



Executive Office for Administration & Finance

COMMONWEALTH OF MASSACHUSETTS

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July 11, 2017

Walter F. Timilty, Senate Chairman
Joint Committee on State Administration and Regulatory Oversight
Room 213-B – State House
Boston, MA 02133

Peter V. Kocot, House Chairman
Joint Committee on State Administration and Regulatory Oversight
Room 22 – State House
Boston, MA 02133

William F. Welch, Senate Clerk
Office of the Clerk of the Senate
Room 335 – State House
Boston, MA 02133

Steven T. James, House Clerk
Office of the Clerk of the House
Room 145 – State House
Boston, MA 02133

Re: Report of the Executive Office for Administration and Finance to the Clerks of the Senate and House of Representatives pursuant to Chapter 5 of the Resolves of 2016, Resolve Examining Commonwealth Procurement Policies Relative to Congo Conflict Minerals.

Dear Chairman Timilty, Chairman Kocot, Senate Clerk Welch and House Clerk James:

The Executive Office for Administration and Finance (“A&F”) is pleased to submit this Report on the Examination of Commonwealth Procurement Policies relative to Congo Conflict Minerals pursuant to Chapter 5 of the Resolves of 2016 (the “Resolve”). A&F consulted with the Office of the Inspector General and we welcomed their input during the drafting of the Report. The Resolve contained the following provision:

...the executive office for administration and finance, in consultation with the inspector general, shall review the procurement policies of the commonwealth and issue a report (Emphasis added.) that analyzes existing policies relative to products that may contain extracted mineral resources from the Democratic Republic of the Congo and its adjoining countries. The report shall: (i) examine best practices to ensure that electronics and information communications technology suppliers provide products that: (A) do not directly or indirectly finance armed conflict or result in labor or human rights violations in the Democratic Republic of the Congo or an adjoining country; (B) contain minerals, including columbite-tantalite, cassiterite, wolframite, gold and other similar or derivative minerals, for which the origin and exporter can be identified; and (C) contain raw materials for which the appropriate tax payments have

been made; (ii) examine the efficacy and implications of penalties or a trade prohibition for businesses that are required to disclose information relating to conflict minerals originating in the Democratic Republic of the Congo or an adjoining country under section 13(p) of the Securities Exchange Act of 1934 and for which a disclosure report is not filed, the disclosure does not comply with said section 13(p) because it was considered under said law to be an unreliable determination or contains false information; and (iii) identify actions, including legislative recommendations, if any, necessary to support mineral exporters from the Democratic Republic of the Congo or an adjoining country that fully discloses their export payments and certifies that their minerals do not directly finance armed conflict, result in labor or human rights violations or damage the environment.

The report shall be filed with the clerks of the senate and house of representatives and the senate and house chairs of the joint committee on state administration and regulatory oversight not later than July 1, 2017. (Emphasis added.)

A&F welcomes efforts to help curb conflict, systemic human rights and labor violations in the Democratic Republic of Congo. We will continue to seek input from all stakeholders as we work to implement this important Resolve.

If you have any questions or need any additional information, please feel free to contact Gary Lambert at the Operational Services Division.

Sincerely,



Kristen Lepore, Secretary
Signed by Gary Lambert, Assistant Secretary for Operational Services/Chief Procurement Officer
Executive Office for Administration and Finance
State House, Room 373
Boston, Massachusetts 02133

CC: Inspector General Glenn Cunha

To: Clerks of the Senate and the House of Representatives and the Senate and House Chairs of the Joint Committee on State Administration and Regulatory Oversight

On February 2, 2017, *Resolve examining commonwealth procurement policies relative to Congo conflict minerals*, Chapter 5 of the Resolves of 2016, was signed by Governor Baker. The Resolve requires the Executive Office of Administration and Finance, in consultation with the Office of the Inspector General, to review state procurement policies and examine best practices in ensuring that the Commonwealth's electronics and information technology suppliers provide products that do not directly or indirectly finance armed conflict or result in labor or human rights violation in the Democratic Republic of Congo or a neighboring country. See S 2463. Specific directives of the Resolve are as follows:

1. Review the procurement policies of the commonwealth, and
2. Issue a report that analyzes existing policies of the commonwealth relative to products that may contain extracted mineral resources from the Democratic Republic of the Congo and its adjoining countries. The report shall:
 3. Examine best practices to ensure that electronics and information communications technology suppliers provide products that:
 - i. Do not directly/indirectly finance armed conflict or result in labor or human rights violations in the Democratic Republic of the Congo or an adjoining country;
 - ii. Contain minerals, including columbite-tantalite, cassiterite, wolframite, gold and other similar or derivative minerals, for which the origin and exporter can be identified; and
 - iii. Contain raw materials for which the appropriate tax payments have been made.
 3. Examine the efficacy and implications of penalties or a trade prohibition for businesses that are required to disclose information relating to conflict minerals originating in the Democratic Republic of the Congo or an adjoining country under section 13(p) of the Securities Exchange Act of 1934 and for which a disclosure report is not filed, the disclosure does not comply with said section 13(p) because it was considered under said law to be an unreliable determination or contains false information; and
 4. Identify actions, including legislative recommendations, if any, necessary to support mineral exporters from the Democratic Republic of the Congo or an adjoining country that fully discloses their export payments and certifies that their minerals do not directly finance armed conflict, result in labor or human rights violations or damage the environment.
- I. Overview of Procurement Standards Utilized to Discourage/Prohibit Use of Congo Conflict Minerals

We welcome the Legislature's Resolution to help curb conflict and systemic human rights violations in the Democratic Republic of Congo. The Congo Conflict is funded in part by mining operations by militias in the region. This resolution builds upon efforts undertaken to improve the rule of law and promote peace and stability in the Congo Region by seeking to discourage the procurement of products that may, through the raw materials supply stream, facilitate ongoing conflict in the region.

Current procurement policies for goods and services do not incorporate standards or requirements with respect to Congo Conflict minerals at the state level. Further, we are unaware of any other public entities in the Commonwealth that have adopted procurement standards or requirements on this topic.

Prohibitions and standards concerning products containing Congo conflict minerals represent an emerging area in public procurement. There is limited experience with development and enforcement of standards on this topic. The most widely recognized and applied standard is Section 13(p) of the Securities and Exchange Act of 1934, which is summarized in greater detail below. We have also provided a brief overview of other public procurement requirements specific to Congo Conflict minerals. To date, only two other states have enacted legislation specific to Congo Conflict Minerals; in both instances, the federal standard is utilized for purposes of determining compliance.

1. Dodd-Frank Wall Street Reform and Consumer Protection Act

Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act¹ ("Dodd-Frank Act") enacted in July of 2010 requires manufacturers and issuers to disclose their use of defined "conflict minerals" in their products or production processes. Section 1502 of the Dodd-Frank Act amends the Securities and Exchange Act of 1934 by adding Section 13(p) requiring companies to be compliance with the provisions of section 1302 of the Dodd-Frank Act. The Dodd-Frank Act applies to all SEC foreign and domestic "issuers" that manufacture or contract to manufacture products where "conflict minerals are necessary to the functionality or production" of a product. The covered area of this provision includes the Democratic Republic of Congo and its adjoining countries of Central Africa Republic, South Sudan, Zambia, Angola, The Republic of Congo, Tanzania, Burundi, Rwanda, and Uganda. Conflict minerals are columbite-tantalite, cassiterite, gold, wolframite, and their derivatives tantalum, tungsten, and tin. These minerals can be included electronics, aerospace, automotive, jewelry, and industrial products among others.

a. Applicability

For purposes of SEC compliance, issuers are anyone who manufactures products or contracts to manufacture products. To be considered an issuer, the entity must (1) possess a degree of control over the manufacturing process that is equivalent to the manufacturing of the product,

¹ The Dodd-Frank Act, Pub. L. 111-203 § 1502, 124 Stat. 1376 (2010).

(2) affix its brand or logo to a generic product that was manufactured by a third party, or (3) service, maintain or repair a product.²

b. Required Disclosures

The Dodd-Frank Act outlines a three-step disclosure process for companies using conflict minerals:

Step 1: The issuer must determine if their products contain conflict minerals. For each product that uses conflict minerals, the conflict minerals must be necessary for the functionality of the product or necessary to the production process.

Step 2: The issuer then must determine if its necessary conflict minerals originated in a covered country. The issuer must conduct a “reasonable country of origin inquiry.” While the process is not enumerated, the end result must be “reasonably designed to determine whether any of the conflict minerals that are not from recycled or scrap sources originated in the covered in countries in good faith.” If the issuer knows or has reason to believe the conflict minerals originated in a covered country then it must proceed to step 3. If the conflict mineral is not in a covered area, the issuer must provide a Special Disclosure Form (“Form SD”) describing how it came to this conclusion.

Step 3: An issuer must conduct Due Diligence and potentially provide a Conflict Minerals Report (“CMR”). The Due Diligence Report must be based on a nationally or internationally recognized due diligence framework. A commonly used framework is provided by the Organisation for Economic Cooperation and Development (“OECD”). The OECD is an international intergovernmental organization that promotes economic development as it relates to social and environmental issues with 35 member-states including the United States. If the minerals are found to be conflict minerals, then the issuer must provide a conflict minerals report.

c. Due Diligence

The Due Diligence Proceedings from the OECD are the most common Due Diligence process followed by companies fulfilling the Dodd-Frank Act. This Due Diligence process has a five part process.³

Part 1: Establish strong company management systems which include a policy for responsible mineral supply chains and a traceability system for the supply chain.

² See Pub. L. 111-203 § 1502(b)(p)(2)(A-B). See also (a) (8) 15 U.S.C.S. § 78c (LexisNexis, Lexis Advance through PL 115-39, approved 6/6/17). See also ERNST & YOUNG, CONFLICT MINERALS: WHAT YOU NEED TO KNOW ABOUT THE NEW DISCLOSURE AND REPORTING REQUIREMENTS AND HOW ERNST & YOUNG CAN HELP (2012) (providing overview of Frank-Dodd Act for affected companies).

³See ORG. FOR ECON. COOPERATION & DEV., OECD DUE DILIGENCE GUIDANCE FOR RESPONSIBLE SUPPLY CHAINS OF MINERALS FROM CONFLICT-AFFECTED AND HIGH-RISK AREAS (2d ed. 2013) Available at: <http://www.oecd.org/corporate/mne/GuidanceEdition2.pdf>

Part 2: Identify and assess risks in the supply chain

Part 3: Manage risks which include a plan to monitor progress, track performance of risk mitigation process, and a creation of a strategy for measurable risk mitigation.

Part 4: Identify points in the supply chain that need to have third-party audits of supply chain due diligence

Part 5: Publicly report on Due Diligence by making the progress on step- 1-4 available on annual basis.

d. Data Concerning Conflict Minerals Submissions

At the beginning of enactment of the Dodd-Frank Act, the SEC estimated that roughly 600 Form SDs and 4500 CMRs would be filed by companies on an annual basis. The actual number of filings was substantially lower than estimated, at 1319 Form SD filings and 1020 CMR filings in 2015. Roughly 93% of semiconductor producers and 83% of automobile parts producers submitted filings. It was common for company filings to be incomplete or short, thus failing to meet the requirements of the Form SDs and the CMRs. About 80% of companies describe their due diligence processes following the OECD guidelines.⁴

2. *State of Maryland*

The Disclosure of Conflict Minerals Originated in Democratic Republic of Congo⁵ was passed in October of 2012 and applies to the state of Maryland's government procurement. This law follows the same terminology and applicability as section 1502 of the Dodd-Frank Act. A noncompliant person is someone that failed to disclose information under federal law relating to conflict minerals per Section 1502. If a person is noncompliant, they would be barred from public procurement with the state of Maryland. Any party interested in procurement that uses conflict minerals must show proof that they are in compliance with section 1502 of the Dodd-Frank Act.

3. *State of California*

In October of 2011, California passed SB 861 which stated that any company not in compliance with Section 13(p) of the Securities Exchange Act of 1934 because of failure to disclose under section 1302 of the Dodd-Frank Act will not be eligible for state contracts for goods or services.⁶ The law follows the same applicability and scope as the Dodd-Frank Act.

4. *Cities and Private Entities*

⁴ See Jeff Schwartz, *The Conflict Minerals Experiment*, 6 HARVARD BUS. L. REV. 129, 144 & 162-63 (2016).

⁵ Disclosure of Conflict Minerals Originated In Democratic Republic of Congo, Md. Code Ann., State Fin. & Proc. § 14-413 (2011).

⁶ Conflict Minerals Law, 2011 Cal Stats. Ch. 715.

A variety of other entities have taken steps to discourage use of Congo Conflict Minerals. For instance, Pittsburgh (Pennsylvania) and St. Petersburg (Florida) both issued proclamations in 2011 against the use of conflict minerals.⁷ These proclamations do not carry the same weight a law holds.

Several private entities have voiced their support for the conflict minerals rule enumerated in section 1302 of the Dodd-Frank Act including Apple, Intel, Tiffany & Co., and Brandeis University.⁸

5. *European Union*

The most recently established standard pertaining to Congo conflict minerals is the European Union's ("EU") recently promulgated Conflict Minerals Regulation.⁹ That regulation differs in scope somewhat from Section 1502 of the Dodd-Frank Act. It involves any entity in the trade of tin, tantalum, tungsten, and gold. The regulation focuses on both conflict-affected and high risk areas as opposed to solely the Congo and its adjoining countries. The EU has taken a phase-in approach and the regulation will not go into effect until the beginning of 2021. At this time, all EU importers of the concerned minerals will have to carry out a due diligence process on their supply chain in order to determine if their materials have been mined in a conflict free zone.

The EU regulation will apply to:

- i. Areas in a state of armed conflict, or
- ii. Fragile post-conflict areas, or
- iii. Areas with weak or non-existent governance and security, such as failed states; and
- iv. In all cases, areas with widespread and systematic violations of international law, including human rights abuses.

II. *Potential Changes to Federal Reporting Requirements*

The SEC partially stayed compliance with the rule pertaining to conflict minerals after a May 2014 US Court of Appeals ruling that it violated the First Amendment in regards to the rule's requirement that companies disclose on their company website and to the SEC that their products are not DRC Conflict Free.¹⁰ In January 2017, Acting Chairman Piwowar directed SEC staff to reconsider whether the 2014

⁷ See KPMG, CONFLICT MINERALS... DOES COMPLIANCE REALLY MATTER? ASK CALIFORNIA, AUSTRALIA, AND THE EU, (2012).

⁸ See Washington Post, *Why Apple and Intel don't want to see the conflict minerals rule rolled back*, February 23, 2017. See *Procurement and Business Services: Conflict Minerals and electronic Procurement*, Brandeis University

⁹ See Official Journal of the European Union 2017 O.J. (L 130) *Regulation (EU) 2017/821 of the European Parliament and of the Council of 17 May 2017 laying down supply chain due diligence obligations for Union importers of tin, tantalum, and tungsten, their ores, and gold originating from conflict-affected and high risk areas.*

¹⁰ Nat'l Ass'n of Mfrs. v. SEC, 419 U.S. App. D.C. 158 (2015). A federal court case in 2015 ruled that Section 13 (p) of the Securities Exchange Act of 1934 "violates the first amendment to the extent the statute and rule require regulated entities to report to the Commission and to state on their website that any of their products have 'not been found to be 'DRC Conflict Free.'"" The court reasoned, in part, because the government failed to show that

guidance on the conflict minerals rule is still appropriate and whether any additional relief is appropriate. In doing so, Piwowar cited the concern that the current Dodd-Frank disclosure requirements have created a “de facto boycott of minerals from portions of Africa....” SEC invited public comment for a 45 day period, but has not yet indicated what changes are under consideration. Most recently, in June 2017, The House of Representatives passed the Financial CHOICE Act which would serve as the replacement for the Dodd-Frank Act if it were to pass the senate.¹¹ The current draft does not address the Congo Conflict Minerals issue and it is unclear if and how section 1302 would be affected.¹²

III. Findings Concerning Federal Reporting Requirements

A recent U.S. Government Accountability Office¹³ report analyzed company disclosures filed with the SEC regarding conflict minerals. For 2015, that report indicates that a majority of companies were unable to determine the country of origin for conflict minerals in their products and whether such minerals benefited or financed armed groups in the covered countries. The report further indicated that the content of forms submitted is often incomplete due to either the inability of the manufacturer to pinpoint the source along its supply chain, or a general disregard to the requirements of the disclosure forms. Companies did, however, report actions that had been undertaken or planned to improve due diligence efforts. Furthermore, companies not subject to the Dodd-Frank Act are often pressured by customers and other groups to comply with the rule.¹⁴

Currently, issuers who do not file required disclosures with section 13(p) of the Securities Exchange Act of 1934 are charged \$100 per day.¹⁵ This has little deterrent effect on larger companies while it could have a more substantial effect on small, medium sized, and minority-owned companies. Furthermore, small, medium sized, and minority owned companies may have much more difficulty being able to identify the source of their products or to bear compliance costs necessary to comply with reporting requirements.

IV. Conclusion and Recommendations

Because this is an evolving area, there is no uniform certification process or standard widely in use by companies seeking to demonstrate that their products are not sourced with conflict minerals. In developing any rule that applies to the procurement process, we are mindful of potential impacts on the

the rule would alleviate the harms asserted. This does not apply to any other disclosures required by the Dodd-Frank Act.

¹¹ Evan Weinberger, *House Passes Bill Overhauling Dodd-Frank*, LAW 360, (June 8, 2017).

¹² See generally Financial CHOICE ACT, H.R. Res. 10, Bill 115th Cong. (April 26, 2017).

¹³ U.S. Government Accountability Office, *SEC Conflict Minerals Rule: 2017 Review of Company Disclosures in Response to the U.S. Securities and Exchange Commission Rule*, April 26, 2017.

¹⁴ See Matthew W. Geekie, Graybar, *Impact of Dodd-Frank Section 1502- Conflict Mineral Rule on Graybar Electric Company, Inc.*, (March 14, 2017)(highlighting shortcomings of Dodd-Frank Act). Graybar, an electronic distribution company, is not subject to Section 1502. However, since many of its customers are subject to Section 1502, Graybar find themselves having to adhere to Section 1502 to satisfy their customers' requirements.

¹⁵ See Schwartz, *supra* note 4 at 162.

competitive bidding process. In particular, existing procurement policies and programs strongly encourage participation in public contracting by small and diverse businesses. Any standard would have to be drafted with consideration of the diverse business pool and the potential burden imposed on small/diverse businesses in determining compliance. For example, local product resellers may not have information on this topic, and likely have no real ability to influence the sourcing decisions of manufacturers; thus, a standard simply prohibiting sale of non-compliant products could present a barrier for these types of businesses.

The most readily available standard to monitor compliance with the intent of this Resolve would be section 13(p) of the Securities Exchange Act of 1934. However, given the current reconsideration by the SEC of the filing requirements pertaining to conflict minerals, it would be preferable to (1) await further action by the SEC concerning the current reporting requirements, and (2) investigate how any modified SEC rule could impact existing and prospective vendors. Additionally, it is not clear at this point how the EU standard may impact industry compliance, but given the phased approach, that compliance protocol will not be mature for a number of years.