RILA
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VIA ELECTRONIC FILING

March 16, 2017

Mr. Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Response to Acting Chairman Piwowar's January 31, 2017, Statement on the Commission's Conflict Minerals Rule and Request for Comments on Need for Relief Under the Conflict Minerals Rule

Dear Secretary Fields:

The Retail Industry Leaders Association (RILA),[1] submits this letter in response to the January 31, 2017 statement by Acting Chair Piwowar and the Securities and Exchange Commission's ("SEC's" or "Commission's") request for public comments regarding potential reconsideration of the Commission's Conflict Minerals Rule,[2] which implemented specific disclosure requirements of Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Section 1502" or "Dodd-Frank Act")[3] and whether any additional relief under the Commission's 2014 Guidance[4] is appropriate.

I. Introduction

The years-long armed conflict amongst various competing factions in the Democratic Republic of the Congo (DRC) and the surrounding region has had tragic consequences resulting in misery, poverty and harsh living conditions for local populations. In 2010, to eliminate one of the sources of funding for the armed militias, Congress enacted Section 1502 of the Dodd Frank Act. The underlying goals of Section 1502 and the Conflict Minerals Rule subsequently issued by the SEC were two-fold: 1) prevent money from the sale of specific minerals (i.e., tin, tantalum, tungsten and gold or "3TGs" or "conflict minerals") from funding armed conflict in the DRC and surrounding region through disclosure reporting; and 2) thereby, improve the living conditions of Congolese and neighboring populations. RILA members reaffirm their strong commitment to the goals of Section 1502 and their support for reasonable and effective efforts to address the humanitarian crisis within the DRC and surrounding region. Sadly, as detailed below, the current Conflict Minerals Rule is neither reasonable, and, most importantly, nor has it been effective in achieving its goals of improving the living conditions of the Congolese and preventing the mining of 3TGs from being a source of funding of armed conflict in the region.

The scope of the Conflict Minerals Rule is unreasonable in two aspects. First, it applies to all filers regardless of their position in global supply chains. Thus, it applies to companies that are directly

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[1] RILA is the trade association of the world's largest and most innovative retail companies. RILA members include more than 200 retailers, product manufacturers, and service suppliers, which together account for more than $1.5 trillion in annual sales, millions of American jobs and more than 100,000 stores, manufacturing facilities and distribution centers domestically and abroad. RILA member contributions to the overall economic well-being of local, national and international economies are unparalleled.
[2] Conflict Minerals Rule, 77 Fed. Reg. 56,274, (Sept. 12, 2012) (codified at 17 C.F.R. § 240.13p-1).
[3] The Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).
[4] U.S. Securities and Exchange Commission, Division of Corporation Finance, Statement on the Effect of the Recent Court of Appeals Decision on the Conflict Minerals Rule (April 29, 2014).

involved in the importation or sourcing of 3TGs and manufacturers that can dictate and trace the source of these raw materials. But, it also applies to retailers despite their position at the end of complex multi-tiered global supply chains. Retailers have little, if any, visibility into, and generally lack practical and cost-effective tools to trace, the location of mines of the 3TGs contained in components of the product they sell. Similarly, retailers have no way to determine whether the original sale of the mineral was used to fund armed conflict in the DRC and surrounding region. Second, the Conflict Minerals Rule contains no *de minimis* exception and requires companies to conduct due diligence to determine whether even *minute trace* amounts of conflict minerals could *potentially* be within products in their inventory.

The cost of implementing and maintaining Conflict Mineral compliance programs is substantial. A 2015 study by Tulane University estimated that issuers had spent a total of $709.7 million as of June 2014 to comply with the Conflict Mineral Rule with each issuer, on average, expending $545,962 to comply.[5] Although some expenses reflected in the Tulane Study include up-front costs, such as new software systems needed to establish a Conflict Mineral compliance program, companies' ongoing compliance costs for annual review and reporting are significant. To require companies so far removed from the targeted mining operations to spend resources on costly compliance operations futilely trying to determine the source of minute amounts of 3TGs in their supply chains is unreasonable.

Given the overly broad application of the Conflict Mineral Rule to all filers regardless of position in global supply chains and the lack of a *de minimis* exception, it is not surprising that the Rule has been ineffective and has failed to provide detailed disclosures regarding the country of origin of 3TGs in products. Two audits of the Conflict Mineral Rule reporting conducted by the U.S. Government Accountability Office ("GAO") have confirmed the failure of the Conflict Mineral Rule to provide valuable reporting.[6] The GAO noted in its most recent report that 51 percent of reporting companies were unable to determine or did not report the country of origin of the 3TGs in their supply chains.[7] After conducting a reasonable country of origin inquiry, the overwhelming majority of reporting companies were unable to confirm the origin of the conflict minerals in their products or whether the sale of the minerals directly or indirectly financed or benefited armed groups in the DRC or surrounding region.[8] Only three percent of reporting companies indicated that they were able to determine whether or not conflict minerals in some of their products financed or benefited armed groups.[9] While the GAO report noted minimal improvement in the number of companies able to make complete disclosures, it is clear based on the small number of companies that have been able to make full disclosures that the Conflict Mineral disclosure requirement has been a failure.

The Conflict Mineral Rule has also failed to accomplish its goals of eliminating revenue from 3TG mining as a source of funding for armed conflict and improving the living conditions of the Congolese and neighboring populations. A 2014 United Nations Report found that armed groups in the DRC continue to profit from mining and minerals trade.[10] The 2014 UN Report also documented serious human

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[5] *See* Dodd-Frank Section 1502: Post-Filing Survey 2014, Chris N, Bayer, PhD, University of Tulane ("Tulane Study").

[6] U.S. Government Accountability Office, SEC Conflict Minerals Rule: Companies Face Continuing Challenges in Determining Whether Their Conflict Minerals Benefit Armed Groups, GAO-16-805, at 9 (Aug. 2016) (quoting 77 Fed. Reg. 56,274) ("GAO 2016 Report"). GAO's finding that companies are unable to determine the source of 3TGS and whether the original sale of the minerals funded armed conflict in consistent with its finding in its 2015 report. *See also*, GAO, SEC Conflict Minerals Rule: Initial Disclosures Indicate Most Companies Were Unable to Determine the Source of Their Conflict Minerals, GAO-15-561 (Washington, D.C.: Aug. 18, 2015). ("GAO 2015 Report").

[7] GAO 2016 Report, p 18.

[8] *Id.*, p 20.

[9] *Id.*, p 21. Again, GAO's 2016 finding is consistent with the prior year's filings. The GAO 2015 Report analyzing 2014 filings found no companies that reported were able to determine whether 3TGs in their products were from the DRC or surrounding region or if the sale of the conflict mineral had financed or benefited armed groups. *Id.*, p 22 fn 35.

[10] Final Report of the Group of Experts on the Democratic Republic of the Congo to the UN Security Council, January 23, 2014, S/2014/42. ("2014 UN Report"). The report noted that armed groups continue to control many of the mining sites for tin,

rights violations, including the recruiting and use of child soldiers, summary executions, sexual violence and the targeting of civilian populations.[11] A 2016 United Nations Report similarly found that armed groups continue to generate significant revenue from the control, taxation or looting of natural resources, including the mining of 3TGs, and that human rights violations continue unabated.[12] And, in its August 2016 Report, the GAO also noted the continuing violence and humanitarian crisis in the DRC and surrounding regions.[13]

II. Recommendations

The Commission is now in the position to address many of the shortcomings and flaws of the current Conflict Minerals Rule. The comments below will focus on several actions the agency can take to make the Rule more effective and to eliminate unnecessary burdens created by the current Rule. We urge the SEC to:

1. Revise of the current Conflict Mineral Rule to be consistent with the statutory language Section 1502 of the Dodd-Frank Act and limit reporting obligations to those companies that manufacture products to Companies that are not true manufacturers and only contract to manufacture products should not be subject to the Rule or required to report;
2. Add a *de minimis* exception to the Conflict Minerals Rule including a process for excepting specific categories of products that meet certain conditions from the reporting requirements under the Rule;
3. Revise the Conflict Mineral Rule to include a safe harbor provision to allow issuers to rely upon defined contract provisions and supplier certifications; and,
4. Work with its interagency partners to develop recommendations for a strategic and holistic approach that will address the humanitarian crisis in the DRC and surrounding region.

Each of these issues is discussed in detail below.

III. Discussion

A. The SEC Should Reconsider the Overly Expansive Scope of the Current Conflict Minerals Rule and Revise it to Accurately Reflect the Statutory Requirements of Section 1502 of the Dodd-Frank Act

Congress, in enacting the Dodd-Frank Act, directed the SEC to promulgate a disclosure rule that would cover those who "manufacture" products that could contain 3TGs mined in the DRC or the surrounding region that fund armed conflict.[14] Congress set forth two sequential requirements in Section 1502 of the Dodd-Frank Act. First, 15 U.S.C. §78m(p)(1)(A) and 15 U.S.C. §78m(p)(2)(B) identifies *who* is subject to the rule and the reporting requirements. Paragraph (2)(B) indicates that a person is subject to the rule if "conflict minerals are necessary to the functionality or production of a product *manufactured by* such person." 15 U.S.C. §78m(p)(2)(B) (emphasis added). Second, 15 U.S.C. §78m(p)(1)(A) provides the details of *what* should be disclosed. Specifically, the legislation requires "a description of the products

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tantalum and tungsten. The report did note that many gold mining sites were in post-conflict areas, but found that production from these areas were blended with production from conflict areas. The report cited the lack of transparency in the gold trade makes it difficult to distinguish conflict gold from conflict-free gold.

[11] *Id.*

[12] Final Report of the Group of Experts on the Democratic Republic of the Congo to the UN Security Council, May 23 2016, S/2016/466. ("2016 UN Report")

[13] GAO 2016 Report, Appendix I: Additional Information Available on Rate of Sexual Violence in Eastern Democratic Republic of the Congo and Adjoining Countries since GAO's August 2015 Report.

[14] 15 U.S.C. §78m(p)(2)(B).

manufactured or *contracted to be manufactured* that are not DRC conflict free." *Id.* §78m(p)(1)(A)(ii) (emphasis added). Under the plain language of the statute, a company is subject to the reporting requirement if, and only if, conflict minerals are necessary to the functionality or production of a product that it manufactures.

There are many reasons why it was logical and reasonable for Congress to require manufacturers, and not retailers and other non-manufacturers, to be subject to the disclosure requirements. Global supply chains for finished consumer goods are not transparent or linear. Instead, they are incredibly complex, multi-layered networks that include raw material suppliers (e.g., minerals, chemicals, cotton, wool, wood), commodity markets, recycled material suppliers, raw and recycled material finishers (e.g., smelters, lumber and textile mills), input providers, component producers, Original Equipment Manufacturers ("OEMs"), trading companies, importers, and distributors. Retailers are at the end of this lengthy supply chain in a position immediately prior to the final end-user, the consumer.[15] Furthermore, retailers seldom specify the mineral make-up of the products they order, and instead, rely on the supplier's component manufacturers and their sub-suppliers to determine if, when and how conflict minerals may be necessary in the production of a product. In today's integrated global economy, finished consumer products purchased by retailers are manufactured from raw and recycled materials, inputs, and components sourced and consolidated from multiple countries, multiple entities and through many channels of distribution.

Issuers that manufacture products, or have substantial control over the manufacturing process, material specifications, and raw or recycled materials and components used in the product, are in a position to know the source of any 3TGs used in the products they manufacture and if these 3TGs are from smelted ores or recycled metals. Manufacturers may also be able to directly impact the situation in the DRC and surrounding area by contracting directly with Conflict-Free Smelters. For additional details regarding the legislative history of Section 1502 of the Dodd-Frank Act supporting the position that Congress did not intend to include retailers and other non-manufacturers in the scope of companies required to report, see RILA's prior comments filed to the SEC on October 27, 2010[16] and November 1, 2011,[17] and the amicus brief filed by the Retail Litigation Center in *National Association of Manufacturers, et al. v. Securities and Exchange Commission*, 748 F.3d 359 (D.C. Cir. 2014).[18]

Disappointingly, the SEC conflated Section 1502's two separate and distinct requirements of *who* should report and *what* should be reported in its final Conflict Mineral Rule. Instead of requiring only those companies that manufacture products to file Form SDs, the SEC issued an overly expansive rule not supported by the underlying legislation that imposes burdensome reporting and audit requirements on retailers and other companies that only contract to manufacture. The result is that retailers have incurred significant compliance costs in a futile effort to try to determine whether any of the products they sell potentially contain conflict minerals from the DRC and surrounding region and whether the proceeds of the sale of the mineral helped to fund armed conflict.[19]

The SEC should take this opportunity to undo past errors and revise the current Conflict Mineral Rule to accurately reflect the intended scope of the statute and disclosure requirement – true manufacturers of

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[15] Retailers often act as importers of record for the products they purchase from foreign suppliers to sell to U.S. consumers. This change of position in the global supply chain does not change retailers lack of visibility into and leverage over distant raw material suppliers.

[16] RILA Letter to SEC on Proposed Rulemaking under Section 1502 of Dodd-Frank Act. (October 27, 2010)

[17] November 1, 2011 RILA Letter to SEC on Proposed Rulemaking under Section 1502 of Dodd-Frank Act. *See also* Joint RILA-Consumer Electronics Retailers Coalition (CERC) comments. March 2, 2011.

[18] *See* Brief for Retail Litigation Center as Amici Curiae Supporting Petitioner, *National Association of Manufacturers, et al. v. Securities and Exchange Commission*, 748 F.3d 359 (D.C. Cir. 2014).

[19] GAO 2016 Report, pp 18-22.

products that contain conflict minerals.[20] Revision of the Conflict Minerals Rule to accurately reflect the party specified under the Dodd-Frank Act will limit the disclosure requirements to those parties (i.e., manufacturers) that are in the best position to determine the source of 3TGs in their supply chains and file accurate and complete disclosures and will relieve retailers and other non-manufacturer filers of the unnecessary costs and burdens imposed under the current Rule.

B. The Conflict Mineral Rule Should be Revised to Include a *De Minimis* Exception and a Process for Eliminating Categories of Products from the Rule's Reporting Requirements

In addition to limiting the scope of the Rule discussed above, the Commission can take other actions that will relieve the burdens of the current Conflict Mineral Rule on filers without undermining the original goals of the Dodd-Frank Act. Specifically, the SEC can revise the current Conflict Minerals Rule to include a *de minimis* exception and develop a process for eliminating categories of products that meet specific conditions from the Rule's reporting requirements. Despite numerous comments during the rulemaking process requesting that a *de minimis* exception be included in the final rule, the SEC declined to do so. Rather than taking a reasonable approach when implementing Section 1502, the SEC chose instead to draft an unnecessarily burdensome rule, which triggers disclosure reporting obligations from "even minute or trace amounts of conflict minerals."[21] The SEC's position on the coverage of products that use a conflict mineral as catalyst during the manufacturing production process is a perfect example of the SEC's overreach in this area. The final Rule includes products made with a conflict-mineral catalyst if "traces" of the catalyst are not fully "washed away" and remain in the product.[22] In taking this overly broad and ultimately unreasonable approach, the SEC readily acknowledged that its failure to include a *de minimis* exception "will be more costly for issuers."[23] In addition to the resulting increased cost to filers, it is clear that the absence of a *de minimis* exception has hindered companies from providing full and complete reporting disclosures.[24]

RILA urges the SEC to uses its inherent exemptive authority to revise the Conflict Mineral Rule to add a *de minimis* exception. Such an approach was advocated by former SEC Commissioner Daniel M. Gallagher at the time the rule was originally published. In fact, Commissioner Gallagher argued that it was "unreasonable" for the Commission not to consider such an exemption.[25] The rationale articulated then by Commissioner Gallagher in favor of a *de minimis* exception still rings true today. Companies whose use of conflict minerals is *de minimis* are burdened with significant compliance costs while their compliance with the rule "could have, at most, a small and indirect impact, if any, in ameliorating the problem – a negligible benefit."[26]

Ideally, the Commission would define a *de minimis* exception so that products that use a minimal amount of 3TGs would not have to report. At a minimum, the *de minimis* exception should eliminate requirements for products that have minute or trace amounts of 3TGs. A *de minimis* exception also could exclude products based upon a defined value of the amount of those products sold by the filer. For example, if a filer sold only $10,000 (or another reasonable amount determined by the SEC) worth of product that could potentially contain 3TGs in that filing period, the filer would not be required to

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[20] Any revision of the Conflict Minerals Rule would also require a corresponding revision of the SEC's 2014 Guidance.

[21] 77 Fed. Reg. 56297-98.

[22] *Id.*, 56297 fn 236. In light of the technological and logistical challenges of determining whether "trace" amounts of a conflict mineral remain in a final product, companies taking a conservative approach to Conflict Mineral compliance will include all products manufactured with a conflict-mineral catalyst as a covered product for reporting purposes, thereby greatly increasing overall compliance costs.

[23] *Id.*, 56298.

[24] GAO 2016 Report, pp 18-22.

[25] Statement of former SEC Commissioner Daniel M. Gallagher (August 22, 2012).

[26] *Id.*

conduct due diligence or file a report on that product. A filer that makes minimal purchases of a product is very unlikely to be directly engaged with the smelter or know the origin of the 3TGs in that product. Defining a *de minimis* exception in this way would relieve compliance burdens for impacted filers while maintaining disclosure requirements for companies most able to provide robust reporting.

Also as part of a *de minimis* exception, the Commission should develop a process by which specific product categories that meet certain conditions can be exempted from the Rule's reporting requirements. There are some categories of products for which the likelihood of conflict minerals being present is remote. If a conflict mineral is present in a product in one of these categories, it is always in a *de minimis* amount. Requiring companies to include all product categories in their annual Conflict Mineral compliance review, even those categories where the potential presence of a conflict mineral is unnecessary and burdensome. Developing a process by which specific product categories could be exempted from the Rule's reporting requirements would eliminate unnecessary costs and help improve overall Conflict Mineral Reporting. A few examples of some product categories that should be considered for a product category exclusion include apparel, footwear, and soft home products. As the SEC moves forward with its reconsideration of the Conflict Minerals Rule, retailers would welcome the opportunity to work with the SEC to develop an effective *de minimis* exception and to develop and implement a process for product category exemptions.

C. The Conflict Mineral Rule Should be Revised to Include a Safe Harbor Provision

Another action that the SEC can take that would provide immediate relief to filers is to revise the current Conflict Minerals Rule to include a new safe harbor provision. In today's global supply chains, many companies are far removed from the sourcing and purchase decisions regarding 3TGs used in products, and therefore, have limited visibility into and leverage over distant supply chain tiers. Filers do have visibility into and the ability to impact first-tier suppliers and, in some instances, second-tier suppliers.[27] In turn, these suppliers have visibility and the ability to impact their first and second tier suppliers. This process is repeated again and again throughout the supply chain until it reaches the smelters and, ultimately, the mining operations for 3TGs. Under a safe harbor provision, companies could use defined procurement practices, including specific conflict mineral commitment contract language requiring first-tier suppliers to obtain similar commitments from their suppliers, and reasonable reliance upon supplier certifications, to comply with the Rule without also being subject to burdensome and impractical reporting and audit requirements.

Such an approach is consistent with other voluntary efforts and legislation that has sought to address human rights issues where the behavior or concern that is targeted is remotely removed from retailers and importers (e.g., the use of forced and child labor in the harvesting of cotton[28] and the mining of specific minerals or gems[29][30]). RILA members urge the SEC to take a practical approach to the issue of conflict minerals that recognizes companies' limited reach beyond first-tier suppliers and revise the current Conflict Mineral Rule to include a safe harbor provision.

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[27] For example, retailers along with leading brands have taken the initiative to work with their first-tier suppliers to develop robust social compliance programs related to labor and employment requirements and appropriate health and safety standards for workers in factories that manufacture products purchased and sold by retailers. These voluntary programs are effective in large part because retailers can proactively engage with their first-tier suppliers, the factories that they directly contract with. Retailers have very limited ability to engage with distant suppliers of 3TG mineral ores or recycled 3TG material.

[28] *See* Cotton Campaign on Uzbekistan Forced Labor; *see also* Coalition Letter to U.S. State Department

[29] *See* Earthworks "No Dirty Gold" Campaign (featuring retailers pledging to encourage "cleaner" sourcing of metals)

[30] *See* Responsible Jewelry Council Chain of Custody Certification Program

D. The SEC Should Work with its Interagency Partners to Develop Recommendations for a Strategic and Holistic Approach that will Effectively Address the Humanitarian Crisis in the DRC and Surrounding Region

The clear intention of Section 1502 of the Dodd-Frank Act was to use disclosure requirements to cut off one source of funding for armed conflict in the DRC and neighboring countries and help address the humanitarian crisis in the region. However, implementation of the Conflict Mineral Rule has failed to provide valuable disclosures for investors.[31] Additionally, the Conflict Mineral Rule has failed to eliminate mining of 3TGs as a source of funding for armed militia and not eased the humanitarian crisis in the DRC and surrounding region.[32] Over the past couple of years, there has been increased recognition by concerned stakeholders, Congress,[33] and most recently the new Administration[34] that now is the time to take a new approach to address this issue.

We urge the Commission to work with its interagency partners to conduct a comprehensive review of the Conflict Minerals Rule to determine its real-world impact, including any unintended consequences of the Rule. The goal of this interagency group should be to develop recommendations for a strategic and holistic approach that could include diplomatic and trade initiatives, as well as legislative and regulatory changes necessary to reasonably and effectively achieve Section 1502's intended goals. Part of this effort should include a review of approaches that other countries and international organizations have taken to address this issue.[35][36] Harmonization of U.S. requirements with international requirements will result in a more coordinated approach to the humanitarian crisis in the DRC and neighboring countries and will help U.S. companies better compete in today's global market place by reducing costs and increasing efficiencies.

IV. Conclusion

RILA appreciates the opportunity to comment on the SEC's reconsideration of the Conflict Minerals Rule. We respectfully request that the Commission adopt our recommendations to revise the Rule to limit its scope to true manufacturers consistent with the statutory language of the Dodd-Frank Act. RILA further urges the SEC to take the actions noted above to minimize the burdens imposed upon filers and improve the disclosure reporting.

Please do not hesitate to contact me if you have any questions or need any additional information.

Respectfully submitted,

Kathleen McGuigan
Senior Vice President & Deputy General Counsel

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[31] See, GAO 2016 Report.

[32] See, 2016 UN Report.

[33] In 2016, two bills were introduced in Congress that would defund or repeal Section 1502 of the Dodd-Frank Act. H.R.5485, the Financial Services and General Appropriations Act would defund the SEC's implementation and enforcement of the Conflict Minerals Rule. H.R.5983, The Financial CHOICE Act would repeal Section 1502.

[34] Andrea Vittorio, "Conflict Minerals Latest Disclosure Rule Targeted for Rollback," Bloomberg BNA, February 10, 2017.

[35] Organisation for Economic Co-operation and Development, OECD (2016), OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas: Third Edition, OECD Publishing, Paris.

[36] *See* European Commission, "EU reaches landmark agreement on conflict minerals regulation."