

Trade in Conflict Minerals -- Congolese Warlords, MNC's, and Dodd-Frank 1502

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Since the start of the First Congo War in 1996, the Democratic Republic of Congo (DRC) has remained in a state of perpetual political and economic instability. Caused by a spillover of conflict from the Rwandan genocide into the DRC (then named Zaire), the Congolese Wars took place over a span of seven years (1996 - 2003) and are the primary factor contributing to the instability within the region (Schneider, 2011). Conflict remains rampant — even after the official conclusion of the Congolese Wars in 2003 — as several warlord-led militias seek to gain control of the DRC's massive mineral reservoirs (Schneider, 2011). These minerals are dubbed “conflict minerals,” due to their part in funding conflicts within the DRC; at their peak in 2008, intrastate wars over conflict minerals in the DRC “killed 45,000 people a month” (Polgreen, 2008). Conflict minerals are undoubtedly the DRC's “resource curse”, as the elevated level of demand for these minerals fuels conflict between rebel groups seeking to control mineral rich land and plunges the country further into instability. The international trade in conflict minerals is profitable for both sellers — rebel militia groups — and buyers — multinational corporations (MNCs) — thanks to favorable prices and the difficulty involved in tracing legitimate buyers to

illegal sellers. Although Section 1502 of the Dodd-Frank Act attempts to suffocate the trade, it is unable to impact illegal sellers of conflict minerals; instead, it harms legitimate miners and mining corporations.

Tin ore (cassiterite), tungsten, tantalum (extracted from columbite-tantalite), and gold — collectively referred to as 3TG minerals — are the raw materials classified as conflict minerals due to their extraction from militia-controlled mines. (Deloitte, 2018). The DRC houses the world's largest deposits of these minerals as its mines contain several billion pounds worth “around \$24 trillion” (Paulas, 2017). The astronomical value assigned to 3TG minerals is a result of their necessity in the supply chains of electronic devices. 3TG minerals are essential in the process of constructing batteries, circuit wires, and processor chips due to their high conductivity and resistance to corrosive substances (Reuters, 2017). Without these minerals, devices such as computers, phones, televisions, and tablets could not properly function. As such, 3TG minerals are the DRC's most valuable factor endowments and have the potential to generate copious amounts of revenue if properly exported. As it currently stands, warlord-led militia groups control around a third of the DRC's mines and other natural repositories (Wolfe, 2015). Much of the DRC's export revenue concerning minerals and ores is not accrued by legitimate state-approved actors — and therefore not reflected in economic data — but by militia

groups instead (CIA, 2018). Consequently, the DRC cannot utilize the entirety of its vast amount of natural resources and put funding towards developing infrastructure, establishing affordable healthcare, or providing quality education.

The international conflict mineral trade market contains several actors, including smelting/refining corporations, intermediary traders, mineral transporters, and component producers (which are companies that make basic mechanisms and devices and sell them to end product producers) (Deloitte, 2018). However, the major economic players in international conflict mineral trade are the Congolese warlord-led militia groups and tech-centric multinational corporations operating outside of the DRC. Both actors wield the most power out of all other groups involved, engage in the conflict mineral trade market to sustain their respective operations, and mutually benefit from trade.

While they “only control [around] 33 percent of the mines within the DRC,” warlord-led militia groups still control land which contains billions of dollars in untapped mineral reserves (Paulas, 2017; Wolfe, 2015). The militia groups have no need for 3TG minerals as resources to utilize in building or repairing electronic devices. Instead, they extract and sell conflict minerals on the black market, using them to obtain munitions, food, and medical supplies (Paulas, 2017). Conflict minerals aid militia groups in solidifying their regional dominance and are simply the most profitable and accessible resources for them.

During the price spike of columbite-tantalite in 2000, about “\$20 million a month went to rebel groups” to finance their war efforts (Schneider, 2011). The main reason why militias can conduct such an operation while turning a massive profit is due to their low operating and opportunity costs. Essentially, militias have a comparative advantage in the extraction of 3TG minerals. Labor costs are non-existent and any physical capital needed is forcibly taken. Militias regularly take over existing mines and utilize their labor force, which usually consists of children and teenagers forcefully conscripted from the surrounding villages (Blanco, 2016). This allows militias to specialize in mineral extraction and trade minerals in exchange for products they need. Sometimes, militia groups choose not to dig for minerals themselves, instead selling individual diggers access to mining pits they control and taking a sizable percentage of the minerals these diggers discover (Raghavan, 2014). After extracting the minerals, militia members sell them to legitimate traders by bribing underpaid public officials to certify their minerals via the “tag and bag” system, which involves “tying a small plastic tag around a bag of minerals to [mark] it as ‘clean’” (Wolfe, 2015).

Although they never directly interact with the militia groups supplying 3TG minerals, MNCs are the second major economic player in the international conflict mineral trade. MNCs that manufacture electronic devices at the end of the supply chain especially rely on cheap and reliable sources of 3TG minerals. In particular,

major technology conglomerates such as Google, Apple, Intel, IBM, Microsoft, and Samsung often turn a blind eye and use “minerals sold to fund combatants in the [DRC]” in the manufacture of their products (Luckerson, 2014). MNCs are undoubtedly the most powerful actors in the conflict mineral trade market due to their financial strength. As the dominant players in the market, MNCs have the luxury of dictating the flow of minerals in accordance with their needs. In accordance with Wallerstein’s core-periphery model (which states that rich, “core countries” dictate the global flow of resources), MNCs based in rich countries control the amount of 3TG minerals suppliers in “periphery countries” (like the DRC) can sell (Lee, 2014). Suppliers in these countries solely rely on the demands of these MNCs. Coltan, the primary component in processor chips, only costs around \$69 per pound, a relatively low cost when one considers the number of chips manufactured using a pound of coltan (each processor only uses a couple grams of coltan) (Metalary, n.d). While other areas like Afghanistan, Australia, and Canada also contain 3TG minerals, acquiring these minerals from the DRC is much cheaper and far less restrictive (Rockwood, 2012). Thanks to the emergence of economic globalization, the supply chains of MNCs engaging in the conflict mineral trade are extremely convoluted. “After minerals are mined, they are sold to a middleman and usually taken to the country’s capital,” where the metals are extracted and blended with other elements (Reuters, 2017). These blended compounds are then exported to

countries where they are further refined and prepped for use in end products (Reuters, 2017). As of 2017, Apple purchases 3TG minerals from smelting and refinery corporations in several — primarily east Asian — countries such as China, Indonesia, Japan, and South Korea (Apple, 2017). During this process, the minerals change hands several times. This divides the cost of processing minerals among multiple actors and reduces the overall price paid by MNCs (Reuters, 2017). As such, it is difficult for auditors — and even the MNCs themselves — to trace the minerals down the supply chain and determine if they originate from an illegitimate mining operation (Reuters, 2017).

While militia groups and MNCs gain from the conflict mineral trade, it negatively impacts Congolese laborers and miners working for legitimate mining operations. In the DRC, around “8 to 10 million people rely on mining to earn a living (Wolfe, 2015). Particularly in the eastern Congo, mining is one of the only existing economic activities following the infrastructural destruction by the Congolese civil wars and militia violence (Reuters, 2009). Legal mining operations are costly to operate and cannot compete with militia groups, which can afford to sell their minerals at far lower prices. As a result, legal mining operations significantly lower their prices; in 2010, “miners were selling a kilogram of tin — about two pounds — for \$7 [although] the world market price averaged \$18 dollars a kilo” (Raghavan, 2014). Due to this competition, miners only earn one to five

dollars a day, which constitutes around fourteen hours of manual labor (Wolfe, 2015). Many of the miners are women, who support themselves and their children through their meager earnings (Wolfe, 2015).

However, artisanal miners are the ones most prominently impacted by the conflict mineral trade market. They operate independently, neither under the jurisdiction of a mining corporation nor under the control of militia groups (Blanco, 2016). As a result, they earn the equivalent of less than one dollar per day and are at risk for attacks by militia groups looking to seize control of the mine (Blanco, 2016). These mines are also rife with smuggling. In 2013, around “\$400 million in gold was smuggled out [from] artisanal mines” (Raghavan, 2014). The state of the “conflict-free” mineral industry in the DRC exemplifies dependency theory (which explores the cyclic relationship between developing countries that provide raw resources and developed countries that provide finished goods). The DRC, as a developing country, supplies raw goods to developed countries at very low prices, thus bolstering the economic growth of the developed countries. Meanwhile, the DRC’s own development stagnates, as it (an other such developing countries) often cannot afford to purchase the finished goods acquired from developed countries, which prevents the modernization of its own economy.

The conflict mineral trade market has not gone unnoticed by governments. Currently, the most definitive reformatory

legislation implemented toward regulating the conflict mineral trade is Section 1502 of the United States’ Dodd-Frank Wall Street Reform and Consumer Protection Act, signed into law on July 21, 2010, Section 1502 “imposes additional reporting requirements on U.S. companies regarding their sources of certain ‘conflict minerals’” (Ayogu & Lewis, 2016). It attempts to cut off the flow of money, which aides conflict mineral suppliers and (by extension) “financ[es] conflict in the DRC region” (Davis, 2017). Becoming law in 2014, Section 1502 requires MNCs that participate in an industry where conflict minerals are “necessary to the functionality or production” of their products to file paperwork with the Securities and Exchange Commission (SEC) and publish an annual conflict minerals report (Ayogu & Lewis, 2016). To properly complete this report, MNCs must thoroughly examine their supply chain, conduct “third-party verification” (hire a third party to audit their trade policies), and list whether the areas from which they acquire 3TG minerals are conflict-free (Ayogu & Lewis, 2016). The purpose of Section 1502 is to publicize their mineral supply chain, thereby exposing any connections to DRC militia suppliers. By forcing MNCs to publicly state whether their products contain DRC conflict minerals, Section 1502 uses the “name and shame” tactic — impacting the corporation’s “brand” and letting consumers determine whether to continue utilizing the offending MNC’s goods and services (Ayogu & Lewis, 2016). Furthermore, the compliance costs MNCs incur by having to adhere to

Section 1502 “fall between \$9 billion and \$16 billion,” attempt to incentivize MNCs in quickly finding conflict-free sources of 3TG minerals (Ayogu & Lewis, 2016). Section 1502 — and the Dodd-Frank Act in general — signifies a shift away from a liberal economic mindset. Instead, Section 1502 is a more realist economic policy, designed to introduce some amount of government regulation that directs how companies should interact in the economy.

Nearly eight years after it passed into law — and four years after its full implementation — controversy surrounds Section 1502 of the Dodd-Frank Act. One charge levied against Section 1502 is that it is far too lenient on MNC, as they simply do not face enough penalties for non-compliance (Paulas, 2017). An independent study that “analyzed every conflict minerals report submitted to the SEC in 2014, 2015, and 2016” categorized each MNC analyzed into one of three groups: “DRC conflict-free” (for MNCs that certified their minerals as 100% conflict free), “no reason to believe [use of conflict minerals]” (a lower standard which implies some level of uncertainty), and “DRC conflict undeterminable” (for MNCs that could not determine where their minerals were sourced from) (Davis, 2017). Only about 1% of the MNCs were classified as “DRC conflict free”, while 19% categorized as “no reason to believe,” and the remaining 80% fell in the “DRC conflict undeterminable” category (Davis, 2017). Most companies which fall under Section 1502 (like Apply, Google, and Samsung)

can absorb the compliance costs, due to their financial robustness. Furthermore, the “name and shame” tactic, which relied on the free market and consumer public to cut profits from MNCs utilizing DRC conflict minerals, was relatively ineffective (Paulas, 2017). The failure of Section 1502 to regulate the behavior of MNCs challenges the notion of whether it succeeds in promoting a realist economic policy.

The second charge levied against Section 1502 is that rather than preventing militia groups from profiting off of conflict minerals, it hurts the Congolese miners working for legitimate mining operations. Although there was a correlation between “[militia] groups’ loss of control and [Section 1502’s] implementation,” many politicians and academics believe that this was due to the increase in “U.N. and Congolese army missions fighting rebel groups” (Wolfe, 2015). Since the act has not encouraged substantive efforts from MNCs to thoroughly audit and restructure their supply chains, militia groups are still able to sell their conflict minerals via smuggling, bribery, or the utilization of several intermediary traders (Paulas, 2017). The prices of conflict-free 3TG minerals have therefore dropped as smelters and refineries fear being labeled as users of conflict minerals (Raghavan, 2014). The price miners earn from conflict-free tin dropped from a price of \$7 per kilo in 2010 to \$4 per kilo in 2014, even though the global market price rose from \$18 per kilo to \$22 per kilo during that same period. Although MNCs fail to sufficiently comply with Section

1502, the Congolese government initially forced Congolese mining operations and traders to comply with Section 1502 and initiate a process which would certify their minerals as conflict-free. As a result, legitimately operated mines shut down for several months. Consequently, foreign smelting and refining companies avoided buying minerals from these mines, thus driving down the price of minerals (Raghavan, 2014). In the DRC, Section 1502 is known as “Loi Obama” (Obama’s Law) and viewed to be a well-intentioned but economically disastrous American law that influenced the Congolese government into enacting detrimental domestic mining policies (Raghavan, 2014). This phenomenon reflects the failure of both the American government and intergovernmental organizations (IGOs) such as the World Trade Organization (WTO) to account for side effects that negatively impact a benign party. Their failure reinforces the argument of critics who state that the WTO and other IGOs are ineffective in assisting developing countries and are only capable of supporting policies that favor developed countries.

In February 2017, the Trump administration prepared an executive order that proposed a “two-year suspension of” the Section 1502 Dodd-Frank financial reforms (Pilkington, 2017). Although passed by the House of Representatives, it still requires confirmation from the Senate. The proposal agrees with the critics of Section 1502 and states that there is “‘mounting evidence’ that the obligation on US firms to prove to

regulators that they are not involved in blood minerals has ‘caused harm to some parties in the Democratic Republic of the Congo’” (Pilkington, 2017). The proposed suspension is extremely divisive, garnering support from critics of Section 1502 and receiving intense criticism from human rights groups who believe that Section 1502 is beginning to see some success (Pilkington, 2017). Additional criticism toward the suspension comes from critics who believe that such action would hold MNCs even less responsible and allow them to renege on the (previously agreed upon) supply chain transparency. Almost simultaneously (in May 2017), the European Union (EU) voted to adopt new import regulations on conflict minerals. The EU Conflict Minerals regulation targets “[3TG] minerals originating from conflict-affected or high-risk areas without being limited to specific geographical locations” (Deloitte, 2018). The act directly applies to corporations — only those which have headquarters in the EU — which import 3TG minerals into the EU, no matter where these metals originate from (Europa, 2017). With an application date of January 2021, the EU regulations are based on Section 1502 of the Dodd-Frank Act and impose similar conditions, such as supply chain inspection and publication of annual audits (Europa, 2017). Like Section 1502, the EU regulations currently have no mechanism in place for penalizing corporations that either refuse to comply with the act or utilize conflict minerals.

The future of the conflict mineral trade market is mired in uncertainty and indecision. Militias continue to wage war in the DRC, and MNCs still acquire cheap 3TG minerals for their products, with both parties engaging in indirect but mutually beneficial trade. Meanwhile, the United States and the European Union remain on the verge of implementing two opposing sets of laws, and it appears that governments are extremely conflicted on how to best stifle conflict mineral trade. As a result, legitimate Congolese mining operations and miners continue to feel the burden of low prices, are crowded out by the conflict mineral trade, and face low demand for their minerals as buyers from both the US and the EU wait for their governments' to ratify effective mineral trade policies. For a paradigm shift to occur, coordinated and homogenous action on the parts of both federal governments and IGOs is necessary to concretely enforce restrictions on conflict mineral trade. A successful end scenario would eliminate militia groups from the equation and involve mutually beneficial trade between MNCs and legitimate Congolese mining operations.

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