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COLLECTING INFORMATION IN THE GOLD INDUSTRY

The gold business is some 3000 years old—and throughout that time, it has been split into the visible business and the other one—the one that believes gold is for bribing the border guard.

In the visible part, you have bullion banks, traders, refiners and processors. You also have an array of consumers, such as jewelers, the electronics industry, automobile manufacturers and pharmaceutical companies that have specialized quality requirements.

- The visible part of the business is governed by the Bank Secrecy Act's anti-money laundering customer due-diligence standards. So the regulatory framework and management systems are already in place.
- Their business is leveraged and relies on a range of financial institutions—banks, futures brokers, traders, insurance companies—so it keeps good records.
- The business is intensely competitive and profit margins are minuscule. These companies have no choice but to be customer oriented.

Other than the bullion banks, there are only a few precious metals companies that report to the SEC. But they will bend over backwards to accommodate their customers, many of whom do come under SEC regulation. They can be counted on to gather the information and produce the records that their customers need to comply with the law.

The less-visible gray market is a different world. It operates informally and flies under the regulatory and tax radar. The functions of the legitimate market are mirrored in the gray market. For every bullion bank, there are hundreds of unregistered money service businesses, cambios and hawaladars. Gold is easy to refine if you aren't fussy about purity or the environment. So for every refiner that invests millions in environmental abatement, there are hidden operations refining with mercury, cyanide or aqua regia. For every secondary processor/refiner, there are thousands of small collectors that deal in cash or exchange scrap for refined metal. Record-keeping is minimal. There is no customer loyalty, and if a buyer asks too much, there are hundreds of other outlets. The gray market will not be a reliable source of information.

The gray market is an important raw material source for the legitimate market. At the points they meet, the volume of metal exchanged is large, and the transfers are complicated.

But ultimately, because of quality standards, the gold used by companies under SEC regulation passes through legitimate refiners, and to a lesser extent through secondary processors. They are the ones best situated to document and track supplies to their origins.

The refiners—and the legitimate part of the gold business—are working actively with the OECD and the EICC. Industry groups such as the London Bullion Market Association, the Responsible Jewellers Council and the World Gold Council will all issue due-diligence guidelines that include third party audits.

Unlike the other conflict metals, gold is a monetary commodity. Its market is unique, complex and very mature. If the regulations are to be realistic, I do hope the commission adopts these industry initiatives in guiding the industry.

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RESPONSES TO QUESTIONS

1. Recycled metals should be exempt from coverage. Gold-bearing scrap is many steps removed in the supply chain from the DRC. Gold in scrap may have been remelted dozens of times, and no militia group in the DRC will benefit from the buying, selling or refining scrap.

   The scrap refining process is characterized by layers of collectors and processors—often more than one at each stage—and eventually ends with a refiner. Each stage involves consolidation and further processing and blending. At each stage, identity of the upstream supplier's gold is lost. The process of identifying upstream suppliers is likely to dead-end at the gray market described in my statement.

2. One of my co-panelists alluded to the possibility that DRC gold might be secreted into a scrap refining lot in the United States. This would be unlikely and uneconomic:
   a. **Unlikely** because, of the roughly 4000 tons of gold produced annually worldwide, approximately 2500 tons is mined gold, of which the DRC produces six to ten tons. The bulk of the DRC's gold, and that of the adjoining countries, is shipped via well-established trade routes to the United Arab Emirates and refined in Dubai. Most is fabricated for shipment to India and the Mid East. Following this well established trade route, shippers can count on receiving a fair market price for their gold. So there is no reason to think that meaningful quantities of DRC gold find their way to United States consumers.
   b. **Uneconomic** because the highest grades of scrap refined in substantial volume in the United States are jewelry scrap, of which 14 karat and 18 karat represent the overwhelming majority. 14 K jewelry is 58% gold; 18 K is 75%. DRC gold is nearly always above 80% in purity and routinely above 90%. To blend DRC gold into a jewelry scrap lot would mean debasing the DRC gold by blending it with a lower grade of far more complex material. Compared to the proven solution of shipping to Dubai, the result would be higher refining charges, higher freight rates, longer transportation time and slower payment.

3. In selecting a guidance standard, as suggested in my statement, I would urge the SEC to consider the work of the specialized groups in the gold industry. The London Bullion Market Association, World Gold Council and Responsible Jewellers Council understand the complexities in their respective sectors. Attention to their recommendations will avoid unenforceable regulations and misdirected efforts.

   I believe I misspoke when I said the OECD gold guidance would be published soon. It appears publication is at least a few months away.

4. Existing gold inventories should be grandfathered and exempted. Only newly mined gold should be the subject of due diligence. Remelted fine gold should be exempted along with scrap. Gold is a monetary commodity and a store of value, so it is very different from the other Conflict Minerals. In the case of tungsten, tantalum and tin, carryover stocks in years of surplus production are consumed the next year, and aboveground stocks might be a few months supply. In the case of gold, world production is roughly 4000 tons a year, whereas aboveground stocks are over 165,000 tons. It is held in national stockpiles, bank vaults, private vaulting companies, personal safes and secret caches all over the world. Determining the provenance of this gold would be a gargantuan task—and futile because if ever there was a benefit to DRC militias, it was remitted months, years—perhaps decades ago.