

Bill Number: SB 861 (Corbett) as amended July 13, 2011

SUMMARY

SB 861 prohibits a scrutinized company, as defined, from bidding or submitting a proposal for a state contract for goods or services, if the company has had a final judgment filed against them by the U.S. Securities and Exchange Commission (SEC) related to the Democratic Republic of Congo and conflict minerals disclosure.

BOARD POSITION

NEUTRAL. Currently, companies seeking contracting opportunities with CalSTRS that have had business activities outside of the U.S. within the past 3 years must certify under penalty of perjury that they are not a scrutinized company in order to be eligible to submit a bid or contract proposal.

This bill redefines a scrutinized company as being in violation of Section 13(p) of the Securities and Exchange Act of 1934 and ineligible to bid on or submit a contract proposal with a state agency if the company has had specific business activities concerning conflict minerals originating in the Democratic Republic of Congo, or adjoining countries. To that degree, this bill does not require CalSTRS to make a determination as to the validity of a company submitting a bid or proposal for a contract is a scrutinized company.

It is the policy of the Board to be neutral on legislation that does not significantly or adversely impact the benefits or services through the funds administered by CalSTRS or the administration of the retirement plans.

SUMMARY OF AMENDMENTS

The Amendment of July 13, 2011:

- Modifies the public contract code relating to the point at which a person will no longer be regarded as a “scrutinized company” to also include when the person files an amended or corrective filing with the SEC that corrects the specified violation.
- Directs Department of General Services (DGS) to establish in the State Administrative Manual or the State Contracting Manual policies and procedures for all state agencies, departments, boards, and commissions to implement the contract prohibition.
- Clarifies that the prohibition also applies to state contracts relating to information technology and communication contracts.

PURPOSE OF THE BILL

To prohibit publicly traded companies that fail to comply with the Dodd-Frank Wall Street Reform and Consumer Protection Act from obtaining procurement contracts with the State of California through the DGS until they comply with the law.

ANALYSIS:**Existing Law:**

The State Contract Act authorizes contracting between state agencies and private contractors and sets forth the requirements for the procurement of goods and services and for the solicitation of bids and the awarding of contracts by public agencies. Current law also prohibits companies involved in specified business activities in Sudan and Iran from entering into a contract with a state agency for goods and services and requires a prospective bidder for a state contract to certify that the company is not engaged in such activities. Current law also specifies penalties for submitting a false certification.

This bill:

SB 861 prohibits a scrutinized company, as defined, from entering into a contract with a state agency for goods or services, as provided. A scrutinized company is a person that has been found to be in violation of Section 13(p) of the Securities and Exchange Act of 1934 by final judgment or settlement entered in a civil or administrative action brought by the SEC and the person has not remedied the violation in a manner acceptable by the commission on or before final judgment or settlements.

SB 861 also states that a person shall cease to be regarded as a scrutinized company when the person is no longer deemed to be in violation of Section 13(p) of the Act, or upon filing an amended or corrective filing which corrects the violations, or after three years from the date of final judgment or settlement, whichever is earlier.

SB 861 directs DGS to establish in the State Administrative Manual or the State Contracting Manual policies and procedures for all state agencies, departments, boards, and commissions to implement the contract prohibition of this section of law. The bill clarifies that the prohibition also applies to state contracts relating to information technology and communication contracts. According to the Assembly Jobs, Economic Development and the Economy Committee, the SEC will maintain a public list of companies that have been found to be in violation of the Act and that a final judgment, settlement or administrative action has been brought by the SEC. State contracting staff will need to be directed on how to best access that information and check on whether the company has subsequently remedied or cured the violation.

There would be no real changes to the current CalSTRS procurement, contracting and purchasing practice. Until DGS publishes its policies and procedures in the State Administrative Manual or State Contracting Manual for state agencies to implement the contract prohibition, CalSTRS would need to develop language to include in the contract boilerplate template for purposes of self-certification that the contract bidder is not a scrutinized company involved with specific business activities concerning conflict minerals originating in the Democratic Republic of the Congo, or adjoining countries. It

is unknown how many SEC regulated companies might be restricted from bidding on state contracts.

In 2010 similar legislation, Chapter 573, Statutes of 2010 (AB 1650, Feuer) prohibited a person who is engaged in investment activities in the energy sector in Iran from bidding on, entering into or renewing a contract with a state agency or public entity for goods or services. The board adopted a neutral, if amended position to exclude from the definition of a person who is engaged in investment activities in Iran, an investment firm that does not invest California public pension funds in the energy sector in Iran and to add the provision that CalSTRS shall take action that is consistent with the fiduciary responsibilities of the Board. In 2008 the board adopted a neutral position on similar legislation, Chapter 272, Statutes of 2008 (AB 498, Hernandez), that prohibits companies involved in specific business activities in Sudan from entering into contracts with state agencies.

LEGISLATIVE HISTORY

HR 4173 (Frank, Public Law 111-203) enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act and among other things, amended the Securities Exchange Act of 1934 to direct the SEC to issue regulations requiring persons for which conflict minerals are necessary to the functionality or production of a product manufactured by that person to make annual disclosures of whether any such conflict minerals originated in the DRC or an adjoining country. Requires the report, regarding any minerals that did originate in the DRC or an adjoining country, to describe: (1) due diligence measures taken on the source and chain of custody of such minerals; and (2) the products manufactured, or contracted to be manufactured, that are not DRC conflict free.

AB 1650 (Feuer, Chapter 573, Statutes of 2010) enacted the Iran Contracts Act of 2010 which prohibited a person from bidding or renewing contract with a public agency entity for goods and services of \$1 million who is identified on a list maintained by the Department of General Services (DGS) and engaging in investment activities in Iran, as specified (applies to a person that provides goods and services for \$20 million). This bill also prohibited a person or entity that is a financial institution that extends \$20 million or more in credit to another person, for 45 days or more, if the person will use the credit to invest in the energy sector in Iran from bidding or renewing a contract with a public entity for goods and services of \$1 million or more, and is also identified on the DGS list as a person engaging in investment activities in Iran. Required DGS to develop this list by June 1, 2011 and update it every 180 days as specified. This bill states the intent of the Legislature to implement the authority granted in H.R.2194, 111th Congress (2009-2010), the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010.

AB 961 (Krekorian, 2009) prohibited "scrutinized companies," i.e. those that were engaged in business with perpetrators of specified genocides that still hold looted or deposited assets of genocide victims or their heirs, from bidding on or submitting proposals for contracts with state agencies.

AB 498 (Hernandez, Chapter 272, Statutes of 2008) required a company that bids or submits a proposal for a contract for goods and services with a state agency to self-certify that it is not a scrutinized company engaged in specified activities in Sudan. The Director of General Services would be able to permit a scrutinized company to bid on or

submit a proposal for a contract with a state agency if it is determined that it is in the best interest of the state to permit the company to do so. The Department of General Services would be required to report the name of the company to the Attorney General in cases where it determines that a company has submitted a false certification that it is not a scrutinized company.

AB 1089 (Hernandez, 2006) required DGS to identify a list of companies that have substantial business operations with the government of Sudan or are associated with the "Darfur genocide" and prohibits state entities from entering into contracts exceeding \$100,000 with such companies.

PROGRAM BACKGROUND

The Legislature has required state contracts to include various terms and conditions designed to ensure that public funds are not used to support illegal and/or immoral acts, such as prohibiting discrimination, and others that support positive actions and efforts by state vendors, such as requiring contractors to maintain a drug free workplace. These terms and conditions are agreed to by the contractor and enforced as part of an executed written contract.

This measure is in response to the conflict and related humanitarian crisis in the Democratic Republic of Congo that has resulted in the deaths of an estimated 5.5 million people since 1998, the intervention of multiple armed forces from other countries in the region and the mismanagement and illicit trade of extractive resources supporting the conflict between militias and armed domestic factions in neighboring countries. Desire for the Congo's mineral wealth has been a prime cause of the atrocities and conflict, and multiple armed groups use mass rape as a strategy to intimidate and control communities as they profit from the illicit trade of Congo's conflict minerals, such as tin, tungsten, and tantalum. Many of these same conflict minerals end up in our electronic devices such as cell phones, laptops, and digital cameras. United Nations Security Council Resolution 1857, unanimously adopted on December 22, 2008, broadens existing sanctions relating to the Democratic Republic of Congo to include "individuals or entities supporting the illegal armed groups... through illicit trade of natural resources".

The Dodd-Frank Wall Street Reform and Consumer Protection Act was signed into law by President Barack Obama on July 21, 2010. This law requires those who file with the Securities Exchange Commission (SEC) and use minerals originating in the Democratic Republic of Congo in manufacturing to disclose measures taken to exercise due diligence on the source and chain of custody of the materials and the products manufactured.

CalSTRS currently obtains most routine office supplies under a state contract entered into by DGS with a private vendor. For other goods, CalSTRS solicits price quotes from two or more vendors and selects the lowest responsive bidder. For purchases greater than \$25,000 CalSTRS conducts a more formal request, which incorporates any special terms or conditions, and the lowest responsive bidder is awarded the contract. Among the contracts that CalSTRS enters into are those with outside investment managers to manage approximately \$92 billion of the CalSTRS portfolio.

FISCAL IMPACT

Program Cost – No program cost associated with this bill.

Administrative Costs/Savings – The cost of implementing the change to the contracting process is minimal as it will only require an additional clause to be added to current contract language. Costs would be minor and absorbable because we currently have similar certification language for other contract certifications required by statute.

ECONOMIC IMPACT

The conflict in eastern Congo – the deadliest since World War II – is fueled in significant part by a multi-million dollar trade in minerals. Armed groups generate an estimated \$144 million each year by trading four main minerals: the ores that produce the metals tin, tantalum, tungsten, and gold. These minerals eventually wind up in electronic devices used every day, such as cell phones, portable music players, and computers, including those sold here in the United States. Given the lack of a transparent minerals supply chain, American consumers may be unwittingly financing armed groups that regularly commit atrocities and mass rape.

This legislation aims to help curb the multi-million dollar trade in illegally extracted minerals from eastern Congo by incentivizing company compliance with federal regulations; influencing the State's electronics industry leaders as they decide whether or not to invest in the Democratic Republic of the Congo and ensure that their supply chains are transparent. SB 861 could help neutralize one of the key economic drivers of the conflict in Congo and protect the country's children from a future stigmatized by violence and brutality.

SUPPORT/OPPOSITION

Support:

The International Corporate Accountability Roundtable (sponsor)
Enough! (sponsor)
Action Evangelique En Prison, Democratic Republic of the Congo
Africa Faith and Justice Network
Amnesty International
Boston Common Asset Management
California Church IMPACT
California Coalition Against Sexual Assault
California Commission on the Status of Women
California National Organization for Women
California Province of the Society of Jesus
Calvert Asset Management Company, Inc.
Catholic Health East
Christian Brothers Investment Services
City of Berkeley
City of West Hollywood
Coalition for Free and Democratic Elections in Congo
Coalition to Abolish Slavery & Trafficking
Congregation of Sisters of St. Agnes, Fond du Lac, WI

Consumer Federation of California
Dominican Sisters of San Rafael
Earth Rights International
Enough Project
Falling Whistles
Feminist Majority
Free the Slaves
Gavin Newsom, Lieutenant Governor
Global Witness
Howard Berman, Congressman
Human Rights First
Human Rights Watch
Interfaith Center on Corporate Social Responsibility
International Corporate Accountability Roundtable
Investor Environmental Health Network
Jewish World Watch
Marianist Province of U.S.
Midwest Coalition for Responsible Investment
PaxWorld Management, LLC
Program for Torture Victims
Responsible Sourcing Network
Sister of the Holy Family
Sisters of St. Francis of Philadelphia
Sisters of St. Joseph of Springfield, MA
Social Investment Forum
Social Responsibility Coordinator JOLT
Spring Water Asset Management
St. Mark Presbyterian Church, Newport Beach
Stop Genocide Now
The Social Equity Group
The Sustainable Group at Loring, Wolcott & Coolidge
Trillium Asset Management Company
Tri-State Coalition for Responsible Investment
US Social Investment Forum
Union for Democracy and Social Progress
Union Pour La Democratie Et Le Progres Social
Zevin Asset Management, LLC

Opposition:

None known

ARGUMENTS

Pro: Would stop California contracts from going to companies that fail to comply with Federal reporting requirements to combat the trade of minerals fueling conflict in the eastern Democratic Republic of the Congo.

Would push California to be the first state to go "Conflict-Free" in its procurement of public contracts for goods and services.

Con: This measure could prohibit CalSTRS from hiring investment managers who invest other institutional investors' funds in the Republic of the Congo, which would limit the universe of possible investment managers for CalSTRS to hire.

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