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CONFLICT MINERALS LEGISLATION: THE SEC'S NEW ROLE AS DIPLOMATIC AND HUMANITARIAN WATCHDOG

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Buried in the voluminous Dodd-Frank Wall Street Reform and Consumer Protection Act is an oft-overlooked provision requiring corporate disclosure of the use of "conflict minerals" in products manufactured by issuing corporations. This Article scrutinizes the legislative history and lobbying efforts behind the conflict minerals provision to establish that, unlike the majority of the bill, its goals are moral and political, rather than financial. Analyzing the history of disclosure requirements, the Article suggests that the presence of conflict minerals in an issuer's product is not inherently material information and that the Dodd-Frank provision statutorily renders nonmaterial information material. The provision, therefore, forces the SEC to expand beyond its congressional mandate of protecting investors and ensuring capital formation by requiring issuers to engage in additional nonfinancial disclosures in order to meet the provision's humanitarian and diplomatic aims. Further, the Article posits that the conflict minerals provision is a wholly ineffective means to accomplish its stated humanitarian goals and likely will cause more harm than good in the Democratic Republic of the Congo. In conclusion, this Article proposes that a more efficient regulatory model for conflict minerals is the Clean Diamond Trade Act and the Kimberly Process Certification Scheme.

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INTRODUCTION

Buried in the voluminous Dodd-Frank Wall Street Reform and Consumer Protection Act[1] (Dodd-Frank) is an oft-overlooked provision requiring corporate disclosure of the use of "conflict minerals" in products manufactured by issuing corporations.[2] This provision, section 1502 of the Act, requires the Securities and Exchange Commission (SEC) to enforce and regulate corporate disclosures on the use of certain minerals originating from the Democratic Republic of the Congo (DRC) or one of its neighboring countries.[3] Although the thrust of Dodd-Frank concerns banking regulations and other measures focusing on the regulation of financial institutions,[4] the legislative history of section 1502 reveals that

1. Pub. L. No. 111-203, 124 Stat. 1376 (2010) (codified as amended in scattered section of the U.S. Code).

2. § 1502, 124 Stat. at 2213 (codified at 15 U.S.C. § 78m(p) (Supp. V 2011)). "Conflict mineral" is defined in the Act as "(A) columbite-tantalite (coltan) [also known as tantalum], cassiterite [also known as tin ore], gold, wolframite [also known as tungsten], or their derivatives; or (B) any other mineral or its derivatives determined by the Secretary of State to be financing conflict in the [DRC] or an adjoining country." § 1502(e)(4)(A)–(B).

3. *See* § 1502. Because of the porous borders of the war-torn DRC and the ease with which smugglers and traders can transport the conflict minerals to the surrounding nations, the Act includes restrictions on exports from DRC's neighboring countries. *Id.* Neighboring countries include Angola, Burundi, Central African Republic, Republic of the Congo, Rwanda, South Sudan, Tanzania, Uganda, and Zambia.

4. Dodd-Frank was signed into law on July 21, 2010, by President Obama. *See* Status of H.R. 4173 (111th): Dodd-Frank Wall Street Reform and Consumer Protection Act,

Congress included it in the Act due to congressional concern about the continuing humanitarian crisis in the DRC.[5] As will be discussed in depth

GOVTRACK.US, http://www.govtrack.us/congress/bills/111/hr4173 (last visited Nov. 16, 2012). The aim of the legislation was the enactment of financial regulatory reform in response to the recent financial crisis. The Act consists of sixteen titles and drastically changed the existing financial regulatory structure. Title I is the Financial Stability Act of 2010 and creates the Financial Stability Oversight Council (FSOC), tasked with monitoring systemic risk in the U.S. financial system. *See* § 111. The FSOC identifies gaps in regulations that pose a threat to financial stability and efficiency. *See* § 112. Title I also creates the Office of Financial Research, tasked with data collection from bank holding companies and nonbank holding companies. *See* § 152. Title II relates to the liquidation authority ascribed to the Federal Deposit Insurance Corporation and the Securities Investor Protection Corporation. *See* §§ 201–217. Title III, the Enhancing Financial Institution Safety and Soundness Act of 2010, abolishes the Office of Thrift Supervision in an attempt to streamline regulation authorities between different regulators. *See* §§ 312–313. Title IV is the Private Fund Investment Advisors Registration Act of 2010 and is intended to increase regulation of hedge funds. *See* §§ 401–416. Title V consists of the Federal Insurance Office Act of 2010 and the Nonadmitted and Reinsurance Reform Act of 2010. *See* §§ 501–527. Title VI is the "Bank and Savings Association Holding Company and Depository Institution Regulatory Improvements Act of 2010" and includes the Volcker Rule, which limits the ability of banking entities to hold more than three percent of total ownership interest in hedge funds or private equity funds. *See* §§ 601, 619. Title VII is the Wall Street Transparency and Accountability Act of 2010 and regulates over-the-counter swaps markets, including credit default swaps and derivatives. *See* §§ 701–774. Title VIII is the Payment, Clearing, and Settlement Supervision Act of 2010, which increases regulation of clearing and settlement activities done by financial institutions. *See* §§ 801–814. Title IX is the Investor Protections and Securities Reform Act of 2010, which restructures the regulatory powers of the SEC and implements additional regulations on broker-dealers, credit rating agencies, and those offering asset-backed securities and municipal securities. *See* §§ 901–991. Title X is the Consumer Financial Protection Act of 2010 and establishes the Bureau of Consumer Financial Protection. *See* §§ 1001–1100H. Title XI deals with the additional governance and oversight the Act provides to the Federal Reserve System. *See* §§ 1101–1109. Title XII, or the Improving Access to Mainstream Financial Institutions Act of 2010, allows certain organizations to provide incentives to low- and middle-income participants in the financial system. *See* §§ 1201–1210. Title XIII is the Pay It Back Act, which amends the Troubled Asset Relief Program (TARP) by limiting the amount of funds available and prohibiting unused funds from being used for any new programs. *See* §§ 1301–1306. Title XIV is the Mortgage Reform and Anti-Predatory Lending Act, which establishes standards for mortgage loan organizations and appraisers. *See* §§ 1401–1498. Title XV, where the conflict minerals provision is located, is simply deemed "Miscellaneous Provisions" and includes other nonfinancial provisions such as requirements to report on mine safety, requirements to report on payments by oil, gas, and mineral extractors, and additional evaluations required of the International Monetary Fund for loans to various countries. *See* §§ 1501–1506. Finally, Title XVI deals with section 1256 Contracts of the Internal Revenue Code that deals with tax implications for futures contracts, foreign currency contracts, or nonequity options. *See* § 1601.

5. *See* § 1502(a) ("It is the sense of Congress that the exploitation and trade of conflict minerals originating in the [DRC] is helping to finance conflict characterized by extreme levels of violence . . . and contributing to an emergency humanitarian situation therein . . . ."). Congress initiated section 1502 as a result of the actions of a few Senators, particularly Senator Brownback. *See* Edward Wyatt, *Congo Minerals Provision Becomes Part of Financial Bill*, N.Y. TIMES, May 22, 2010, at B8. Beyond the personal convictions of Senator Brownback and other Congressmen, the effort to pass legislation that attempts to quell the violence in the DRC has been actively supported by nonprofit groups such as the Enough Project, Global Witness, Resolve, and Friends of the Congo. *See* Letter from Fr. Rocco Puopolo, Exec. Dir., Africa Faith & Justice Network, et al., to Russ Feingold, U.S.

below, section 1502 is not a "financial" regulation, but rather a provision aimed at ending the atrocities of a war occurring seven thousand miles from Wall Street. In fact, the prologue of section 1502 expressly declares:

> It is the sense of Congress that the exploitation and trade of conflict minerals originating in the Democratic Republic of the Congo is helping to finance conflict characterized by extreme levels of violence in the eastern Democratic Republic of the Congo, particularly sexual- and gender-based violence, and contributing to an emergency humanitarian situation therein, warranting the provisions of section 13(p) of the Securities Exchange Act of 1934, as added by subsection (b).[6]

The eastern region of the DRC has been embroiled in one of the deadliest conflicts since World War II.[7] Fueled by decades of ethnic tensions, the conflict in the region reached a tipping point when groups of militiamen fled across the border into the DRC following the 1994 genocide in Rwanda.[8] Although not the underlying cause of the war, mineral resources in the region supply the funding necessary for local rebel militias to continue the fight.[9] Four minerals in particular have played an integral part

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Senator (Nov. 30, 2010), *available at* http://opensocietypolicycenter.org/wp-content/uploads/Senator-Russ-Feingold-thank-you1.pdf.

6. § 1502(a).

7. *See* Nicholas D. Kristof, Op-Ed, *Death by Gadget*, N.Y. TIMES, June 27, 2010, at WK11. The conflict in the DRC has claimed the lives of over 5.4 million people. *Id.*

8. Mary Beth Sheridan, *Trying To Curb Trade of "Conflict Minerals*,*"* WASH. POST, July 21, 2010, at A1. The history of ethnic tensions in the region does not begin with the Rwandan genocide in 1994. Rather, ethnic battles have plagued Congo for over a century. *See Forever in Chains: The Tragic History of Congo*, INDEPENDENT (July 28, 2006), http://www.independent.co.uk/news/world/africa/forever-in-chains-the-tragic-history-of-congo-409586.html#. Originally colonized in 1885 by Belgian King Leopold II, the DRC achieved independence from Belgium in 1960 but was ruled for the following thirty years by the authoritarian regime of Mobutu Sese Seko. *Id.* In 1997, Laurent Kabila toppled Mobutu's regime, but the country was thrown into civil war, during which rebel groups took over various regions of the DRC. *Id.* Kabila was assassinated in 2001 and power shifted to his son, Joseph Kabila, under whose reign the fighting has not ceased. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-12-763, CONFLICT MINERALS DISCLOSURE RULE: SEC'S ACTIONS AND STAKEHOLDER-DEVELOPED INITIATIVES 5 (2012), *available at* http://www.gao.gov/assets/600/592458.pdf [hereinafter GAO REPORT] ("As we reported in 2010, illegal armed groups and some Congolese national military units are consistently and directly involved in human rights abuses against the civilian population in eastern DRC and are involved in the exploitation of conflict minerals and other trades. We also reported that there is a culture of impunity in eastern DRC in which those who have committed human rights abuses do not face justice for the crimes they have committed. After decades of instability and war, the central government in the capital, Kinshasa, currently has little administrative capacity and control over remote regions, including eastern DRC. The long distances between the capital and eastern DRC and the rudimentary infrastructure, which make transportation and communication difficult, further limit the central government's control in eastern DRC.").

9. Shannon Raj, Note, *Blood Electronics: Congo's Conflict Minerals and the Legislation That Could Cleanse the Trade*, 84 S. CAL. L. REV. 981, 985 (2011). In addition to funding rebel militias, conflict minerals are often smuggled over the DRC border to neighboring countries in order to subvert or avoid taxation by the Congolese government. John Prendergast & Sasha Lezhnev, *From Mine to Mobile Phone: The Conflict Minerals Supply Chain*, ENOUGH, 5 (NOV. 10, 2009), http://www.enoughproject.org/files/publications/

in the ongoing violence: tin, tantalum, tungsten—also known as the "3Ts"[10]—and gold. Because these minerals are intrinsically tied to the violence in the DRC, they are referred to as "conflict minerals" and are the subject of section 1502.[11]

Section 1502 requires issuing companies to disclose whether they use any of the minerals included in the "conflict mineral" definition[12] and to locate the source of the minerals they use.[13] Although this may seem like a minor task, mandating disclosure of the origin of the minerals used in products is no small request to make of issuers who are now forced to scrutinize their supply chains. Furthermore, the scope of issuers affected by this legislation is enormous, as thousands of companies manufacture and sell products containing at least one "conflict mineral." For example, the 3Ts can be found in a number of consumer electronic goods, including cell phones and computers, as well as a number of other nonelectronic products such as certain types of packaging or even children's shoes.[14] Likewise, gold is found in jewelry, of course, but can also be found in electric plating and wiring as well as in components for jet engines.[15] The number of industries, let alone individual companies, that section 1502 affects is daunting from a regulation standpoint. Nevertheless, the SEC has been tasked with that regulation, despite never having had to tackle anything remotely similar to date.

This Article will first discuss the history of disclosure requirements mandated by the SEC. Part II will then examine the legislative history of

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minetomobile.pdf. In Uganda, for example, over $74 million worth of gold was exported in 2007 but only $600 worth of gold was produced by the country in that same year. *Id.* Similarly, Rwanda exported upwards of $30 million worth of tin in 2007 but only officially produced $8 million of that amount. *Id.*

10. *See* Prendergast & Lezhnev, *supra* note 9, at 1. According to estimates, the mineral trade generates more than $180 million in profit for armed rebel groups in Congo. Roughly 65 percent of the world's coltan (which can be separated to produce tantalum) reserves are located in the DRC. Press Release, Brownback, Durbin Introduce Conflict Mining Bill (May 23, 2008), *available at* http://votesmart.org/public-statement/359180/brownback-durbin-introduce-conflict-mining-bill#.UGCQeZjK2fQ. *But see* Kristof, *supra* note 7 ("Even the Enough Project, an anti-genocide organization that has been a leading force in the current campaign, estimates that only one-fifth of the world's tantalum comes from Congo.").

11. *See* Dodd-Frank § 1502, 15 U.S.C. § 78m(p) (Supp. V 2011).

12. *See* § 1502(e)(4) (defining conflict mineral as "columbite-tantalite (coltan), cassiterite, gold, wolframite, or their derivatives" or "any other mineral or its derivatives determined by the Secretary of State to be financing conflict in the [DRC] or an adjoining country").

13. *See* § 1502(b).

14. *See* Prendergast & Lezhnev, *supra* note 9, at 1. Cassiterite, or tin, is used by the electronics, automotive, industrial manufacturing, and construction industries as a crucial component in solders for joining pipes and circuits; it is also used in automobile parts, steel plating, and various alloys. MICHAEL LITTENBERG ET AL., SCHULTE ROTH & ZABEL LLP, CONFLICT MINERALS DUE DILIGENCE 4 (2012), *available at* http://www.srz.com/files/upload/Littenberg_Damania_Valane_PLC_Nov_2011_Conflict_Minerals.pdf. Children's shoes that light up upon impact also contain cassiterite. *Id.* at 3. Likewise, columbite-tantalite, or coltan, is used in hearing aids, pacemakers, carbide tools, and jet engines. *Id.* at 4. Wolframite, or tungsten, is used in metal wires, electrodes, and welding instruments. *Id.*

15. LITTENBERG ET AL., *supra* note 14, at 4.

section 1502 and the SEC's final rule implementing the provision. In Part III, this Article will analyze the shortcomings of the new rule, including the costs imposed on affected industries, and the scope of statutory liability for noncompliance with the rule. In Part IV, this Article will show that the regulation and enforcement of section 1502 falls well outside of the SEC's mandate. In doing so, this Article criticizes the efficacy of enacting disclosure requirements for U.S. companies with the aim of exacting a diplomatic and international benefit and demonstrates that the SEC is not the appropriate regulatory agency for accomplishing these diplomatic and humanitarian objectives. Part IV then posits that the legislation will prove meaningless because if a company both uses conflict minerals and complies with section 1502, then there is no real consequence other than mere "naming and shaming." This Part also analyzes the use of section 1502 as an embargo with limited international cooperation that could lead to regulatory arbitrage. Finally, Part V contemplates a different model for regulating conflict minerals using the example of the Kimberley Process and the regulation of conflict diamonds.

I. THE HISTORY OF THE SECURITIES AND EXCHANGE COMMISSION'S DISCLOSURE REQUIREMENTS

The Securities and Exchange Commission was founded in 1934 with the mandate that it would: (a) protect investors; (b) maintain fair, orderly, and efficient markets; and (c) facilitate capital formation.[16] Notably absent from that mandate is any authority or charge to effect international, diplomatic, or human rights-oriented goals. The focus, rather, is preserving market integrity. The hallmark of the first two prongs of the mandate, investor protection and assurance of fair markets, lies in market transparency and is achieved through disclosure of material information to investors.[17] As the SEC states on its own website: "Only through the steady flow of timely, comprehensive, and accurate information can people make sound investment decisions."[18]

A. Legislative History of the 1933 and 1934 Acts

In 1933, in the wake of the stock market crash of 1929 and the Great Depression, Congress passed the Securities Act of 1933 ('33 Act).[19] The

16. *The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, SEC, http://www.sec.gov/about/whatwedo.shtml (last visited Nov. 16, 2012) [hereinafter *The Investor's Advocate*].

17. *See, e.g.*, Basic Inc. v. Levinson, 485 U.S. 224, 230 (1988); *see also* Cynthia A. Williams, *The Securities and Exchange Commission and Corporate Social Transparency*, 112 HARV. L. REV. 1197, 1199–1200 (1999).

18. *The Investor's Advocate*, *supra* note 16.

19. Securities Act of 1933, 48 Stat. 74 (1933) (codified as amended at 15 U.S.C. §§ 77a–77aa (2006)).

House Committee Report accompanying the ’33 Act[20] quotes President Roosevelt in outlining the Act’s purpose: “What we seek is a return to a clearer understanding of the ancient truth that those who manage banks, corporations, and other agencies handling or using other people’s money are trustees acting for others.”[21] The ’33 Act’s primary means of regulating and enforcing accountability of banks and other financial institutions was disclosure. Introducing the ’33 Act on the House floor on May 5, 1933, Representative Sam Rayburn stated:

> [T]oday the owner of shares in a corporation possesses a mere symbol of ownership, while the power, the responsibility, and the substance which have characterized ownership in the past have been transferred to a separate group which holds control. . . . The owners of these symbols are entitled to know what the symbols represent. . . . These managers are truly trustees. One of their duties as trustees is to furnish security owners, in being and in prospect, with reliable information.[22]

The House unanimously adopted Rayburn’s sponsored bill on a voice vote. The House bill became the final version of the bill, which passed the Senate on May 23, 1933, and was signed into law by President Roosevelt on May 27, 1933.[23] A few months later, in February 1934, Senator Duncan Fletcher and Representative Rayburn introduced the Securities Exchange Act of 1934[24] (’34 Act) “for the protection of investors, for the safeguarding of values, and, so far as it may be possible, for the elimination of unnecessary,

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20. The bill was drafted by a team of representatives assembled by Felix Frankfurter that consisted of James Landis, Benjamin Cohen, and Thomas Corcoran, who reported to Sam Rayburn. JOEL SELIGMAN, THE TRANSFORMATION OF WALL STREET 61–63 (3d ed. 2003).

21. H.R. REP. NO. 73-85, at 2 (1933). Professor Williams points out that Roosevelt was highly influenced by the writings of Louis Brandeis and his emphasis on the importance of disclosure in securities regulation. Williams, *supra* note 17, at 1212–14. Indeed, Brandeis is oft-quoted for the saying: “Sunlight is said to be the best of disinfectants; electric light the most efficient policeman.” *Id.* at 1212. Professor Williams also notes that Brandeis greatly influenced Felix Frankfurter, who was instrumental in passing the Securities Act of 1933 and was subsequently appointed to the Supreme Court by Roosevelt. *Id.* at 1221–22.

22. 77 CONG. REC. 2910 (1933) (statement of Rep. Sam Rayburn). In his introduction, Congressman Rayburn relied on a book by Adolf Berle and Gardiner Means, which pointed out the drastically increasing rise in economic power that large corporations enjoyed. *Id.* at 2918 (citing ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (1932)). Berle and Means noted that in large corporations, ownership and control became increasingly separated and that, without adequate accountability, “controllers” could profit from actions that were not in shareholders’ interests. *See* ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 119–25 (1932). Because of this, Berle and Means argued for a shift in management’s fiduciary duties. *See id.* at 220–32. In addition, Berle and Means emphasized that disclosure requirements would promote market efficiency and price discovery, and would act as an additional means of accountability for corporate managers. *See id.* at 317–25.

23. SELIGMAN, *supra* note 20, at 38.

24. 48 Stat. 881 (1934) (codified as amended at 15 U.S.C. §§ 78a–78nn (2006)). The ’34 Act created the SEC and empowered it with broad authority over the securities industry, including the power to require periodic reporting of information by companies with publicly traded securities. *See The Laws that Govern the Securities Industry*, SEC, http://www.sec.gov/about/laws.shtml#secexact1934 (last visited Nov. 16, 2012).

unwise, and destructive speculation."[25] The Senate Committee Report, acknowledging that the individual stock exchanges faced challenges when attempting to increase the amount of information that companies disclosed, made clear that the prerequisite for trading on an exchange would be the "furnishing of complete information relative to the financial condition of the issuer, which information shall be kept up to date by adequate periodic reports."[26] Similarly, the House Committee Report underscored the importance of "honest publicity" in the disclosure of complete and accurate financial statements on a regular basis in order to achieve accurate valuation of securities.[27]

In passing the '33 and '34 Acts, Congress mandated regular material disclosures by companies with publicly traded securities.[28] First, companies must make initial disclosures when new securities are issued to the public.[29] Thereafter, public companies must make periodic disclosures quarterly and annually.[30] Disclosures are also required regarding elections at annual shareholder meetings,[31] as well as when any major corporate event takes place, such as a merger or sale of the business.[32]

B. The Importance of Materiality

The disclosure regime established in the '33 and '34 Acts is intended to be a regulatory mechanism that allows for investor protection and accurate valuations of securities.[33] Disclosure regulations also boost investor confidence and incentivize corporate managers to behave more diligently.[34] To comply with disclosure regulations, publicly traded companies must

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25. 78 CONG. REC. 2264 (1934) (message from President Franklin D. Roosevelt).

26. S. REP. NO. 73-792, at 10 (1934).

27. H.R. REP. NO. 73-1383, at 11–12 (1934).

28. *See* Securities Act of 1933, 48 Stat. 74 (1933) (codified as amended at 15 U.S.C. §§ 77a–77aa (2006)); 48 Stat. 881.

29. *See* Securities Act of 1933, §§ 5, 7, 10.

30. *See* Securities Exchange Act of 1934, §§ 12, 13, 15D.

31. *Id.* §§ 14(f), 15.

32. *Id.* § 14.

33. *See generally* Michael D. Guttentag, *An Argument for Imposing Disclosure Requirements on Public Companies*, 32 FLA. ST. U. L. REV. 123 (2004). Professor Guttentag analyzes the economic and regulatory benefits of imposing additional disclosure requirements on public companies when balanced against the costs of disclosure by private or public firms. *See generally id.* at 132–65. He points out that disclosure requirements can improve share price accuracy, reduce the amount of information to which only managers have access, and reduce agency costs because the more the parties to a transaction are informed, the less they will need a regulator to evaluate the merits of the transaction. *Id.* at 133–35.

34. Susanna Kim Ripken, *The Dangers and Drawbacks of the Disclosure Antidote: Toward a More Substantive Approach to Securities Regulation*, 58 BAYLOR L. REV. 139, 146 (2006) ("The emphasis in securities law on providing information to the public is premised on the belief that individuals are rational, self-governing actors who are willing and able to process the information wisely. If we assume that investors are rational risk calculators who are consistently capable of weighing the costs and benefits of risky alternatives and selecting the best option, then a system of disclosure makes good sense.").

disclose any information considered *material*.[35] The '33 and '34 Acts prohibit the disclosure of any untrue statement of material fact or any omission of material fact.[36] Neither Congress, the SEC, nor the Supreme Court defined "material information" until 1976, when the Court resolved the issue in *TSC Industries v. Northway, Inc*.[37] Specifically, the Court held that a material fact is one that "would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[38] This was generally understood to mean "information that significantly affected a company's financial performance and consequently translated into stock market gains or losses."[39]

In 1988, the Supreme Court reaffirmed this standard of materiality in *Basic v. Levinson*[40] and unanimously held that a bright-line rule regarding what information is considered material is inappropriate and unnecessary.[41] The Court stated that materiality is, as Professor Langevoort described, "about what is important to investors, nothing more and nothing less."[42] Specifically, the *Basic* Court held that a fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote in a corporate election.[43] The Court applied the "probability times magnitude test" for estimating when speculative or forward-looking information is sufficiently important to rise to the level of "material."[44]

Since its *TSC* and *Basic* rulings, the Supreme Court, as well as the SEC through its regulations, has implicitly defined material information as information that bears on the *economic* value of an investment.[45] The

35. *See, e.g.*, Basic Inc. v. Levinson, 485 U.S. 224, 230 (1988).

36. *See* 15 U.S.C. §§ 77k–l, 78j. SEC Rules expanded on this general theory. For example, Regulation S-K sets forth certain information that companies must disclose. 17 C.F.R. § 229 (2012). Likewise, Rule 408 and Rule 12b-20 provide that "there shall be added such further material information, if any, as may be necessary to make the required statements, in light of the circumstances under which they are made, not misleading." *Id.* §§ 230.408(a), 240.12b-20. Failure to comply with these rules can expose a company to Rule 10b-5 antifraud liability. *Id.* § 240.10b-5.

37. 426 U.S. 438 (1976).

38. *Id.* at 449.

39. John M. Fedders, *Qualitative Materiality: The Birth, Struggles, and Demise of an Unworkable Standard*, 48 CATH. U. L. REV. 41, 42 (1998). Fedders points out that in the wake of *TSC Industries*, the SEC attempted to adopt a qualitative, rather than quantitative, standard for materiality and traces the SEC's efforts throughout the 1970s and 1980s to enforce qualitative disclosure. *Id.* at 43. Qualitative disclosure included unadjudicated violations of law, as well as the issuer's or management's antisocial or unethical behavior, regardless of the impact on the issuer's bottom line. *Id.* at 43–44. Fedders concludes that the qualitative standard has since met its demise because "[i]t was a standard that had no standards." *Id.* at 86.

40. 485 U.S. 224 (1988).

41. *Id.* at 249.

42. Donald C. Langevoort, Basic *at Twenty: Rethinking Fraud on the Market*, 2009 WIS. L. REV. 151, 152 (2009).

43. *Basic*, 485 U.S. at 238 (citing SEC v. Tex. Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968)).

44. *Id.*

45. Williams, *supra* note 17, at 1264.

SEC's understanding of the materiality standard is that a reasonable investor "generally focuses on matters that have affected, or will affect, a company's *profitability and financial* outlook."[46] As will be described in more depth below, congressional action since the '33 and '34 Acts has sought to enlarge the scope of the materiality definition to include nonfinancial information, including the issuer's use of conflict minerals as mandated in section 1502.

II. DODD-FRANK SECTION 1502

In 2001, the U.N. Security Council (UNSC), in response to the unending violence and human rights abuses occurring in the DRC, passed a resolution in which it condemned "all illegal exploitation of the natural resources of the [DRC], *demand*[*ed*] that such exploitation cease and *stress*[*ed*] that the natural resources of the [DRC] should not be exploited to finance the conflict in that country."[47] Subsequently, the UNSC called on member states to "take measures, as they deem appropriate, to ensure that importers, processing industries and consumers of Congolese mineral products under their jurisdiction exercise due diligence on their suppliers and on the origin of the minerals they purchase."[48]

Eight years later, in the summer of 2009, Secretary of State Hillary Clinton visited the DRC to encourage the Congolese government and the United Nations to end the violence that is ravaging the country.[49] Secretary Clinton's publicized concerns with the state of affairs in the DRC was not news to then-Senator Sam Brownback, who had already drafted legislation requiring action to alleviate the crisis in the DRC.[50] Senators Richard Durbin and Russ Feingold had also traveled to the DRC and were struck by the deleterious humanitarian situation. Joined by Congressman Jim McDermott, the Senators introduced new legislation to address the crisis.[51]

46. Note, *Should the SEC Expand Nonfinancial Disclosure Requirements?*, 115 HARV. L. REV. 1433, 1434 (2002) (emphasis added) (quoting Memorandum from David B.H. Martin, Dir., Div. of Corp. Fin., SEC, to Laura Unger, Acting Chair, SEC (May 8, 2001)).

47. S.C. Res. 1376, ¶ 8, U.N. Doc. S/RES/1376 (Nov. 9, 2001), *available at* http://www.un.org/ga/search/view_doc.asp?symbol=S/RES/1376(2001).

48. S.C. Res. 1857, ¶ 15, U.N. Doc. S/RES/1857 (Dec. 22, 2008), *available at* http://www.un.org/ga/search/view_doc.asp?symbol=S/RES/1857(2008).

49. *See* Jeffrey Gettleman, *Clinton Presses Congo on Illicit Minerals*, N.Y. TIMES, Aug. 11, 2009, at A7. Of particular concern for Secretary Clinton was the increased violence against women, as she declared, "Women are being turned into weapons of war." *Id.* More than 200,000 rapes were reported since the beginning of the current war in DRC, resulting in eastern Congo being labeled the "rape capital of the world." *See* Margot Wallstrom, *"Conflict Minerals" Finance Gang Rape in Africa*, GUARDIAN (Aug. 14, 2010, 11:00 AM), http://www.guardian.co.uk/commentisfree/2010/aug/14/conflict-minerals-finance-gang-rape. The militant groups have used sexual violence as a war tactic. *Id.*

50. *See infra* notes 54–55 and accompanying text.

51. *See* Press Release, Russ Feingold, U.S. Senator, Feingold Statement on Congo Conflict Minerals and Transparency Amendments to Financial Regulatory Reform Bill (May 19, 2010), *available at* http://www.africafocus.org/printit/mob.php?http://www.africafocus.org/docs10/cgk1007a.php ("This amendment specifically responds to the continued crisis in the eastern region of the [DRC]. Despite efforts to curb the violence, mass atrocities and

The result of the initial efforts by Senators Brownback, Feingold, and Durbin was section 1502, which was added to Dodd-Frank in the Senate during floor debate on the initial Senate version (i.e., the pre-conference-committee version) of the bill.[52] Eventually, Amendment No. 3997, also known as the Brownback Amendment and later section 1502, was confirmed by unanimous consent pursuant to a voice vote.[53]

A. Legislative History and the Evolution of Section 1502

The genesis of section 1502 reveals a great deal about the goals of its drafters. As early as 2008, variations of legislation similar to the Brownback Amendment had been put forth by members of Congress, often by Senator Brownback himself. In May 2008, Senator Brownback introduced a bill in the Senate Finance Committee, which was cosponsored by Senator Durbin, called the Conflict Coltan and Cassiterite Act of 2008 (CCCA).[54] This bill, had it become law, would have made it unlawful to import products from the DRC that contain coltan or cassiterite.[55] At the time of this bill's introduction, Senator Brownback stated in a press release that this legislation was intended to "bring accountability and transparency to the supply chain of minerals used in the manufacturing of many electronic devices."[56]

The CCCA never received a floor vote, and on April 23, 2009, Senator Brownback again introduced legislation, this time in the Senate Banking, Housing, and Urban Affairs Committee, to address the humanitarian crisis in the DRC.[57] The contours of Senator Brownback's subsequently proposed bill, called the Congo Conflict Minerals Act of 2009 (CCMA), were much more closely aligned with the Brownback Amendment. The CCMA took a noted step back from the more aggressive CCCA in that it did not include criminal penalties for willfully violating the CCMA's other provisions.[58] Like the Brownback Amendment, the CCMA would have amended the '34 Act by adding certain disclosure requirements, and it

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widespread sexual violence and rape continue at an alarming rate. Some have justifiably labeled eastern Congo as 'the worst place in the world to be female.' Several of us in this body, including Senators Brownback and Durbin and I, have traveled to this region and seen first-hand the tragedy of this relentless crisis.").

52. *See* 156 CONG REC. S3865–66 (daily ed. May 18, 2010).

53. *See id.*

54. S. 3058, 110th Cong. (2008).

55. *Id.* §§ 3–4.

56. Press Release, Sam Brownback, *supra* note 10.

57. Congo Conflict Minerals Act of 2009, S. 891, 111th Cong. (2009). Similar legislation was proposed in the House of Representatives by Rep. Jim McDermott. *See* Conflict Minerals Trade Act, H.R. 4128, 111th Cong. (2009).

58. *Compare* S. 891, *with* S. 3058. According to Senator Feingold, "[W]e must tread carefully because there are many communities in eastern Congo whose livelihoods are intertwined with the mining economy. All-out prohibitions or blanket sanctions could be counterproductive and negatively affect the very people we seek to help. I am confident that [the CCMA] is sensitive to that complex reality." 155 CONG REC. 10600 (2009) (statement of Sen. Feingold).

would have made it U.S. policy to promote peace and security in the DRC.[59]

Several important differences exist between the reporting requirements mandated by the proposed CCMA and section 1502. For example, the disclosure requirements under section 1502 apply only to those who require conflict minerals for "the functionality or production of a product manufactured by such person."[60] The proposed CCMA, on the other hand, would have applied to persons who engaged in "the commercial exploration, extraction, importation, exportation, or sale of" conflict minerals or use conflict minerals "in the manufacture of a product for sale."[61] Moreover, the CCMA would have applied the disclosure requirements not only to parties that engage in the relevant activities but also to any person who controls another person or entity (defined as controlling 50 percent of the voting stock or capital) that engages in the relevant activities.[62] Conversely, section 1502 applies only to those persons who actually manufacture or contract to manufacture the products.[63] Thus, section 1502's disclosure requirements apply to a substantially narrower group of companies than the CCMA. Nevertheless, this legislation affects companies throughout the entire supply chain because they need to be prepared to respond to due diligence requests from those subject to the disclosure requirements.

Besides the difference in scope, there are several other important differences between the proposed CCMA and section 1502. One important difference is that section 1502 requires an independent audit of the source and chain of custody of the conflict minerals, along with an identification of the auditor, the facilities used to process the conflict minerals, the country of origin of the conflict minerals, and the efforts used to determine the mine location.[64] The CCMA would have only required the disclosure of the mine

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59. *See* S. 891 §§ 3, 5. Ultimately, this bill was cosponsored by twenty-two senators in addition to Senator Brownback. *See* Status of S. 891 (111th): Congo Conflict Minerals Act of 2009, http://www.govtrack.us/congress/bill.xpd?bill=s111-891 (last visited Nov. 16, 2012). At the time the CCMA was introduced in committee, Senator Brownback stated, "We have taken a strong hard look at [the CCCA] and have done our best to improve on it." 155 CONG. REC. 10598 (2009) (statement of Sen. Brownback). Senator Feingold, joining as an original co-sponsor, added that "the long-term goal is not to shut this trade down, but to support a conflict-free mining economy that benefits the Congolese people." *Id.* at S4697 (statement of Sen. Feingold).

60. Dodd Frank, § 1502(b), 15 U.S.C. § 78m(p)(2)(B) (Supp. V 2011). The SEC's final rule did not shed much light on what will be considered "necessary for the functionality or production of a product" and instead indicated that it would be a fact based determination on a case-by-case basis. Conflict Minerals Final Rule, 77 Fed. Reg. 56,274, 56,349 (Sept. 12, 2012) (to be codified at 17 C.F.R. pts. 240, 249b). Notably, the SEC's final rule omitted a de minimis exception, so any trace amount of a conflict mineral in a product will require the issuer to comply with section 1502. *Id.* at 56,298.

61. S. 891 § 5.

62. *See id.*

63. *See* Dodd-Frank § 1502(b).

64. *See id*.

of origin of the conflict minerals with no independent audit necessary.[65] Additionally, the final version of section 1502 deleted a provision that would have allowed the SEC to review or temporarily waive the disclosure requirements if the SEC determined that a waiver was "(A) necessary for the protection of investors; and (B) in the public interest."[66] Another important difference is that the CCMA would not have obligated companies to post the required disclosures on their company website.[67] Overall, these changes were a product of Congress's additional consideration of the complex issues surrounding conflict minerals and the influence of a myriad of industry members affected by the legislation.[68]

B. What Section 1502 Requires

Section 1502 of Dodd-Frank amends section 13 of 'the '34 Act[69] by increasing mandatory disclosure requirements for producers of goods that include minerals derived from the DRC.[70] In general, this provision mandates the annual disclosure of whether conflict minerals necessary in the production of a company's manufactured goods originate in the DRC or an adjoining country.[71] The term "conflict mineral" is defined to mean "(A) columbite-tantalite (coltan) [also known as tantalum], cassiterite [also known as tin ore], gold, wolframite [also known as tungsten], or their derivatives; or (B) any other mineral or its derivatives determined by the Secretary of State to be financing conflict in the [DRC] or an adjoining country."[72] If the conflict minerals in use originated in the DRC or an adjoining country, the disclosing party must submit a report to the SEC that includes: (i) a description of the due diligence process undertaken by the disclosing party with regard to the source and chain of custody of those conflict minerals, which must be independently audited;[73] and (ii) a description of the products manufactured or contracted to be manufactured that are not "DRC conflict free," the identity of the independent auditor of the source and supply chain, the facilities that process the conflict minerals used by the disclosing party, the country from which the conflict minerals were obtained, and the efforts used to determine the origin (i.e., the specific

65. *See* S. 891 § 5.

66. *Compare* § 1502(b), *with* S. 891 § 5.

67. *Compare* § 1502(b), *with* S. 891.

68. According to Senator Feingold, "The Brownback amendment was narrowly crafted in consideration of [industry members'] challenges, and it includes waivers and a sunset clause after five years" to help properly balance the competing concerns. Press Release, Russ Feingold, *supra* note 51.

69. 15 U.S.C. § 78m.

70. Dodd-Frank, § 1502(b).

71. 15 U.S.C. § 78m(p)(1)(A). "Adjoining countries" include Angola, Burundi, Central African Republic, Republic of the Congo, Rwanda, South Sudan, Tanzania, Uganda, and Zambia.

72. Dodd-Frank § 1502(e)(4)(A)–(B).

73. 15 U.S.C. § 78m(p)(1)(A)(i). This independent audit must be certified by the disclosing party, which is an integral part of the due diligence process. *Id.* Additionally, this audit must be considered reliable by the SEC. *See id.* § 78m(p)(1)(C).

mine) of the conflict mineral.[74] For a product to be considered "DRC conflict free," the product must not contain minerals that finance, directly or indirectly, any armed groups in the DRC or adjoining countries.[75]

The reach of this disclosure requirement extends to any individual or company subject to any of the '34 Act's disclosure requirements if such companies or individuals require conflict minerals in the production of the products they manufacture or contract to be manufactured.[76] Beyond making the relevant disclosures to the SEC, those subject to this provision must post the required disclosures on their company websites.[77]

Within 270 days of the passage of Dodd-Frank, the SEC was required to promulgate regulations concerning the disclosure requirements mandated under subsection (p) of the '34 Act.[78] The SEC issued proposed regulations in December 2010,[79] and received thousands of comments during the comment period.[80] In April 2011, the SEC announced that its target date for publication of the final rule would be between August 2011 and December 2011.[81] Because of the numerous and varied concerns expressed by companies that are required to comply with the new provision, the SEC held a roundtable discussion in October 2011 to discuss stakeholder issues. In December 2011, the SEC stated that it would issue its final rule between January and June 2012.[82] Due to the intensity of comments from the public, Congress, and affected companies, as well as the amount of time that was required to perform an economic analysis, the SEC again delayed the final rule, but stated in July 2012 that it would vote on the final rule on August 22, 2012.[83] On that date, the final rule was issued and adopted by the Commission by a 3–2 vote.[84]

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74. *Id.* § 78m(p)(1)(A)(i)–(ii).

75. *Id.* § 78m(p)(1)(D).

76. *Id.* § 78m(p)(2)(A)–(B).

77. *Id.* § 78m(p)(1)(E).

78. *Id.* § 78m(p)(1)(A).

79. Conflict Minerals Proposed Rule, 75 Fed. Reg. 80,948 (proposed Dec. 23, 2010) (to be codified at 17 C.F.R. pts. 229, 249b).

80. *See Proposed Rule: Conflict Minerals*, SEC, http://www.sec.gov/comments/s7-40-10/s74010.shtml (last visited Nov. 16, 2012) [hereinafter Comments on Proposed Rule].

81. *See* GAO REPORT, *supra* note 8, at prologue. The SEC delayed issuing the final rules due to the complexity of the regulation and the numerous amounts of comments provided by industry members, congressional representatives, and nongovernmental organizations. *See* Comments on Proposed Rule, *supra* note 80. The comment period was opened again in the fall of 2011 to allow additional comments on the proposed rules. *Conflict Minerals Final Rule Deadline Postponed Again: SEC Makes It Official*, SUSTAINABILITY COUNSEL (Jan. 17, 2012, 8:44 AM), http://sustainability-counsel.com/2012/01/17/conflict-minerals-final-rule-deadline-postponed-again-sec-makes-it-official/.

82. *See* GAO REPORT, *supra* note 8.

83. *Id.*

84. Press Release, SEC Adopts Rule for Disclosing Use of Conflict Minerals (Aug. 22, 2012), *available at* http://sec.gov/news/press/2012/2012-163.htm. Commissioners Schapiro, Aguilar, and Walter voted in favor of the final rule; Commissioners Paredes and Gallagher dissented. *See* Edith Orenstein, *SEC Narrowly Passes Conflict Minerals, Resource Extraction Rules*, FIN. REPORTING BLOG (Aug. 22, 2012, 1:28 PM), http://www.financial

C. The SEC's Final Rule: Three Steps for Compliance

The SEC's regulations set out three steps issuers should follow in order to comply with the requirements of section 1502.[85] These steps are outlined below.

1. Determining if the Provision Applies

First, issuers must determine whether section 1502 applies to them.[86] As noted above, the provision applies to any issuer that files reports with the SEC under section 13(a) or 15(d) of the '34 Act, and for which conflict minerals are necessary to the functionality or production of a product manufactured by that issuer.[87] According to the SEC's final rule, issuers that directly manufacture products using conflict minerals, as well as those that contract the manufacturing of such products, are subject to the rule.[88] Under the proposed rule, this included issuers selling generic products under their own name brand, as long as the issuer had contracted with another party to have the product manufactured specifically for that issuer.[89] However, under the final rule, the SEC narrowed the scope of companies considered to have "contracted to manufacture" certain products. Specifically, a company is considered to be "contracting to manufacture" a product if it has some actual influence over the manufacturing of that product.[90] The SEC clarified this definition by listing examples of when a company is *not* deemed to have influence over the manufacturing of a product such as (1) if a company merely affixes its brand, marks, logo or label to a generic product manufactured by a third party; (2) if a company services, maintains, or repairs a product manufactured by a third party; or (3) if a company specifies or negotiates contractual terms with a

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executives.org/KenticoCMS/FEI_Blogs/Financial-Reporting-Blog/August-2012/SEC-Narrowly-Passes-Conflict-Minerals,-Resource-Ex.aspx.

85. Conflict Minerals Final Rule, 77 Fed. Reg. 56,274, 56,283 (Sept. 12, 2012) (to be codified at 17 C.F.R. pts. 240, 249b).

86. *Id.*

87. *Id.* at 56,274. Although the proposed rule stated that the SEC would consider miners as "manufacturers" subject to the regulation, the SEC exempted miners from the definition of manufacturers in its final rule. *Compare id.* at 56,292, *with* Conflict Minerals Proposed Rule, 75 Fed. Reg. 80,948, 80,972 (Dec. 23, 2010) (to be codified at 17 C.F.R. pts. 229, 249b).

88. Conflict Minerals Final Rule, 77 Fed. Reg. at 56,288.

89. Conflict Minerals Proposed Rule, 75 Fed. Reg. at 80,952.

90. Conflict Minerals Final Rule, 77 Fed. Reg. at 56,291. Thus, under the proposed rule, Costco would have been a good example of a nonmanufacturer that contracted for the manufacturing of its own products, namely its Kirkland Signature brand. *See* Conflict Minerals Proposed Rule, 75 Fed. Reg. at 80,952. Under the final rule, however, Costco does not fall under the definition of manufacturer unless it has "actual influence over the manufacturing" of the products to which it affixes its label. Conflict Minerals Final Rule, 77 Fed. Reg. at 56,291. This change to the final rule came as a result of aggressive lobbying by major retailers such as Wal-Mart and Target. *See* Jessica Holzer, *Wal-Mart, Target Avoid Mining Rule*, WALL ST. J., Aug. 23, 2012, at B1.

manufacturer that do not directly relate to the manufacturing of the product.[91]

In addition, in assessing whether the provision applies, issuers must determine if the conflict minerals are "necessary" to the functionality or production of the product.[92] The SEC did not define when a conflict mineral is necessary to the functionality or production of a product in its proposed rule; however, the two congressional sponsors of section 1502 indicated in a comment letter that they believe the provision should cover "all uses of conflict minerals coming from DRC—except those that are 'naturally occurring' or 'unintentionally included' in the product."[93] The SEC's final rule stated that issuers should consider whether the conflict mineral is necessary to the product's "generally expected function, use or purpose," and if the conflict mineral is included only for purposes of decoration or embellishment, whether the primary purpose of the product is ornamentation.[94] Notably absent from the final rules is a de minimis exception for such products. Therefore, any product with any trace of conflict minerals that are necessary to the functionality or production of the product must comply with the rule's disclosure requirements.

2. Determining if the Minerals are "Conflict"

Once issuers have determined that their products contain minerals listed in section 1502, they must determine if these minerals are *conflict* minerals, as defined by the statute, and conduct an inquiry into the origin of the contents of their products.[95] In determining the origin of the minerals, the regulation requires a "reasonable country of origin inquiry," undertaken in good faith.[96] However, the SEC did not set forth guidelines as to what constitutes a reasonable country of origin inquiry.[97] Nevertheless, the rule requires that issuers disclose the origin of the minerals, even if the origin is not the DRC or a neighboring country.[98]

The SEC clarified that one way for an issuer to satisfy the reasonable country of origin inquiry is for the issuer to receive reasonably reliable representations from the facility that processed its conflict minerals that those minerals did not originate from the DRC or a neighboring country.[99] This concept of a "conflict-free smelter" as satisfying the requirement under section 1502 has spurred some industry participants to implement a

91. Conflict Minerals Final Rule, 77 Fed. Reg. at 56,291.
92. 15 U.S.C. § 78m(p)(1)(A) (Supp. V 2011).
93. Conflict Minerals Proposed Rule, 75 Fed. Reg. at 80,953.
94. Conflict Minerals Final Rule, 77 Fed. Reg. at 56,297.
95. *Id*. at 56,291.
96. *Id.* at 56,310–12.
97. *Id.* at 56,311 ("The final rule does not specify what steps and outcomes are necessary to satisfy the reasonable country of origin inquiry requirement because, as stated in the Proposing Release, such a determination depends on each issuer's particular facts and circumstances.").
98. *Id.* at 56,314–15.
99. *Id*. at 56,312.

conflict-free smelter program aimed at creating a list or network of clean smelters.[100]

If, after completing a reasonable country of origin inquiry, the company knows or has reason to believe that the minerals *did not* originate in any of the listed countries or are from scrap or recycled sources, the company must provide a brief description of the basis for its determination.[101] This disclosure must be provided on newly created Form SD, which the issuer must file with the SEC.[102] The issuer must also post that description on its website and disclose the website address to the SEC on Form SD.[103]

On the other hand, if a company knows or has reason to believe that the minerals *may* have originated in one of the listed countries or may not be from scrap or recycled sources, the company must perform due diligence on the source and supply chain of its minerals and submit a Conflict Minerals Report (CMR) as an exhibit to Form SD.[104] The CMR must also be posted on the company website.[105]

3. Creating the Conflict Mineral Report

The CMR itself must include proof that the company conducted due diligence on the source and supply chain of the conflict minerals.[106] The quality of this due diligence must meet a standard that is nationally or internationally recognized, such as the due diligence guidance approved by the Organisation for Economic Cooperation and Development (OECD).[107]

A company's products can still be labeled "DRC conflict free" if the minerals originate from one of the listed countries but they did not finance or benefit armed groups.[108] If a company determines, after conducting due diligence, that its products are "DRC conflict free," it is not required to file a CMR with its Form SD, but must include in its Form SD a description of the due diligence undertaken and the results thereof.[109]

If, after conducting due diligence, a company cannot assert that its products are "DRC conflict free," then the company must state in its CMR: (1) that the products manufactured or contracted to be manufactured have

100. *See* Elec. Indus. Citizenship Coal., Inc. & Global e-Sustainability Initiative, *EICC-GeSI Conflict Free Smelter Assessment Program: Frequently Asked Questions*, CONFLICT FREE SMELTER, 12 (Mar. 30, 2012), http://www.conflictfreesmelter.org/documents/Conflict-FreeSmelterFAQ.pdf. Elements of the conflict-free smelter program include: (1) due diligence where companies work with their suppliers to verify the smelters in their mineral supply chain; (2) third-party validation of a smelter's sourcing practices and a determination of whether its sources are conflict free; and (3) an in-region mineral certification system that enables the traceability and certification of minerals mined in the DRC. *Id.* 9–11.

101. Conflict Minerals Final Rule, 77 Fed. Reg. at 56,285.

102. *Id.* at 56,312.

103. *Id.* at 56,361–63.

104. *Id.* at 56,320–24.

105. *Id.* at 56,333.

106. *Id.* at 56,320–24.

107. *Id.* at 56,324.

108. *Id.* at 56,317.

109. *Id.* at 56,320–21.

not been found to be “DRC conflict free”; (2) the facilities used to process the conflict minerals; (3) the country of origin of the conflict minerals; and (4) the efforts to determine the mine or location of origin with the “greatest possible specificity.”[110] In addition, the company must (1) obtain an independent private sector audit of its CMR; (2) certify that it obtained the audit; (3) identify the auditor; and (4) append a copy of the audit report as part of the CMR.[111]

Finally, if a company is unable to determine whether its products are “DRC conflict free,” because it cannot determine the country of origin or whether the minerals in its products financed or benefited armed groups, it will be subject to a temporary two-year transition period during which its products will be labeled “DRC conflict undeterminable.”[112] For smaller reporting companies, the temporary transition period is extended to four years.[113] The company must still file a CMR, stating: (1) the facilities used to process the conflict minerals; (2) the country of origin, if known; (3) the efforts to determine the mine or location of origin with the greatest possible specificity; and (4) the steps the company has taken or will take to mitigate the risk that its necessary conflict minerals benefit armed groups, including any steps to improve its due diligence process.[114] In this case, however, the company is not required to obtain an independent private sector audit of its CMR.[115]

III. LOGISTICAL ISSUES WITH IMPLEMENTING SECTION 1502

Section 1502 presents a number of potential challenges. It creates significant hurdles to issuers, and costs of compliance with the regulation could be astronomical, depending on the issuer and its product. The provision itself is also vague, creating additional obstacles to effective and efficient compliance. In addition, it places an unrealistic burden on the SEC to regulate a provision aimed at eradicating human rights abuses—an area in which the SEC does not tread.

A. Cost of Compliance

Section 1502 has a number of critics in all arenas that cite a variety of obstacles with the implementation of the provision.[116] The sharpest criticisms of section 1502 came from industry members who the requirement will affect and who believe the requirement is overly burdensome in terms of cost.[117] The SEC was well aware of the economic

110. *Id.*
111. *Id.*
112. *Id.*
113. *Id.* at 56,281.
114. *Id.* at 56,320–21.
115. *Id.* at 56,321.
116. *See* Comments on Proposed Rule, *supra* note 80 (listing comment letters received by the SEC).
117. Conflict Minerals Final Rule, 77 Fed. Reg. at 56,286, 56,291.

concerns surrounding the rule, as numerous comments to the SEC from industry members stressed the financial burdens of compliance.[118] The SEC estimated in its proposed rule that the cost for those affected by the regulation will total approximately $71 million.[119] In its final rule, however, the SEC estimated that the financial burden would be approximately $3–4 billion at the outset in order for companies to develop compliance programs.[120] The SEC then estimated that it would cost approximately $207–609 million for annual ongoing compliance.[121] However, the National Association of Manufacturers estimates that the compliance costs will be between $8 and $16 billion.[122]

Nonprofit lobbying groups have rebutted the arguments claiming that the legislation is too burdensome to implement, pointing to a statement made by Hewlett Packard—in front of several other titans of the electronics industry—that compliance with section 1502 would cost those companies less than one cent per product.[123] The Hewlett Packard statement, however, might not be indicative of the costs across the industry, according to a Tulane Law study undertaken in October 2011.[124] The Tulane study found that the proposed rule's estimated cost of $71.2 million underestimated the implementation cost, in part because it did not take into account the range of actors affected by the law.[125] The study further noted, "On the other hand, the [National Association of Manufacturers'] estimate of $9–16 billion overstates these costs by inflating the supplier number and not taking into account significant overlap in supplier/customer relationships, as well as cost efficiencies from existing (and developing) information exchange

118. *See, e.g.*, Comment Letter from Cecilia L. Gardner, Pres., CEO & Gen. Counsel, Jewelers Vigilance Comm., et al., to Elizabeth M. Murphy, Sec'y, SEC (Mar. 2, 2011) [hereinafter JVC Comment Letter], *available at* http://www.sec.gov/comments/s7-40-10/s74010-144.pdf.

119. Conflict Minerals Proposed Rule, 75 Fed. Reg. 80,948, 80,965 (Dec. 23, 2010) (to be codified at 17 C.F.R. pts. 229, 249b).

120. Conflict Minerals Final Rule, 77 Fed. Reg. at 56,334.

121. *Id.* The SEC acknowledged in the open meeting issuing the final rule that pinpointing an actual estimate for this rule was nearly impossible due to the number of assumptions those creating the economic analysis had to make. Daniel M. Gallagher, Comm'r, SEC, Statement at SEC Open Meeting: Proposed Rule to Implement Section 1502 of the Dodd-Frank Act—the "Conflict Minerals" Provision (Aug. 22, 2012) [hereinafter Statement of Commissioner Gallagher], *available at* http://sec.gov/news/speech/2012/spch082212dmg-minerals.htm.

122. Conflict Minerals Final Rule, 77 Fed. Reg. at 56,334.

123. *See Intel Hit by Protests over Congo Minerals*, THINQ.CO.UK (May 27, 2010), http://www.thinq.co.uk/2010/5/27/intel-hit-by-protests-over-congo-minerals/ [hereinafter Intel & Congo Minerals].

124. *See* Chris Bayer, *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*, LAW PROFESSOR BLOGS (Oct. 17, 2011), http://lawprofessors.typepad.com/files/tulane-study.pdf.

125. *Id.* at 3.

platforms."[126] Based on its own assessments, the Tulane study estimated the cost of implementing the regulation to be $7.93 billion.[127]

Citing the Tulane study, additional comment letters were sent to the SEC, including one from Senator Olympia Snowe and other members of Congress, pressing the SEC to consider the cost to small businesses forced to comply with section 1502.[128] In her letter, Snowe wrote that members of the Senate and House Small Business Committees were concerned that the SEC's initial analysis of the costs of the proposed rule and its impact on small businesses was inadequate.[129] Among other things, the Senator urged the SEC to consider adding a de minimis standard to the regulation, exempting products that contain less than a set amount of conflict minerals from the regulation.[130] In addition, they encouraged the SEC to consider creating an "indeterminate origin" category within the rule to allow for a more lenient standard for compliance if small businesses are unable to determine the origin of the minerals.[131] Although the SEC raised its cost estimates in the final rule, it still did not carve out any exemptions for small businesses nor did it exempt the de minimis use of conflict minerals.[132]

Indeed, despite including an economic analysis of the regulation in the SEC final rule, the business community has already challenged the SEC over the costs associated with compliance, and recent case law indicates that the SEC may be fighting a losing battle regarding the adequacy of its cost assessment.[133] In a recent ruling in *Business Roundtable v. SEC*,[134] the D.C. Circuit struck down the SEC's proxy disclosure rule, in part because the agency did not conduct an adequate cost-benefit analysis.[135] In a fairly scathing opinion, the court held that the agency "acted arbitrarily and capriciously for having failed once again . . . [to] adequately . . . assess the economic effects of a new rule."[136] The court also determined that the SEC "inconsistently and opportunistically framed the costs and benefits of

126. *Id.*

127. *Id.* ("Almost half of the total cost—$3.4 billion—would be met with in-house company personnel time, and the rest—$4.5 billion—would comprise outflows to 3rd parties for consulting, IT systems and audits. Comparing the costs to the issuers vs. the suppliers, the bulk of the total costs—$5.1 billion or 65%—would be incurred by the suppliers (the group not included in SEC's analysis), while the smaller portion of the total—$2.8 billion or 35%—would be carried by the issuers.").

128. Comment Letter from Olympia Snowe, U.S. Senator, et al., to Mary Schapiro, Chairman, SEC 1 (Nov. 17, 2011), *available at* http://www.sec.gov/comments/s7-40-10/s74010-427.pdf.

129. *Id.*

130. *Id.* at 3.

131. *Id.*

132. Conflict Minerals Final Rule, 77 Fed. Reg. 56,274, 56,298, 56,359 (Sept. 12, 2012) (to be codified at 17 C.F.R. pts. 240, 249b).

133. C.M. Matthews, *Business Groups Sue To Block "Conflict Minerals" Rule*, WSJ BLOGS (Oct. 22, 2012, 4:38 PM), http://blogs.wsj.com/corruption-currents/2012/10/22/business-groups-sue-to-block-conflict-minerals-rules/.

134. 647 F.3d 1144 (D.C. Cir. 2011).

135. *Id.*

136. *Id.* at 1148.

the rule; failed adequately to quantify the certain costs or to explain why those costs could not be quantified; neglected to support its predictive judgments; contradicted itself; and failed to respond to substantial problems raised by commenters."[137] Given that the Tulane study and other industry estimates are drastically higher than the SEC estimate for the costs associated with section 1502 compliance, the agency may very well have delayed its final regulations to ensure that it can protect against a result similar to the *Business Roundtable* decision.[138] Nonetheless, the recent challenge of section 1502 by the National Association of Manufacturers and the U.S. Chamber of Commerce indicates that the affected industries are unwilling to merely accept the costs associated with this provision.

B. Problems with Determining the Source of Minerals

One of the more serious critiques of this first-of-its-kind legislation is that it is too difficult for companies to determine whether the minerals used in production are in fact conflict minerals.[139] Shortly after the passage of Dodd-Frank, the Electronics Industry Citizenship Coalition (EICC) and Global e-Sustainability Initiative (GeSI)—both industry trade groups—commissioned a report by Resolve, an American nonprofit organization, which outlined three major challenges concerning conflict mineral transparency requirements down to the mining-level.[140] These concerns were: (1) supply chains are not sufficiently transparent to this level; (2) tracking capacity and accountability mechanisms to this level are missing or limited; and (3) the on-the-ground capacity (in conflict regions) to differentiate sources and ensure independence from operations that may support warring groups does not exist.[141]

One particular concern is issuers' ability to track the origin of gold used in their products. The OECD, which issued guidance for due diligence in supply chains for tin, tantalum, and tungsten, finalized its supplement for the gold supply chain nine months after publishing its guidance for the 3Ts supply chain, adding fuel to the argument that the gold supply chain has unique aspects that render it more difficult to regulate.[142] In particular, advocates for treating gold separately from the other conflict minerals point out that gold is refined by thousands of diverse operators, and is often

137. *Id.* at 1148–49.

138. The Chamber of Commerce and other industry participants have filed suit based on the SEC's economic estimate, similar to the situation in *Business Roundtable*. Ian Thoms, *SEC'S Toned-Down Conflict Mineral Rule Still Faces a Fight*, LAW360 (Aug. 22, 2012, 5:47 PM), http://www.mayerbrown.com/files/News/d1217489-3fea-44f4-adf6-0a606a1c0d03/Presentation/NewsAttachment/ed52f4c7-d35a-409d-9e35-0b928ec0053d/SEC's%20Toned-Down%20Conflict%20Mineral%20Rule%20Still%20Faces%20A%20Fight.pdf; *see also* Matthews, *supra* note 133.

139. *See* Sheridan, *supra* note 8.

140. Resolve, *Tracing a Path Forward: A Study of the Challenges of the Supply Chain for Target Metals Used in Electronics*, EICC, 5 (April 2010), http://www.eicc.info/documents/resolvereport4.10.10.pdf.

141. *Id.*

142. JVC Comment Letter, *supra* note 118, at 6–8.

refined more than once. In addition, newly mined gold is often melded together with scrap and other existing stocks of gold, and the sources of the already-existing gold is impossible to determine.[143] Unlike the other conflict minerals listed, gold is inherently valuable and often used as currency, making the market for gold very dynamic and fluid, which increases the difficulty in charting its supply chain.[144]

C. Timing for Compliance

An issuer with a disclosure obligation under section 1502 must file its first report by May 31, 2014, regardless of its filing date for other SEC reports.[145] The CMRs due in 2014 cover the calendar year of 2013. Large companies, such as Kraft Foods, have complained that they will need additional time to perform proper due diligence on their entire supply chains and that the due diligence could take longer than a year.[146] The SEC has indicated, however, that it will allow for a phase-in period for companies required to disclose, so that these companies can perform the requisite due diligence of their supply chains.[147] The final rule reflects the "phase-in period" and refers to the temporary two-year period in which a company can state that its products are "DRC conflict undeterminable."[148]

D. Statutory Liability: "Furnished" vs. "Filed"

Another important point regarding the overall efficacy of this provision lies in the procedural requirements of the CMR itself and the liability that attaches to those requirements. Section 1502 does not include stated

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143. *Id.* at 12.

144. *Id.* at 6–8. Gold industry members encouraged the SEC to adopt a phased-in approach for section 1502 to allow them to prepare for compliance with the obstacles inherent in the gold supply chain. *Id.* at 4–11.

145. *See* Conflict Minerals Final Rule, 77 Fed. Reg. 56,274, 56,305 (Sept. 12, 2012) (to be codified at 17 C.F.R. pts. 240, 249b). It should be noted that section 1502 does not mandate that the disclosure be provided in a registrant's annual report, unlike Dodd-Frank's section 1503, Reporting Requirements Regarding Coal and Other Mine Safety, and section 1504, Disclosure Payments by Resource Extraction Issuers, which required disclosures to be provided in a company's "periodic report" or annual report, respectively. *Compare* Dodd-Frank, § 1502, 15 U.S.C. § 78m (Supp. V 2011), *with id.* §§ 1503–1504. For this reason, the SEC had the freedom to create Form SD in order to streamline compliance with the conflict mineral regulation. It should be noted, however, that the recent suit filed by the Chamber of Commerce and the National Association of Manufacturers could result in a stay of the final rule, which would delay its enforcement and provide additional time for companies affected by the rule. *See* Matthews, *supra* note 133.

146. Sarah Johnson, *Searching for Missing Supply-Chain Links*, CFO (Oct. 19, 2011), http://www3.cfo.com/article/2011/10/supply-chain_sec-conflict-minerals-rule-searching-for-missing-supply-chain-links. Kraft Foods, with 40,000 products and 100,000 suppliers, recently determined that the minerals may be a component in the pouch packaging of juice products. Edward Wyatt, *Behind the Blood Money*, N.Y. TIMES, Mar. 20, 2012, at B1.

147. Sarah Lynch, *SEC To Have Phase-In on Conflict Minerals Rule*, REUTERS (Mar. 6, 2012, 1:52 PM), http://www.reuters.com/article/2012/03/06/us-minerals-conflict-schapiro-idUSTRE8251DE20120306.

148. Conflict Minerals Final Rule, 77 Fed. Reg. at 56,322–23.

punishments or liabilities for noncompliance with the provision. According to the SEC's proposed rule, issuers were merely required to "furnish," rather than "file," the CMR and the certified audit that accompanies it to the SEC.[149] This difference was not a semantic one; merely "furnishing" the report with the Commission meant that the issuer was not open to section 18 liability.[150] This did not mean that these disclosures were immune from any liability; rather, they would have been open to the same liability that accompanies section 13a and section 15d disclosures.[151] Section 13(a) and section 15(d) liability typically attaches if an issuer fails to furnish a required exhibit or if a required exhibit is "unreliable."[152] The penalties for these violations may be injunctive, civil, or criminal and can extend to executives of the issuing company.[153]

In its proposed rule, the SEC noted that because the conflict minerals regulation is vastly different from other reporting requirements that typically deal with the financial health of a corporation, it would not submit issuers to the additional section 18 liability.[154] In practical terms, this meant that there would have been no private right of action for failure to comply with section 1502, aside from a claim based on fraud. Instead, only the SEC would have had the authority to enforce compliance and to punish noncompliance.

After much pressure from members of Congress and other nongovernmental organizations, however, the SEC increased the scope of liability in its final rule. In its final rule, the SEC changed the language of the rule to require that issuers *file* the newly created Form SD and (if

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149. *See* Conflict Minerals Proposed Rule, 75 Fed. Reg. 80,948, 80,949–50 (Dec. 23, 2010) (to be codified at 17 C.F.R. pts. 229, 249b). In a letter to the SEC on February 16, 2012, Senator Patrick Leahy, Representative Howard Berman, and other members of Congress indicated their concern over the rule's requirement of "furnishing" rather than "filing" the CMR. *See* Comment Letter from Patrick J. Leahy, U.S. Senator, et al., to Mary L. Schapiro, Chairman, SEC 1 (Feb. 16, 2012), *available at* http://www.sec.gov/comments/s7-40-10/s74010-497.pdf. The letter states that, as a result, the rule does not reflect congressional intent to protect investors and hold issuers accountable for the substance of the disclosures. *Id.* at 2. Additionally, the letter evinces congressional concern that the rule allows for an indeterminate country of origin category in contrast with other members of Congress who encouraged inclusion of an indeterminate country of origin category. *Id.* at 1.

150. Section 18 of the '34 Act makes reporting issuers liable for "false or misleading statements" if investors rely on such statements when purchasing or selling securities at a price which was affected by such statements. Securities Exchange Act of 1934 § 18, 15 U.S.C. § 78m (2006).

151. The SEC alone regulates disclosures pursuant to sections 13 and 15 of the '34 Act. Of course, all material disclosures open issuers up to section 10b-5 liability for fraud. 15 U.S.C. § 78j.

152. *International Trade Alert, Conflict Minerals Update: Letter from Congress Indicates SEC Final Rule is Imminent*, AKIN GUMP STRAUSS HAUER & FELD LLP, 2 (Feb. 17, 2012), http://www.akingump.com/files/Publication/908f6607-f535-4df6-aee1-991835fec513/Presentation/PublicationAttachment/c2b3d597-b221-43f5-80ec-f80353e4fdc2/120217_Conflict_Minerals_Update_Letter_From_Congress.pdf.

153. *Id.*

154. Conflict Minerals Proposed Rule, 75 Fed. Reg. at 80,960–61.

necessary) the CMR as an exhibit to that form.[155] This change now opens issuers up to potential shareholder liability, as well as potential investigations from the SEC itself. Of course, the SEC must enforce compliance with section 1502 in the same way it enforces compliance with its other material disclosure requirements. This means that the SEC is charged with evaluating disclosures made by electronics corporations, mining corporations, and others affected by the legislation, to ensure that the corporations' disclosures pertaining to the origin of minerals is accurate.[156] The SEC will likely rely upon the independently certified audits to enforce compliance; however, a certified audit is only required if a company determines that it does, in fact, use conflict minerals in its products. This means that any company that denies the use of conflict minerals is not required to have a certified audit, and the SEC likely will have little capacity to validate that assertion.

However, the specter of 10b-5 liability that attaches to any disclosure requirement should not be underestimated.[157] Rule 10b-5 provides a private right of action to shareholders injured in the sale or purchase of a security by false or misleading statements made by corporate insiders,[158] and the threat of 10b-5 liability alone is sufficient to incentivize a company to comply with any statutorily required disclosures. Rule 10b-5 is the biggest proverbial stick available to both the SEC and private shareholders and has been referred to as "a judicial oak which has grown from little more than a legislative acorn"[159] as it applies to all corporate statements, not only those required in periodic and annual filings.[160] The threat of 10b-5 liability, in addition to the newly accorded private right of action to shareholders by virtue of Form SD being "filed" rather than merely "furnished," will surely incentivize issuers to fully comply with the new regulation.

155. Conflict Minerals Final Rule, 77 Fed. Reg. 56,274, 56,280 (Sept. 12, 2012) (to be codified at 17 C.F.R. pts. 240, 249b).

156. *See* 15 U.S.C. § 78m(p)(1)(A)(i)–(ii) (Supp. V 2011).

157. Rule 10b-5 provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5 (2012).

158. *See* Kardon v. Nat'l Gypsum Co., 69 F. Supp. 512, 513 (E.D. Pa. 1946).

159. Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 737 (1975).

160. *See, e.g.*, Perry E. Wallace, *Disclosure of Environmental Liabilities Under the Securities Laws: The Potential of Securities-Market-Based Incentives for Pollution Control*, 50 WASH. & LEE L. REV. 1093, 1115–16 (1993).

IV. LEGAL AND GLOBAL POLICY ISSUES WITH SECTION 1502

Section 1502 represents a marked departure from traditional disclosure requirements mandated under section 13. As discussed above, section 13 of the '34 Act, which was amended by section 1502, historically has required broad reporting requirements focused on financial and economic data, giving investors insight into the financial health of an issuer and the risks associated with any sweeping changes in the company.[161] For example, one important, and prototypical, section 13 disclosure requirement applies to persons holding more than 5 percent of a certain class of security.[162] This disclosure is required because the acquisition of more than 5 percent of a certain class of security could indicate the presence of an activist shareholder and could result in a substantial change in shareholdings. A holder of more than 5 percent of a certain class of securities can potentially seek to influence management or the direction of a shareholder vote or transaction.[163] This type of information is decidedly financial and, perhaps for that reason alone, important to investors.

Section 1502, however, stands in stark contrast to the existing section 13 disclosure requirements and to the SEC's mandate itself.[164] In particular, the newly instituted statutory disclosure requirement will force companies to provide nonmaterial information to investors and the public. In other words, section 1502 statutorily renders material the nonmaterial information of the presence of conflict minerals in an issuing company's product. Generating this obligation to disclose a fact that, absent the legislative requirement, likely would not affect a reasonable investor's decision to invest in a company, is problematic from both a securities law standpoint and a public international law standpoint, as will be discussed below.[165]

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161. Securities Exchange Act of 1934 § 13, 15 U.S.C. § 78m (2006).

162. *Id.* § 78m(d).

163. *See* MARK SCHONFELD ET AL., ENFORCEMENT ACTION ON SECTION 13(D) DISCLOSURE REQUIREMENTS FOR INSTITUTIONAL INVESTORS CLARIFIES EXCEPTION FOR "ORDINARY COURSE OF BUSINESS," SEC. REG. & L. REP. (BNA) 3 (Aug. 31, 2009), *available at* http://www.gibsondunn.com/publications/Documents/Schonfeld-Moloney-Loseman-Enfor ActionSec13(d).pdf.

164. In its Comment Letter to the SEC, Davis Polk & Wardwell LLP noted that "[s]ection 1502 was added to further an important public policy relating to the tragic events occurring in the Congo, rather than to further investor protection." Comment Letter from Davis Polk & Wardwell LLP to Elizabeth M. Murphy, Sec'y, SEC 4 (Mar. 2, 2011) [hereinafter DPW Comment Letter], *available at* http://www.sec.gov/comments/s7-40-10/s74010-142.pdf. The Comment Letter underscored the lack of investor protection in the legislation's goals as an argument that the information should not be required in a registrant's annual report. *Id.* at 4–5.

165. *See, e.g.*, Statement of Commissioner Gallagher, *supra* note 121 ("I do not like to see social or foreign policy provisions engrafted onto the securities laws. I have serious doubt, in any event, about the efficacy of using the securities laws to effect social and foreign policy aims, however noble and urgent.").

A. Rendering Nonmaterial Information Material

The critical importance of disclosure in securities law is relevant to the critique of section 1502 because, as indicated in the legislative history of the Brownback Amendment, Congress hopes that investors will consider an issuer's use of conflict minerals as material information.[166] The ultimate question, therefore, is whether the use of conflict minerals is *material* information.[167] Obviously, the legislation itself renders that question moot by statutorily requiring disclosure rather than requiring an analysis of materiality. However, disclosure of social and environmental information is typically not required because that information, to date, has not been regarded as relevant or material to the financial condition of a company.[168] As noted above, the SEC regulations, while not explicitly adopting an economic standard for materiality, implicitly define material information as that which bears on the economic value of an investment.[169] Consider the

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166. DPW Comment Letter, *supra* note 164, at 2.

167. The question of materiality for use of conflict minerals is one that this Article does not undertake in its entirety, given that the question is rendered moot by the legislative requirements. A more robust analysis of materiality as it relates to conflict mineral disclosure will be handled in my future scholarship.

168. *See* David Monsma & Timothy Olson, *Muddling Through Counterfactual Materiality and Divergent Disclosure: The Necessary Search for a Duty To Disclose Material Non-financial Information*, 26 STAN. ENVTL. L.J. 137, 161 (2007). Monsma and Olson observe, however, that nonfinancial information can be considered "economic" in sustainable development terms "and in this way financially relevant to socially responsible investors." *Id.* at 185. In addition, Monsma and Olson state that financial analysts in several countries have begun to factor in corporate social and environmental responsibility, such as carbon emissions efficiency, in evaluating a company's investment potential. *Id.* at 185–86. Monsma and Olson argue that socially responsible investor firms consider nonfinancial social responsibility and environmental performance as material information for their funds. *Id.* at 196–97. Without a clear economic link to the valuation of an investment, however, the social and environmental information may not rise to the legal definition of materiality as espoused by the SEC and the Supreme Court.

169. Williams, *supra* note 17, at 1264; *see also* BENN STEIL & ROBERT E. LITAN, FINANCIAL STATECRAFT: THE ROLE OF FINANCIAL MARKETS IN AMERICAN FOREIGN POLICY 64 (2006) ("[T]he SEC assesses materiality on the basis of its relevance to investor financial interests. The SEC's role is not to advise investors about what is good for them—let alone what might be good for the United States—or even to educate investors regarding ethical, religious, or foreign policy matters which may attach to doing business overseas. These matters may well be assigned, through appropriate legislation, to other arms of the government but ill-suit an agency whose reputation for integrity across the globe is intimately bound up with its ability to remain scrupulously neutral in questions as to which businesses do and do not 'deserve' private capital. This reputation is critical to America's ability to attract capital markets activity within its legal jurisdiction.").

Steil and Litan point to the example of PetroChina to show the evolution of requiring disclosure of nonfinancial information. *Id.* at 65. In 2000, China National Petroleum Company (CNPC) decided to list on the New York Stock Exchange (NYSE) with the hopes of raising $5–10 billion in equity capital. *Id.* at 58. The offering resulted in strong pushback from members of Congress and interest groups who were opposed to CNPC's heavy involvement in the Sudanese oil industry. *Id.* CNPC reacted to the criticism and restructured itself in such a way that only a subsidiary entity with no Sudanese assets, PetroChina, would be listed on NYSE. *Id.* PetroChina's critics were not assuaged and continued campaigning against its IPO. *Id.* Ultimately, the PetroChina IPO was downsized to roughly $3 billion. *Id.* at 59.

scenario in which a company files a CMR with a clear misstatement of fact and is sued by a shareholder. The materiality question that would be paramount to the analysis of such a case is whether the shareholder could prove loss or loss causation. This is typically proven by evaluating the change in stock price when the issuer makes various announcements, such as the corrective disclosure.[170] In the case of conflict minerals, it seems unlikely that such a disclosure would drastically move a company's share price, thus proving the immateriality of the information.

Indeed, the SEC's proposed rule stated exactly that point:

> It appears that the nature and purpose of the Conflict Minerals Provision is for the disclosure of certain information to help end the emergency humanitarian situation in the eastern DRC that is financed by the exploitation and trade of conflict minerals originating in the DRC countries, *which is qualitatively different from the nature and purpose of the disclosure of information that has been required under the periodic reporting provisions of the Exchange Act.*[171]

Amending section 13 to include this disclosure requirement flies in the face of the SEC's mandate, and is not in keeping with the existing disclosure requirements of section 13.[172] Furthermore, requiring the SEC to enforce

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In the wake of the PetroChina IPO, Representative Frank Wolf issued a letter to the then-acting SEC Chairman Laura Unger stating:

> While other governmental agencies have jurisdiction over human rights, national security and other related abuses in Sudan, in this case it is corporations with securities that have been offered to U.S. investors, not governments, that have committed offenses. For that reason, the SEC, with its authority and mandate to oversee disclosure to inform and protect investors, should recognize material omissions by the companies as a violation of their disclosure requirements and take appropriate action.

Id. at 63. Unger responded by proposing enhanced disclosure requirements for foreign registrants conducting business in sanctioned countries, noting that U.S. investors should receive adequate disclosures about where the proceeds of their securities investments are going and how they are being used, regardless of whether such disclosures were considered material under the SEC's standard of materiality. Letter from Laura S. Unger, Acting Chairman, SEC, to Frank P. Wolf, U.S. Representative 3 (May 8, 2001), *available at* http://www.uscc.gov/researchpapers/2000_2003/pdfs/cpapp6.pdf. As a result of the requirement of additional disclosures set forth in the Unger Letter, in 2004 the SEC created an Office of Global Security Risk (OGSR) within its Division of Corporation Finance to "monitor whether the documents public companies file with the SEC include disclosure of material information regarding global security risk-related issues." *Office of Global Security Risk*, SEC, http://www.sec.gov/divisions/corpfin/globalsecrisk.htm (last visited Nov. 16, 2012). Thus, through the pressure from Congress in the wake of the Sudanese crisis in Darfur, the SEC systematically shifted its disclosure requirements beyond the strict definition of materiality. Notably, however, Roger Robinson, Chairman of the Casey Institute, stated in his response to the Unger letter that "'[n]ational security, human rights and religious freedom are now regarded as material risks to investors.'" STEIL & LITAN, *supra*, at 65.

170. *See generally* Jon Koslow, *Estimating Aggregate Damages in Class-Action Litigation Under Rule 10b-5 for Purposes of Settlement*, 59 FORDHAM L. REV. 811 (1991).

171. Conflict Minerals Proposed Rule, 75 Fed. Reg. 80,948, 80,960 (Dec. 23, 2010) (to be codified at 17 C.F.R. pts. 229, 249b) (emphasis added).

172. Commissioner Gallagher made this point in his dissenting remarks at the August 22, 2012, SEC Open Meeting to adopt the final rule:

these disclosure requirements stretches thin an already overburdened agency and demands that it oversee diplomatic and humanitarian regulations for which it lacks the institutional competence.

B. Indirect Extraterritorial Jurisdiction: Regulation of an Entire Supply Chain

In attempting to curb violence in the Congo the stated aim of section 1502—Congress could have asserted more direct extraterritorial jurisdiction and banned any product from any company, domestic or foreign, to be sold in the United States if it contained conflict minerals.[173] In the case of section 1502, however, Congress chose a more indirect approach to meet its extraterritorial goals. Extraterritorial jurisdiction of section 1502 is indirect in that foreign firms not registered on an American exchange, and therefore not subject to the jurisdiction of the SEC, may be forced to comply with the provision because they are part of a supply chain in which the final product is manufactured by an issuing company. Although outside the reach of any SEC disclosure requirement or liability scheme, a foreign company may feel the pressure from an issuing company to have an entire supply chain in compliance with section 1502, which may result in foreign companies rising to meet the standard required by the provision despite not facing any similar requirements in their home jurisdiction.

Of course, section 1502 is not the first time Congress has indirectly allowed for the SEC to exert extraterritorial jurisdiction. One prior example of such indirect jurisdiction is the Foreign Corrupt Practices Act[174] (FCPA).

> It is easy to see that the SEC role in this provision is the anomaly. That's because disclosure requirements in the securities laws are about telling investors what they reasonably should want to know before investing in a company. The point is to give investors information that is inherently "material" to their investment decisions. Disclosure is, and should be, the primary tool for the SEC to use in satisfying its mission. And so it is paramount that we focus on getting timely, material disclosures to investors. . . . Unfortunately, Section 1502 is *about* curtailing violence in the DRC; it is not about investor protection, promoting fair and efficient markets, or capital formation. Warlords and armed criminals need to fund their nefarious operations. Their funding is their lifeline; it's a chokepoint that should be cut off. That is a perfectly reasonable foreign policy objective. But it's not an objective that fits anywhere within the SEC's threefold statutory mission.

Statement of Commissioner Gallagher, *supra* note 121.

173. *See* CHRIS BRUMMER, SOFT LAW AND THE GLOBAL FINANCIAL SYSTEM: RULE MAKING IN THE 21ST CENTURY 37–39 (2012). Brummer, in describing territoriality and financial statecraft, lists various possibilities for direct extraterritorial application, none of which fall directly in line with the jurisdiction of section 1502. One example of direct extraterritorial jurisdiction that he notes is direct regulation of foreign firms, but this applies in the case of section 1502 only where the foreign firm is registered on an American exchange. *Id.* at 38. Another example he observes is jurisdiction over foreign firms when the foreign firms engage in conduct that has effects on the regulating country, but section 1502 does not go this far and does not regulate, at least directly, foreign firms who sell products with conflict minerals in the United States. *Id.* at 40.

174. Pub. L. No. 95-213, 91 Stat. 1494 (1977) (codified as amended at 15 U.S.C. §§ 78dd-1 to -2 (2006)). In 1977, Congress passed the FCPA, aimed at eradicating bribery

Interestingly, both the FCPA and section 1502 require corporate due diligence as means of compliance; both provisions arose out of a concern regarding foreign activities; and both provisions mirror international guidelines and goals.[175] Although both regulations aim at stemming an activity occurring abroad, the FCPA, unlike section 1502, has its underlying roots in preventing market manipulation and fraud.[176] This is a critical difference, given that the SEC—the agency responsible for ensuring market fairness and transparency—is also the regulatory agency responsible for enforcing section 1502, and has concurrent jurisdiction over regulating the FCPA with the Department of Justice. In other words, the FCPA involves regulation of malfeasance of the corporation's employees that directly relates to an issuer's financial bottom line, making the SEC a reasonable entity for regulating the accounting and records fraud inherent in FCPA violations. Obviously, the SEC has clear jurisdiction over the actions of employees or agents of issuers. Section 1502, on the other hand, deals only with disclosures of questionably material information, with the goal that the malfeasance of *others*, not employed or linked to the corporation, be stemmed. That is, section 1502 aims at deterring the activities of warlords and rebels in the DRC, not the employees or agents of issuers. As such, its enforcement falls well outside the mandate and expertise of the SEC.[177]

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occurring overseas, for the purpose of obtaining business. *Id.* The impetus for this legislation was that the SEC had investigated numerous companies in the 1970s and discovered that over four hundred companies had made questionable payments totaling over $300 million to foreign officials. *See* Daniel Patrick Ashe, Comment, *The Lengthening Anti-bribery Lasso of the United States: The Recent Extraterritorial Application of the U.S. Foreign Corrupt Practices Act*, 73 FORDHAM L. REV. 2897, 2902–03 (2005). Specifically, the FCPA prohibits the corrupt use of the mail or any other instrumentality of interstate commerce in furtherance of any offer, payment, promise to pay, or authorization of the payment of money or any other thing of value to any person, knowing that all or some of the payment will be offered, given or promised, directly or indirectly, to a foreign official to influence or induce the foreign official to either commit an act in violation of his or her lawful duty, or to secure an improper advantage in obtaining or retaining business. 15 U.S.C. §§ 78dd-1(a), -2(a) (Supp. V 2011). In addition to the antibribery provision regulated by the Department of Justice, the FCPA also includes accounting provisions that require corporations to make and keep books and records that accurately and fairly reflect the transactions of the corporation and to devise and maintain an adequate system of internal accounting methods. *Id.* § 78m.

175. *See, e.g.*, OECD, CONVENTION ON COMBATTING BRIBERY OF FOREIGN PUBLIC OFFICIALS IN INTERNATIONAL BUSINESS TRANSACTIONS AND RELATED DOCUMENTS 1997, *available at* http://www.oecd.org/investment/briberyininternationalbusiness/anti-bribery convention/38028044.pdf; OECD, OECD DUE DILIGENCE GUIDANCE FOR RESPONSIBLE SUPPLY CHAINS OF MINERALS FROM CONFLICT-AFFECTED AND HIGH-RISK AREAS 2011 [hereinafter OECD DUE DILIGENCE GUIDANCE], *available at* http://www.oecd.org/investment/guidelinesformultinationalenterprises/46740847.pdf;

176. *But see* Barbara Black, *The SEC and the Foreign Corrupt Practices Act: Fighting Global Corruption Is Not Part of the SEC's Mission*, 73 OHIO ST. L.J. (forthcoming 2012), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2009991 (theorizing that the FCPA and the act of combatting global corruption is not within the mandate of the SEC and that the SEC's enforcement of the FCPA diverts scarce resources from the SEC's core mission).

177. *See supra* Part I.

C. Efficacy of "Name and Shame" Legislation in Achieving Humanitarian Goals

Critics of section 1502 contend that it likely will not have an effect on the conflict mineral enterprise in Congo. First, the thrust of the legislation is that it will cause companies to disclose their use of conflict minerals and that this disclosure alone will merely result in "naming and shaming." Ideally, the "shaming" will incentivize the corporations to make changes and become better corporate actors. The regulation, however, does not require that companies cease, or even attempt to cease, their use of conflict minerals. That is, the efficacy of the provision turns on the public consciousness and reaction to learning that certain corporations have products that contain conflict minerals. This, of course, assumes that not only investors, but the public at large will review the companies' websites or SEC disclosures to learn whether a particular company has made a conflict mineral disclosure.[178]

The ultimate consideration concerning the efficacy of the "name and shame" legislation is this: What is the consequence for a company that uses conflict minerals and then complies with section 1502 and discloses this fact? In such a situation, the SEC obviously plays no role because the company has complied with regulatory standards. Ostensibly, a company can file a CMR with the SEC, publish the CMR on its website, and cross its fingers hoping that there is no public backlash that affects its bottom line or its brand. From a public international law standpoint, it would seem that the possibility of a remorseless, albeit SEC-compliant company, reduces the legislation to a toothless tiger.

Based on citizen outcry related to conflict minerals, however, it is very possible that the "name and shame" legislation could be effective.[179] For example, some companies were accused of lobbying to undercut the utility of section 1502 and were met with backlash from citizens. Intel, for example, had been specifically targeted for the way in which it has handled its stance on this legislation and was forced to analyze its supply chain.[180]

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178. *See* Ripken, *supra* note 34, at 146 ("In order for a disclosure system to be effective, not only must information that is supplied be disclosed completely . . . it must also be read and comprehended by the consumer."). The emphasis in securities law on providing information to the public is premised on the belief that individuals are rational, self-governing actors who are willing and able to process the information wisely. If we assume that investors are rational risk calculators who are consistently capable of weighing the costs and benefits of risky alternatives and selecting the best option, then a system of disclosure makes good sense.

179. *See* Monsma & Olson, *supra* note 168, at 184 ("Brand reputation, among other business incentives, drives companies to manage areas that lie beyond regulatory compliance and tangible financial relevance.").

180. *See* Intel & Congo Minerals, *supra* note 123. Intel initially deleted critical comments on its Facebook page made by activists over its stance on the conflict mineral legislation. After reinstating the deleted comments, Intel released a statement that said, "For well over a year, we have been engaged in both conversations with NGOs and our own industry focused on creating workable solutions. We have shared with our suppliers our current position on the issue. . . . We also support the objective of US legislation to address

Indeed, the public awareness of conflict minerals has increased over the past few years, with celebrity activists including Robin Wright and Ben Affleck lobbying Congress on the issue and writing op-eds online and in major newspapers.[181]

The general public, however, is not the constituency of the SEC; investors are.[182] If the SEC administered its regulations with an eye toward protecting all citizens, rather than only shareholders, it would be difficult to maintain capital formation and to balance the requirements of the agency's mandate. For this reason, as described in the previous section, the SEC has never waded very far into regulation of human rights or even corporate social responsibility.[183]

D. Hurting More Than Helping? A De Facto Embargo

The likely result of the implementation of section 1502 is that the disclosure requirements "may lead to a de facto embargo on formal trade if businesses decide to pull out of the region."[184] This concern was addressed by Senator Feingold in his statement to the Senate Banking, Housing, and Urban Affairs Committee, which reiterated that the goal of the legislation is not to shut down the mineral trade, but to support a conflict-free mining economy that benefits the Congolese people.[185] Nevertheless, Congolese activists and others have continually asserted that this regulation will lead, and has already led, to an embargo of Congolese minerals, a drastic cost

this problem." Press Release, Intel, Intel's Statement on Conflict Minerals Issue (May 19, 2010), *available at* http://blogs.intel.com/csr/2010/05/intels_statement_on_conflict_m.php.

181. Robin Wright, *From Dragon Tattoo to Congo: Combatting the Scourge of Violence Against Women*, HUFFINGTON POST (Jan. 10, 2010, 2:22 PM), http://www.huffingtonpost.com/robin/from-dragon-tattoo-to-con_b_1197226.html; Ben Affleck, *The Deadliest War*, WASH. POST, Nov. 30, 2010, at A21.

182. *See* STEIL & LITAN, *supra* note 169, at 71 ("[T]he SEC is chartered to protect American investor interests. It is not chartered to protect, let alone advance, American foreign policy interests.").

183. There are, however, advocates for compelling the SEC to expand nonfinancial, social disclosure requirements. These advocates point to socially conscious investors who deem such information as material to their investment decisions. *See, e.g.*, Monsma & Olson, *supra* note 168, at 161; *see also* Comment Letter from Iain Richards, Reg'l Head of Corporate Governance, Aviva Investors, et al., to Elizabeth M. Murphy, SEC (Nov. 1, 2011), *available at* http://www.sec.gov/comments/4-637/4637-11.pdf (advocating for improved corporate reporting on supply chain factors because they pose material risks to investors that are not typically disclosed); *see also* Rachel Cherington, Note, *Securities Laws and Corporate Social Responsibility: Toward an Expanded Use of Rule 10b-5*, 25 U. PA. J. INT'L. ECON. L. 1439 (2004).

184. *U.S. Shines Glare on Congo's Conflict Minerals*, REUTERS, July 21, 2010, *available at* http://uk.reuters.com/article/2010/07/21/congos-conflict-minerals-idUKLNE66K04720100721 (quoting Nicholas Garrett, Director, Resource Consulting Services).

185. 155 CONG REC. 10599–10600 (2009) (statement of Sen. Feingold). Notably, both dissenting SEC Commissioners at the SEC Open Meeting remarked the logical result of such a rule is a de facto embargo of the DRC. *See* Statement of Commissioner Gallagher, *supra* note 121; Troy A. Paredes, Comm'r, SEC, Statement at SEC Open Meeting to Adopt a Final Rule Regarding Conflict Minerals Pursuant to Section 1502 of the Dodd-Frank Act (Aug. 22, 2012), *available at* http://www.sec.gov/news/speech/2012/spch082212tap-minerals.htm.

that would outweigh any purported benefits of the regulation.[186] Indeed, with major American corporations shying away from using Congolese minerals, certain mines in Congo have suspended operations, forcing many Congolese out of work.[187] By mid-2011, exports of tin, tantalum, and tungsten from the DRC had fallen by 70 percent since the previous summer, a phenomenon that the local miners refer to as "Obama's embargo."[188] Furthermore, the de facto embargo is not even alleviating the human rights abuses occurring in the DRC, which is the stated aim of section 1502.[189]

Importantly, conflict minerals legislation could lead to an embargo that has only limited international cooperation, which could lead to regulatory arbitrage. As noted above, the third mandate of the SEC's regulatory authority is facilitating capital formation. This prong is often in tension with the other two prongs of the SEC's authority: protecting investors and maintaining fair markets. The reason for this tension is that if the U.S. markets are highly (or, arguably, overly) regulated, investors will flee the U.S. market for less burdensome markets, taking their capital along with them.[190] This concept of regulatory arbitrage is usually the central critique of additional regulations, and section 1502 is not immune to this criticism.

The assertion that section 1502 will result in open season for other countries to exploit Congolese minerals is not without merit. China, for example, has capitalized on the stringent U.S. regulation and now seems to possess a virtual monopoly on the Congolese minerals.[191] A Congolese civil society member stated that the Chinese mineral buyers are

> paying 20 percent less, maybe even 30 percent less than the old price, because now they are the only buyers. . . . The lower price means fewer people are bringing minerals to sell, and a lot of mines have suspended operations. But the Chinese are buying what comes to them. Their warehouses are full, with constant turnover.[192]

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186. *See, e.g.*, David Aronson, *How Congress Devastated Congo*, N.Y. TIMES, August 8, 2011, at A19; *see also* Hans Bader, *Thousands of Jobs and Billions in Wealth Wiped Out by Dodd-Frank Conflict Minerals Provision*, OPEN MARKET (July 27, 2011), http://www.openmarket.org/2011/07/27/thousands-of-jobs-and-billions-in-wealth-wiped-out-by-dodd-frank-conflict-minerals-provision/.

187. *See* Mary Kay Magistad, *Why Chinese Mineral Buyers Are Eyeing Congo*, PRI'S WORLD (Oct. 26, 2011), http://www.theworld.org/2011/10/chinese-conflict-minerals-congo/.

188. Editorial, *Africa and "Obama's Embargo,"* WALL ST. J., July 18, 2011, at A12.

189. Laura Seay, *Congo Conflict Minerals Bill Hurts the Miners It Hopes To Help*, CHRISTIAN SCI. MONITOR (July 18, 2011, 2:56 PM), http://csmonitor.com/layout/set/print/content/view/print/398136 ("[C]utting off demand for Congolese minerals on international markets does absolutely nothing to stop violence against civilians and only makes life for many civilians worse by leaving them with no viable means of financially supporting themselves or their families.").

190. *See generally* Harald Baum, *Globalizing Capital Markets and Possible Regulatory Responses*, *in* LEGAL ASPECTS OF GLOBALIZATION: CONFLICT OF LAWS, INTERNET, CAPITAL MARKETS AND INSOLVENCY IN A GLOBAL ECONOMY 77 (Jurgen Basedow & Toshiyuki Kono eds., 2000).

191. Magistad, *supra* note 187.

192. *Id.*

The optimal solution to the problem of regulatory arbitrage and the subsequent exploitation of the American boycott of conflict minerals is that other countries will follow suit and enact legislation similar to section 1502. Indeed, certain international organizations have encouraged conflict mineral regulation in member states, including the OECD and the United Nations.[193] Ideally, other countries would follow the United States' example and enact legislation similar to section 1502, much like what has happened internationally with the FCPA and its international equivalents, such as the U.K. Bribery Act.[194] Thus, unlike section 1502, the FCPA now has international counterparts, making eradication of global corruption a truly international goal. However, in the case of section 1502, until there is more international involvement in the potential embargo on Congolese minerals the risk for arbitrage and exploitation remains very real and very high.

V. A BETTER MODEL: THE KIMBERLEY PROCESS AND THE CLEAN DIAMOND TRADE ACT

Rather than looking to the SEC to regulate and police the potentially unwieldy number of issuers that will produce CMRs, Congress should have modeled its conflict mineral regime on the existing conflict diamond regulatory scheme.[195] In January 2003, a coalition of states, NGOs, and corporations launched the Kimberley Process Certification Scheme ("Kimberley Process," or "KPCS"), an international governmental certification scheme designed to prevent trade in conflict diamonds.[196] Countries participating in the Kimberley Process were required to pass domestic legislation enforcing a set of import and export controls for rough

193. *See, e.g.*, S.C. Res. 1857, ¶ 15, U.N. Doc. S/RES/1857 (Dec. 22, 2008), *available at* http://www.un.org/ga/search/view_doc.asp?symbol=S/RES/1857(2008); OECD DUE DILIGENCE GUIDANCE, *supra* note 175.

194. 2010, c. 23 (Eng.).

195. Conflict diamonds are defined as "diamonds that originate from areas [in Africa] controlled by forces or factions opposed to legitimate and internationally recognized governments, and are used to fund military action in opposition to those governments." U.N. Dep't of Pub. Info., *Conflict Diamonds: Sanctions and War*, U.N. (Mar. 21, 2001), http://www.un.org/peace/africa/Diamond.html.

196. *The Kimberly Process*, GLOBAL WITNESS, http://www.globalwitness.org/campaigns/conflict/conflict-diamonds/kimberley-process (last visited Nov. 16, 2012). The initial enthusiasm behind the Kimberley Process started as early as 1998, when Global Witness began exposing the role that diamonds play in funding conflict in central African states. In May of 2000, representatives from the diamond industry and diamond producing countries met in Kimberley, South Africa, to discuss ways of handling the conflict diamond trade. Karen E. Woody, *Diamonds on the Souls of Her Shoes: The Kimberley Process and the Morality Exception to WTO Restrictions*, 22 CONN. J. INT'L. L., 335, 343 (2007). This initial meeting led to three years of negotiations to enact the Kimberley Process. *See id.* at 343–44. In the Interlaken Declaration of November 5, 2002, representatives of the United States and forty-seven other signatory countries announced the imminent launch of the Kimberley Process Certification Scheme. *Id.*

diamonds.[197] Thus, in 2003, President Bush signed the Clean Diamond Trade Act[198] (CDTA), mandating that the importation into, and exportation from, the United States of any rough diamonds be controlled by the KPCS standards and procedures.[199] Specifically, the KPCS standards required that the United States trade rough diamonds only with other signatories to the KPCS.[200] In addition, according to the KPCS, all participating countries' internal controls must include requiring a certificate of origin for all rough diamonds imported or exported.[201] The KPCS is chaired by participating countries on a rolling basis, and members of the KPCS, as well as industry representatives[202] and civil society observers, meet twice a year at plenary meetings to monitor the success of the regime.[203] Although not lacking in critics,[204] the KPCS has reduced the international trade in

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197. Woody, *supra* note 196, at 345. Significantly, the KPCS only regulates *rough* diamonds, or diamonds that have not been cut or polished. *See id.* at 344. Rough diamonds are also easier to trace because once diamonds are cut and polished, any form of identification can be erased. *Id.* at 344 n.71. Because the KPCS regime is concerned primarily with the source of the diamond, it limited its reach to only rough diamonds. *See id.* at 344.

198. Pub. L. No. 108-19, 117 Stat. 631 (2003).

199. *Id*. § 2.

200. Raj, *supra* note 9, at 995–96. The current participating entities are Angola, Armenia, Australia, Bangladesh, Belarus, Botswana, Brazil, Canada, Central African Republic, China, Congo, Cote d'Ivoire, Croatia, European Union members, Ghana, Guinea, Guyana, India, Indonesia, Israel, Japan, Korea, Laos, Lebanon, Lesotho, Liberia, Malaysia, Mauritius, Mexico, Namibia, New Zealand, Norway, Russian Federation, Sierra Leone, Singapore, South Africa, Sri Lanka, Switzerland, Tanzania, Thailand, Togo, Turkey, Ukraine, United Arab Emirates, United States of America, Venezuela, Vietnam, and Zimbabwe. *KP Participants and Observers*, KIMBERLEY PROCESS, http://www.kimberleyprocess.com/web/kimberley-process/kp-participants-and-observers (last visited Nov. 16, 2012). These members account for approximately 99.8 percent of the global production of rough diamonds. *KP Basics*, KIMBERLEY PROCESS, http://www.kimberleyprocess.com/web/kimberley-process/kp-basics (last visited Nov. 16, 2012).

201. Raj, *supra* note 9, at 995–96.

202. The World Diamond Council participates in the KPCS as an observer, monitoring the effectiveness of the certification scheme and providing technical and administrative advice. *See Mission Statement*, WORLD DIAMOND COUNCIL, http://www.worlddiamondcouncil.org/about-wdc/mission-statement (last visited Nov. 16, 2012).

203. *KP Basics*, *supra* note 200. The United States is the chair of the KPCS for 2012. *Id.*

204. Recently, the KPCS has come under fire for, among other things, its continued inclusion of Zimbabwe among its members. *See, e.g.*, *Loopholes in the Kimberley Process: Illegal Trade Undermines Efforts To Combat Conflict Diamonds*, GLOBAL WITNESS, 4 (Oct. 2007), http://www.globalwitness.org/sites/default/files/import/loopholes_in_the_kimberley_process.pdf (noting that the KPCS needed to be more proactive in monitoring infringements); Press Release, Global Witness, Global Witness Leaves Kimberley Process, Calls for Diamond Trade To Be Held Accountable (Dec. 5, 2011), http://www.globalwitness.org/library/global-witness-leaves-kimberley-process-calls-diamond-trade-be-held-accountable (announcing that one of the founding NGOs in the KPCS abandoned the program because of conflict diamond trading in Cote d'Ivoire, Venezuela, and Zimbabwe, all signatories to the KPCS); *see also* Devon Maylie, *Split Opens in Body Monitoring Diamonds*, WALL ST. J., Jun. 25–26, 2011, at A11 (detailing how the KPCS leadership overrode objections from the U.S. and allowed exports of diamonds from the Marange field in Zimbabwe, an area where the Zimbabwe army seized control and allegedly committed human rights violations).

conflict diamonds to a fraction of 1 percent, as compared to estimates of up to 15 percent in the 1990s.[205]

Section 1502 and the CDTA are both legislative measures aimed at curbing trade in materials that fund rebels in Africa.[206] The goal of these measures is to establish peace and the rule of law and stem the human rights atrocities ravaging the continent.[207] There are, however, crucial differences

205. *KP Basics*, *supra* note 200.

206. Despite the similar goals of the KPCS and section 1502, there are also differences between the materials being regulated by the respective legislation. Although rough diamonds will eventually be cut and polished, they are not smelted or combined with other materials before becoming part of a final product. In this way, it is arguably easier to track diamonds in the supply chain. Diamonds in themselves are valuable and can be used as currency, unlike the 3Ts, but much like gold.

207. In passing the CDTA, Congress spelled out the human rights violations prompting legislative action. *See* Clean Diamond Trade Act, Pub. L. No. 108-19, § 2, 117 Stat. 631, 631–32 (2003) ("(1) Funds derived from the sale of rough diamonds are being used by rebels and state actors to finance military activities, overthrow legitimate governments, subvert international efforts to promote peace and stability, and commit horrifying atrocities against unarmed civilians. During the past decade, more than 6,500,000 people from Sierra Leone, Angola, and the Democratic Republic of the Congo have been driven from their homes by wars waged in large part for control of diamond mining areas. A million of these are refugees eking out a miserable existence in neighboring countries, and tens of thousands have fled to the United States. Approximately 3,700,000 people have died during these wars. (2) The countries caught in this fighting are home to nearly 70,000,000 people whose societies have been torn apart not only by fighting but also by terrible human rights violations. (3) Human rights and humanitarian advocates, the diamond trade as represented by the World Diamond Council, and the United States Government have been working to block the trade in conflict diamonds. Their efforts have helped to build a consensus that action is urgently needed to end the trade in conflict diamonds. (4) The United Nations Security Council has acted at various times under chapter VII of the Charter of the United Nations to address threats to international peace and security posed by conflicts linked to diamonds. Through these actions, it has prohibited all states from exporting weapons to certain countries affected by such conflicts. It has further required all states to prohibit the direct and indirect import of rough diamonds from Sierra Leone unless the diamonds are controlled under specified certificate of origin regimes and to prohibit absolutely the direct and indirect import of rough diamonds from Liberia. (5) In response, the United States implemented sanctions restricting the importation of rough diamonds from Sierra Leone to those diamonds accompanied by specified certificates of origin and fully prohibiting the importation of rough diamonds from Liberia. The United States is now taking further action against trade in conflict diamonds. (6) Without effective action to eliminate trade in conflict diamonds, the trade in legitimate diamonds faces the threat of a consumer backlash that could damage the economies of countries not involved in the trade in conflict diamonds and penalize members of the legitimate trade and the people they employ. To prevent that, South Africa and more than 30 other countries are involved in working, through the 'Kimberley Process', toward devising a solution to this problem. As the consumer of a majority of the world's supply of diamonds, the United States has an obligation to help sever the link between diamonds and conflict and press for implementation of an effective solution. (7) Failure to curtail the trade in conflict diamonds or to differentiate between the trade in conflict diamonds and the trade in legitimate diamonds could have a severe negative impact on the legitimate diamond trade in countries such as Botswana, Namibia, South Africa, and Tanzania. (8) Initiatives of the United States seek to resolve the regional conflicts in sub-Saharan Africa which facilitate the trade in conflict diamonds. (9) The Interlaken Declaration on the Kimberley Process Certification Scheme for Rough Diamonds of November 5, 2002, states that Participants will ensure that measures taken to implement the

in the execution of the legislative goals of these two bills. First, the CDTA came into being *as a result of* American participation in the KPCS. In other words, the international groundswell to handle the problem of conflict diamonds existed prior to the enactment of the legislation, and the United States joined an international effort by passing domestic legislation furthering the aims of the KPCS. Unlike the formidable beginning of the CDTA, there is not similar legislation to that of section 1502 in other countries nor is there an international agreement among countries to fight the exportation of conflict minerals from the DRC.[208] Instead, the United States has acted somewhat unilaterally in tackling the humanitarian crisis funded by conflict minerals in the DRC.[209]

Second, Executive Order No. 13,312 implemented the CDTA, leaving the authority over the CDTA's regulation in the hands of the executive, then President George W. Bush.[210] In his executive order, Bush assigned certain regulatory functions to the Secretary of State[211] and others to the Secretary of the Treasury (and the Treasury Department's Office of Foreign Assets Control).[212] In addition, the CDTA authorizes the Bureau of Customs and Border Protection to enforce the import and export regulations.[213] Section 1502, on the other hand, will be partially regulated by the SEC. It is only "partially" regulated because if an issuer determines—correctly or not—that its product does not contain any conflict minerals, it will not issue a conflict mineral report at all, and the SEC likely will not have the resources to investigate all companies furnishing conflict mineral reports, let alone all companies *failing* to furnish the report.[214] Unlike the CDTA, which spreads responsibility of enforcement across agencies best equipped to handle certain tasks, section 1502 tasks the SEC with regulation of the entire conflict mineral compliance scheme.

Kimberley Process Certification Scheme for Rough Diamonds will be consistent with international trade rules.").

208. Although not a binding international agreement, the OECD has issued guidance for due diligence on supply chains for conflict minerals. *See supra* Part II.C.3.

209. Some advocates of section 1502 attest that international action is being taken. For instance, the U.N. report issued in November 2011 stated that Rwandan border officials returned eighty tons of intercepted minerals to Congolese authorities due to improved traceability of parcels of cassiterite, coltan, and wolframite. U.N. Secretary-General, *A Report of the Secretary-General on the United Nations Organization Stabilization Mission in the Democratic Republic of the Congo*, U.N. Doc. S/2012/65 13 (Jan. 26, 2012), *available at* http://daccess-dds-ny.un.org/doc/UNDOC/GEN/N12/206/29/PDF/N1220629.pdf.

210. Exec. Order No. 13,312, 68 Fed. Reg. 45,151 (July 29, 2003).

211. The State Department is responsible for waiving the KPCS requirements if it is in the country's national interests; conducting an annual review of the efficacy of the KPCS; publishing a list of all KPCS participants in the Federal Register; creating and coordinating the Kimberley Process Coordination Committee; and providing annual reports to Congress. The Secretary of the Treasury is responsible for recordkeeping and issuing any licenses or regulations necessary for carrying out the CDTA. *Id.*

212. *Id.*

213. Clean Diamond Trade Act, Pub. L. No. 108-19, § 8(c), 117 Stat. 631, 631–32 (2003).

214. *See supra* Part II.C.

Moreover, the Department of State and the Office of Foreign Assets Control (OFAC) of the Treasury Department are a better fit for conflict mineral regulation. These entities handle international affairs and, in the case of OFAC, existing sanctions programs. Because the stated aim of section 1502 is to exact diplomatic and humanitarian results, the regulatory body should be one more adept at effectuating these types of goals. The SEC, as noted above, is not concerned with international human rights or diplomacy issues and should not have its resources tapped to regulate section 1502.

CONCLUSION

What is clear about section 1502, both from the legislative history and the text of the provision itself, is that its goals are diplomatic and humanitarian. Although these goals are lofty and admirable, Congress should not place the burden of achieving these goals on the SEC. Additional disclosure requirements aimed at effecting diplomatic ends do not comport with the traditional financial disclosure requirements mandated by section 13, nor do they effectively solve the international crises they seek to alleviate. Further, the costs associated with the regulation, as well as the direct and indirect effects of the legislation on the DRC and adjoining countries, are only some of the reasons that section 1502 is an ill-advised provision of Dodd-Frank. In sum, the burden of diplomatic and humanitarian aid should come from agencies and groups that can better shoulder the formidable responsibility of peacemaking in the DRC.