magnitude.

This, according to Claigan, is the biggest difference between its estimate and the much larger estimates of the NAM and Tulane University. Claigan has not discussed with a range of NAM members whether they can use the EICC-GeSI template. Had they done so they would have found that most large companies would have told them no.

Second, the Claigan estimates are based on an assumption of an average supply chain of hundreds of companies (apparently based on discussions with two companies). As noted in my statement above, the actual number appears to be 7,000, and the NAM's economic estimate was conservatively based on an estimate of 2,000. The costs and complexities of compliance with such larger supply chains are much more formidable than estimated by Claigan.

Additionally, much of Claigan's cost estimate is based on estimates of the cost of complying with the European Union's Reduction of Hazardous Substances (RoHS) regulations. RoHS, prohibits the uses of lead, mercury, cadmium, and three other substances, and it is not an overwhelming problem to conduct physical or chemical tests to determine whether those substances are present. Determining not only what is in the product, but also where the metals and ores came from is hugely more expensive – metals don't have a fingerprint identifying their origin.

Nevertheless, the NAM also cited the RoHS costs in our submission to the SEC, noting an average cost per company for initial compliance being $2,640,000. Were that to be the cost for complying with the Final Rule, that implies $16 billion for all nearly 6000 affected issuers.

The Claigan report also assumes static supply chains, claiming that once a supplier chain is validated, that validation is good forever. In truth, NAM member company supply chains are dynamic, always changing as companies seek more efficient suppliers or suppliers with better components.

Another difficulty with the Claigan report is that it states that contractual changes will not be needed as companies ask their suppliers to comport with the SEC's Final Rule, since most supply contracts already state that the supplier must be in conformity with all its legal obligations. The problem here is that since most suppliers are not listed companies, they have no obligation to the Final Rule, and contracts will have to be renegotiated. As contracts tend to be multi-year, and come up for renewal at different periods, this is a major problem.

Additional comments appear in the attachments to my statement. But the bottom line, is that based on discussions with actual manufacturers, the Claigan report severely underestimates the likely cost.

Conclusion

My testimony today has highlighted three aspects of the SEC's Proposed Rule that are of compelling importance, but there are additional issues as well. These include:

Recycled Material -- Recycled material, both industrial as well as post-consumer scrap, should not be treated as if it originated from the DRC or adjoining countries. Doing so would ignore the very nature of recycled materials and undermine a growing trend to use recycled materials to reduce manufacturers' footprint on the environment. Information available to us indicates that recycling accounts for 30-40 percent of U.S. demand for the four metals at issue when including industrial and post-consumer sources.

We believe use of recycled metals should be encouraged, to reduce the demand for minerals that would support armed groups in the DRC and adjoining countries. This could be accomplished by providing that after a manufacturer conducts a reasonable inquiry into the source of its conflict minerals no further action is required if the metals originated from a scrap or recycled source. The burdens of carrying out extensive due diligence to determine that the materials are indeed recycled, the burden of filing a "Conflict Minerals Report," and the burden of providing for expensive third party audits should not be imposed on recycled materials because there is no discernible benefit from doing so. To encourage recycling, it is imperative that products produced from recycled materials be classified as "DRC Conflict Free" in the same manner as products produced from newly mined minerals known to be from areas other than the DRC and surrounding countries.

De Minimis – A *de minimis* standard is important to balance the costs and benefits of the rule and to prevent manufacturers from having the impossible task of tracking trace amounts of minerals. For most products, a quantity of a material must reach a certain threshold before it is possible to identify its actual presence in a part or component.

10-K – The legislation does not specify that issuers should disclose their use of conflict minerals in their annual reports filed on Form 10-K. Rather the legislation only requires that issuers "to disclose annually whether the conflict minerals did originate in the DRC or adjoining countries." Issuers whose conflict minerals did originate from the DRC or adjoining countries must "submit to the Commission a report." Given the already-formidable time requirements and size of most companies' 10-K forms, issuers should be allowed to disclose to the SEC by furnishing a separate disclosure to the SEC.

Thus, in conclusion, we believe that the impact and cost of the regulation necessitate narrowly tailoring the requirements, acknowledging the current lack of infrastructure, taking a practical and rational approach to the requirements, differentiating between issuers who "don't know" the origin after reasonable inquiry from those that do nothing to establish origin, and supporting a phased-in approach to the disclosure requirements that requires increasingly more detailed disclosure as infrastructure comes online and supply chains become more transparent.

Thank you, Mr. Chairman.

Attachments

NATIONAL ASSOCIATION OF Manufacturers

Stephen Jacobs

Senior Director
International Economic Affairs

February 10, 2012

The Honorable Mary L. Schapiro
Chairman
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

RE: Cost Estimates for Section 1502 of the Dodd-Frank Act (Conflict Minerals)

Dear Chairman Shapiro:

I am writing in response to the January 17, 2012 and other submissions made by an environmental consulting company, Claigan Environmental of Ontario, Canada, concerning the expected costs of implementation of the "Conflict Minerals" rule pursuant to section 1502 of the Dodd-Frank Act. The National Association of Manufacturers' (NAM) member companies with experience in many different markets believe the Claigan submission is misleading on several levels. Since it suggests that the cost estimates provided by the NAM and Tulane University "should be disregarded," we offer our views on some of those criticisms.

To support its assertions, Claigan cites eight conflict minerals policy statements issued by leading electronics or information technology firms. Claigan extrapolates from those limited statements to conclude the "vast majority" of reporting issuers are following the Electronics Industry Citizenship Coalition/Global e-Sustainability Initiative (EICC/GeSI) process. That is simply not correct, as the vast majority of NAM members are awaiting the final SEC regulation before developing full compliance programs – as one would expect when the SEC requirements remain unknown. NAM members have pointed out that:

1. The EICC/GeSI format was designed by and for *electronic industry* supply chains. While we admire and appreciate the leadership shown by EICC/GeSI, electronics industry supply chains – as opposed to other industries - generally have fewer suppliers and tiers. Electronic industry product lines also tend to be more focused, making it somewhat easier to identify relevant suppliers and ultimately product origin. The same cannot be said of other industrial and consumer markets, many of which have complex supply chains with more suppliers and numerous tiers. Many NAM members have parts numbers that are counted in the ***millions***. The EICC/GeSI approach can be cumbersome and difficult to apply outside relatively concentrated electronic industry supply chains.

   For that reason firms in other sectors have not yet endorsed the EICC/GeSI protocol and process. In some cases, those firms require different industry-specific supply chain verification. Accordingly some NAM member firms will follow the EICC/GeSI protocol for their electronics industry customers but will be developing different protocols for other sectors based on the unique conditions of those supply chains.

2. The EICC/GeSI conflict-free smelter certification program is still very much a work in progress. Only 11 tantalum smelters are listed in the EICC database; no other conflict minerals smelters have been certified as conflict-free to our knowledge.

3. Further, the NAM estimate was driven by information provided by its membership and therefore does indeed reflect "actual processes implemented by companies" from industries as varied as aircraft, machine tools, and chemicals. Conflict mineral due diligence costs incurred by some member firms are already substantial, even prior to full implementation of a due diligence program that takes into account the final SEC rule once issued. One NAM member firm reported it faces a significant IT investment for supplier communication and record keeping and annual due diligence costs in over 40 business units and 65 countries.

4. The argument that the Tulane Study does not mention “country of origin” is circular. What constitutes a “reasonable country of origin” inquiry is central to the underlying cost/benefit analysis. The Tulane Study pointed out that previous SEC and NGO cost estimates failed to consider the expensive steps many firms – especially those outside the electronics industry – face in trying to satisfy such a standard. Moreover, Claigan does not address costs that may occur if the SEC does not provide an exception for trace levels of these minerals – or at least an intentionally added standard – in the final rule. The cost of tracking and reporting trace levels of these minerals for many thousands of products could be considerable.

5. NAM believes Claigan is understating the compliance cost burden for small businesses in reporting issuer supply chains. Claigan states it has quoted small business compliance cost programs “at ~ 3% of the cost…they have publicly reported”. That raises several questions: (a) Are those firms exclusively or primarily in the electronics industry with its more focused supply chains? (b) Is this based on a representative sampling of all small businesses potentially affected by the rule? (c) How could these quotes meet all compliance requirements in the absence of a final SEC rule? Where supply chains include millions of parts and numerous supply tiers, small businesses in tiers closer to the finished product will incur considerable cost tracking the origin of 3T or gold used in their components through numerous upstream tiers. As the Small Business Administration Office of Advocacy noted in its October 25, 2011 letter to the SEC, “*Because the SEC does not take into account the complexity of supply chains and the number of small businesses that are part of those supply chains, the SEC has underestimated the number of small businesses that would be impacted by the proposed rule.*”

6. Claigan's seven-step process is unrealistic for many manufacturers, especially large manufacturers with complex supply chains. The seven-step process overlooks a number of issues and necessary tasks, and consequently Claigan's quotes are unrealistically low (at least for larger manufacturers). An Excel spreadsheet (such as the EICC-GeSI Conflict Free Reporting Template) to collect information for a supply chain with millions of part numbers is unrealistic. Nor has the spreadsheet offered by EICC-GeSI been proved or validated for conflict minerals data collection in other than the electronics industry.

7. No standard audit protocol is currently available for validating supplier information in terms of conflict minerals (this internal "audit" appears to be required under the OECD Guidelines, which are not even mentioned in Claigan's process). It is unrealistic to believe that corporate officers would provide the SEC with a report based merely on suppliers information derived from a software template like the EICC/GeSI template.

8. Employee training costs, outside legal counsel, and contract modification also seem not to have been considered by Claigan. Elsewhere, Claigan states, “[T]he legal notices that go out in year one will not need to be sent in successive years,” but fails to account for the frequent changes in suppliers and product composition that many companies implement to remain competitive. Supplier contracts do not all begin and end at once, and may extend for three to five years or more.

Thank you for the opportunity to provide these additional views.

Sincerely,

Stephen P. Jacobs

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February 14, 2012

The Honorable Mary L. Schapiro
Chairman
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

RE: Cost Estimates for Section 1502 of the Dodd-Frank Act (conflict minerals)

Dear Chairman Shapiro:

IPC – Association Connecting Electronics Industries is writing in response to the January 17, 2012 and previous submissions made by Claigan Environmental of Ontario, Canada (Claigan), concerning the expected costs of implementation of the "Conflict Minerals" rule pursuant to section 1502 of the Dodd-Frank Act. IPC believes Claigan's submission is misleading and inaccurate. We believe Claigan's cost estimates are based on a number of erroneous assumptions and are not representative of costs likely to be experienced by companies affected by the aforementioned regulations.

IPC apologizes for the late nature of this letter but is nevertheless providing these comments in the hopes that you will not base any part of your rulemaking decisions on the misleading and inaccurate Claigan submissions.

October 28, 2011 Claigan Report

This initial submission is the basis for all future Claigan submissions. The number of errors in this initial submission cast doubt on the usefulness of this and future Claigan submissions.

Claigan wrongly assumes a direct cost comparison between electronics companies' burden in complying with the European Union Restriction on Hazardous Substances (RoHS) Directive and affected industries' burden in complying with the proposed conflict minerals regulations. Although conflict minerals regulations do not include the technical challenges of materials' substitutions, the challenges related to compliance with the proposed conflict minerals regulations will likely exceed those of compliance with the EU RoHS Directive. While the EU RoHS Directive compliance requires knowledge about the presence/absence of substances in products, conflict minerals legislation requires companies to trace the source of the minerals in their products all the way back to the smelter. Many of the easiest and simplest ways of assuring compliance with the EU RoHS Directive involve non-invasive scanning of a product by X-ray

fluorescence (XRF).[1] There is no corresponding simple "check" for conflict minerals compliance – thus necessitating supplier audits which Claigan Environmental has omitted from their estimate. Although supplier audits are not required by the SEC, they would likely be conducted by any company required to report to the SEC due to the penalties associated with incorrect statements on SEC filings. It is highly unlikely that a CEO/President of a company would sign off on an SEC filing where the information was taken from a supplier letter or form without any verification of its completeness.

Further Claigan's citation of RoHS compliance costs of 0.8% of revenue is factually incorrect and misleading. The EU study referenced by Claigan estimates compliance costs to be between 1 and 2% of "turnover."[2] A second study, conducted by the Consumer Electronics Association (CEA), which was also referenced by Claigan, cites RoHS compliance cost of 1.1% of industry revenue.[3] This average also neglects the significantly higher impact on Small and Medium Enterprises (SMEs), estimated at 5.2% of turnover[4] in the EU study and approximately 5.5% by CEA for $5M-$10M companies.

Claigan makes several additional incorrect assumptions in this study that are carried over to future studies, tainting all subsequent conclusions:

1. Claigan grossly understates the breadth of industry sectors impacted. The statement, "an argument can be put forward that 3TG reporting will be required by more than just the electronics supply chain" is an understatement. Also, they cite the CEA study on RoHS for an estimate of 90,000 electronic OEM, component suppliers and EMS. This estimate is an incomplete assessment of the impacts of the RoHS Directive as it omits PCBs, wire and cable, raw materials, and a number of other sectors that were affected by RoHS.

2. Claigan goes on to reduce its erroneous estimate of impacted companies by an additional 50 percent. This reduction is based on the completely unsupported assumption about the number of suppliers impacted by the regulations. In their estimate Claigan states, "But for conservative purposes it seems fair to reduce this number by at least 50%." It is entirely unclear what is fair or conservative and why or how they chose to reduce the estimate of affected companies by 50 percent.

3. The proposed rules would require issuers to file and have audited a conflict minerals report for all recycled materials in their supply chain, yet Claigan assumes this is not the case by stating, "The [cost estimates] would also change drastically if the final rules issued by the SEC….brings 3TGs in recycled material into scope."

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[1]European Commission, Study on RoHS and WEEE Directives N° 30-CE-0095296/00-09. March 2008, p. 107.
[2]Consumer Electronics Industry, Economic Impact of the European Union RoHS Directive on the Electronics Industry, 21 January 2008, Executive summary p. III.
[3]Study on RoHS and WEEE Directives N° 30-CE-0095296/00-09. March 2008.
[4]Consumer Electronics Industry, Economic Impact of the European Union RoHS Directive on the Electronics Industry. 21 January 2008 p. 123.

4. Claigan makes the erroneous assumption that no legal changes are needed as existing, standard supplier contracts contain standard provisions requiring suppliers to comply with relevant laws. Claigan overlooks the fact that these provisions would not cover conflict minerals as the suppliers (unless they are also SEC issuers) have no legal compliance obligation. Supplying their customers (the issuers) with information may be necessary to the issuer's compliance, but the law places no legal obligation on the supplier and therefore would not be covered by existing contract clauses.

5. Claigan states, "There is no reasonable basis for the cost of the software for conflict minerals to be more expensive." Tracing the source of minerals as opposed to presence/absence of a metal (as in the EU RoHS Directive) may indeed require more sophisticated software, especially as this virtual supply chain must be auditable, another requirement that RoHS does not have.

6. Claigan's faulty assumption that, "the legal notices that go out in year one will not need to be sent in successive years," fails to account for the frequent changes in suppliers that many companies experience in order to maintain competitive pricing. Supplier contracts do not all begin and end at once, and may extend for three to five years or more. Employee training costs, outside legal counsel, and contract modification also appear to not be considered by Claigan.

7. Claigan's assumption that training will be minimal fails to account for employee turnover.

December 1, 2011 Claigan Report

This submission is vague and entirely non-transparent regarding its information sources. Claigan states that the basis for their reduced cost estimates was derived, "during budgeting discussions with affected corporations." Claigan does not specify what types of companies (what industry, size, etc.) were queried, how many companies were queried or what size the companies were. Additionally, indication of the size, representativeness or a statistical significance of the sample population is not provided, raising significant doubts regarding the validity of the submission.

Significant errors in this submission include the following:

1. Regarding estimated audit costs, Claigan states, "This section is not our area of primary expertise and we welcome costing input from 3rd party auditors," and then reduces previous third party audit costs by 1/3.

2. Claigan reduces the ridiculously low $100 per supplier data gathering costs even further to $40 based on "entry into the market of professional data providers." No providers are identified or referenced, nor is IPC aware of any. Again, Claigan fails to mention supplier audit needs.

3. Claigan again naively claims that companies have only hundreds, not thousands of affected suppliers. This assessment is based on supplier lists from a mere 2 companies – a statistically insignificant number which cannot begin to represent the breadth of affected companies.

December 16, 2011 Claigan Report

Significant errors in this submission include the following:

1. Claigan states that their cost to quote of $228,000 is worst case, stating, "228K is higher than most service quotations being issued for complete conflict minerals program." No further information on these quotes is provided (i.e. who made them or what they include). Furthermore, since final regulations have yet to be issued, one must regard skeptically any service quotes for a "complete program."

2. Claigan further reduces the estimate of affected suppliers again, stating that companies have overestimated the number of affected suppliers by a factor of 5 to 10. They base this reduction on, "Careful inspection of actual bills of materials from a cross sample of companies." No information about the number, size or type of this "cross sample" is provided. Furthermore, bills of material are usually for individual products, not all the products a company may make.

3. Claigan incorrectly states that the Tulane Study[5] heavily references the NAM Study[6] when in actuality; the Tulane Study cites IPC numbers, uses their own cost model, and compares their costs to NAM.

January 17, 2012 Claigan Report/ NAM's Recent Comments

1. Claigan makes the outlandish and unsupported claim that their previous estimate of supply chain costs should be reduced because, "vast majority" of reporting issuers are using the EICC/GeSI template. This claim of "vast majority" of reporting issuers appears to be based on examination of conflict minerals policy statements issued by eight electronics firms. This assumption is simply not correct, as the vast majority of affected companies are awaiting the final SEC regulations before developing full compliance programs. Claigan's submission further misrepresents the EICC/GeSI template by calling it a "standard," when in fact it was created, reviewed, and approved by a small group of consumer electronics companies and their suppliers and in no way represents an industry standard. While some companies have chosen to use the EICC/GeSI template,

[5]Tulane University Law School Payson Center for International Studies, A Critical Analysis of the SEC and NAM Economic Impact Models and the Proposal of a 3rd Model in view of the Implementation of Section 1502 of the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act

[6]National Association of Manufacturers (NAM). *Comments submitted to the SEC.* March 2, 2011. http://www.sec.gov/comments/s7-40-10/s74010-212.pdf

the majority of companies are displeased with the format and have not committed to using it.

2. The EICC/GeSI conflict free smelter (CFS) certification program does not yet constitute a reliable source of conflict-free conflict minerals. Only 11 smelters - all tantalum smelters have been certified as conflict free smelters - no smelters of the other three conflict minerals have been certified as conflict free to our knowledge. Furthermore, the 11 smelters identified as conflict-free are outside the DRC region, thus forcing those relying on the CFS program to enforce a "de-facto" embargo on the DRC.

3. The argument that the Tulane Study does not mention "country of origin" is circular. What constitutes a "reasonable country of origin" inquiry is central to the underlying cost/benefit analysis. The Tulane Study pointed out that previous SEC and NGO cost estimates failed to consider the expensive steps many firms - especially those outside the electronics industry - face in trying to satisfy such a standard. Moreover, Claigan does not address costs that may occur if SEC does not provide an exception for trace levels of these minerals - or at least an intentionally added standard - in the final rules. The cost of tracking and reporting trace levels of these minerals for many thousands of products could be considerable.

4. By focusing on statements from large electronics industry firms, Claigan completely ignored the burden and compliance costs that small businesses in reporting issuer supply chains will incur.

5. Claigan's seven-step process is unrealistic for many manufacturers, especially large manufacturers with complex supply chains. The seven-step process overlooks a number of issues and necessary tasks, and consequently Claigan's quotes are unrealistically low (at least for larger manufacturers). As noted above, the idea that large manufacturers of complex parts with millions of part numbers, could rely upon an excel spreadsheet (such as the EICC-GeSI Conflict Free Reporting Template) to collect, organize, and store information for a large supply chain of is unrealistic. Nor has the spreadsheet offered by EICC-GeSI been proven or validated for conflict minerals data collection except by a small subset of electronics manufacturers.

6. There is no standard audit protocol currently available for validating supplier information in terms of conflict minerals (this internal "audit" appears to be required under the OECD Guidelines, which are not even mentioned in Claigan's process). It is unrealistic to believe that corporate officers would provide the SEC with a report based merely on suppliers information from a form derived from a software template like EICC/GeSI.

Finally, it would be instructive to know who or what organization "asked [Claigan] to make a further detailed submission…." While of course the IPC is not a disinterested party in this matter as it will affect the vast majority of IPC members, neither is Claigan. It stands to receive business

as a result of SEC regulations through its consulting services designing company compliance programs.

If you have any questions or wish to discuss this further please do not hesitate to contact me.

Sincerely,

Fern Abrams
Director, Government Relations and Environmental Policy