

# LME position paper on responsible sourcing: feedback analysis



SETTING THE GLOBAL STANDARD



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## 1. EXECUTIVE SUMMARY

On 5 October 2017, the LME released – via Notice 18/257 (“LME position paper on responsible sourcing, 5 October 2018, the “position paper”) – a position paper outlining its proposals in respect of responsible sourcing. These proposals were designed to ensure that metal eligible for delivery against LME contracts (LME-listed brands) appropriately embodies the responsible sourcing standards expected by the global industry. The paper provided the LME’s analysis in respect of the background and context of the ongoing debate on responsible sourcing and explored work undertaken to date. It also outlined the LME’s rationale for taking action now, and included the results of the 2017-2018 responsible sourcing survey undertaken with the producers of all LME-listed brands. Finally, the paper asked for market feedback on the proposal laid out for the incorporation of responsible sourcing standards within the LME’s existing physical specification requirements for listed brands.

The LME would like to thank the 39 market participants who provided written feedback to the position paper, as well as all those who contacted the LME and provided their ideas and thoughts through meetings and calls. The Exchange very much appreciates the time and effort taken by all those who contributed.

The LME has taken all the feedback received into careful consideration, and this paper explores that feedback in detail, and explains the amendments the LME is proposing to make to its original proposal on the basis of such feedback and the LME’s own analysis. It also outlines that feedback which it has not incorporated into its broader proposals and provides a rationale for these decisions.

Further, the LME is also outlining its next steps in respect of responsible sourcing, and has today published a consultation on proposed amendments to the LME Rulebook to introduce responsible sourcing requirements for LME-listed brands (the “Responsible Sourcing Consultation”), under Notice 19/130 (“Next steps for LME responsible sourcing”). The consultation period will run for two months and the LME welcomes all feedback from market participants in relation to this. Any market participant wishing to submit a response to the Responsible Sourcing Consultation, or to arrange for further discussions seeking clarification in relation to such, is asked to contact Hugo Brodie at [responsiblesourcing@lme.com](mailto:responsiblesourcing@lme.com), or +44 20 7113 8766.

## 2. FEEDBACK TO THE POSITION PAPER

In broad terms, the majority of responses provided to the position paper were highly supportive of the initiative, and encouraged the LME to implement responsible sourcing requirements while ensuring that market disruption and unintended consequences are minimised. More specifically, a smaller set of respondents called on the LME to ensure that any implemented requirements do not discourage the sourcing of metal from higher-risk areas, notwithstanding the proviso that such sourcing is conducted in accordance with global standards. The LME fully agrees with these priorities, believes that they are core to its proposal, and will continue to work with the market to ensure the alignment of its approach as such.

While supportive of the LME's intentions and the broad outline of its route forward, many respondents also offered suggestions as to how the LME's proposal could be refined to ensure that it both reflects best practice in terms of responsible sourcing standards, but equally remains practical and achievable in respect of implementation by LME brands. These suggestions focused on five main areas of the proposal and this paper will consider each of these areas in turn, alongside a sixth section to cover additional comments not otherwise categorised as follows:

- Proposed scope of the LME requirements
- Considerations around the red flag assessment
- Considerations around responsible sourcing standards
- Considerations around the separate provisions for cobalt and tin
- Timeline
- Other considerations

### 2.1. Proposed scope of the LME requirements

The LME went into some detail in the position paper as to the proposed scope for its responsible sourcing initiative, and its rationale for that scope<sup>1</sup>. This section is not designed to reiterate that analysis, but rather to address the specific questions raised by respondents. These were largely focused on achieving clarity in terms of the inclusion of (i) secondary material, (ii) by-products, (iii) third party suppliers including transportation and logistics, (iv) environmental standards, and (v) potential scope changes in the future. These topics notwithstanding, for the sake of clarity the LME would also like to take this opportunity to confirm which of the metals contracts listed on the LME for trading are included in its proposal. These requirements would apply to all physically settled LME contracts, including aluminium, aluminium alloy, North American Special Aluminium Alloy Contract ("NASAAC"), copper, lead, zinc, tin, nickel and cobalt. The LME's ferrous contracts are cash settled so are out of scope, as is LME Molybdenum, which was converted from a physically settled to a cash settled contract by the LME on 11 March 2019. Finally, although LMEprecious contracts are physically settled for both gold and silver, the contracts are settled via the loco London vaulting process which is outside of the LME's direct control.

The most significant area of discussion in respect of scope was in reference to secondary materials. A number of respondents pointed to work undertaken by organisations such as the London Bullion Market Association ("LBMA") and the Aluminium Stewardship Initiative ("ASI") as examples of how requirements to ensure the responsible sourcing of secondary (or scrap) material can be incorporated within a responsible sourcing scheme or standard. In general, these respondents were

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<sup>1</sup> Please see in particular Section 5.2, "Principles underlying the LME proposal", for more detail

in favour of including such material within the LME's scope immediately, with a smaller number proposing either a delayed implementation for secondary material, or an amended set of requirements to take into account the specificities of such material.

However, a much broader group, including those advocating for a reduction in scope, argued for the exclusion of secondary material, pointing out that the Organisation for Economic Co-operation and Development ("OECD") Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas ("OECD Guidance") supplement on tin, tantalum and tungsten (the "3T supplement") – the basis for the LME's own scope – does not include such material and, as a result, this should be out of scope for the LME also. The LME is in agreement with this assessment, and feels that the arguments in favour of including these materials, while understandable, do not outweigh concerns about practicality or the more theoretical debate about the principle of imposing responsible sourcing standards on metal sourced before such requirements were in place. As such, the LME is not minded to deviate from the OECD Guidance scope, which is clear on this point. That said, the LME does agree that some existing standards have found meaningful ways to include such material in their scope, and would propose to keep secondary material in mind for any future expansion of its requirements, dependent on market demand and notwithstanding the arguments in respect of such expansion as outlined below.

In respect of by-products, concerns here were largely focused on clarifying that materials not considered to be a core component of the metal would be out of scope. By way of illustration, for aluminium, core components would include bauxite and alumina but not, for example, lime. The LME agrees with this assessment and further, believes that this is consistent with the broad market understanding on this topic. Accordingly, the LME considers that such by-products, and their associated supply chains, are not within its scope.

Similarly, the LME also does not consider that supply chain due diligence, for the purposes of the LME's requirements, includes transportation companies or other logistics suppliers. However, for the avoidance of doubt, companies within a specific supply chain which are responsible for producing or supplying material are included, as this analysis is core to the OECD Guidance. The LME accepts that obtaining this information from third party suppliers will, in some cases, be challenging, but it does not believe that this obviates the importance of this information in order to achieve a meaningful red flag or standards assessment.

The final two points of debate in this area relate more broadly to the areas of responsible sourcing included in the LME's requirements – as discussed in the position paper, based primarily on the OECD Guidance – and how, and when, these might change in the future.

As alluded to above, a number of respondents questioned specifically whether the LME should include requirements relating to environmental standards in its responsible sourcing proposal, arguing that work to progress a sustainable agenda is sufficiently well established to compel such an outcome. Strong proponents of this argued that the LME's proposal was not sufficiently ambitious and did not accurately reflect the expectations of the downstream consumer market. Equally, a number of respondents took the opposing position, and pointed out that this position (notwithstanding the proposed requirement for ISO 14001, discussed further below in Section 2.3.6) was in line with the OECD Guidance, and further, avoided what they saw as the significant issue which would arise if a substantial number of LME brands were unable to meet such requirements. As an example provided by one respondent, should such requirements preclude the use of coal produced products, an estimated 67% of world production of aluminium would be excluded from trading on the LME. The

LME's view on the inclusion of environmental standards was explored in the position paper<sup>2</sup> and the LME continues to believe that it has not seen the market demand to require such a move, further than ISO 14001, at the current time, but will continue to keep this under review.

To which point, a number of respondents noted the LME's language in respect of the potential for scope expansion over time, a prospect informed by the expectation that the global demand for minimum standards in respect of responsible sourcing is likely to evolve and expand over coming years. While agreeing with this analysis, these respondents were concerned that "scope creep" in respect of the LME proposal could cause significant difficulties for LME brands if implemented while those brands were still working to embed the requirements of the current proposal. The LME understands these concerns, and fully aims to ensure that its requirements will not evolve in such a manner which contradicts or undermines the existing proposals until all of these are established and embedded. However, the LME feels that it would be unfair to commit to a minimum timeframe at this point, given the extent to which this commitment depends on external factors, including customer demand and broader market standards. However, in line with the LME's belief in the importance of market collaboration, any change to the LME's responsible sourcing standards would be made following consultation with the market

## **2.2. Considerations around the LME Red Flag Assessment ("RFA")**

The main focus of feedback received in response to the position paper was in respect of the details of the Red Flag Assessment ("RFA"), the process through which LME-listed brands would self-assess in order to categorise themselves as higher- or lower-focus brands for the purpose of the LME's requirements.

This feedback focused on requests for the LME to provide greater clarity in respect of four main areas of the proposed process, as follows: (i) report criteria, including the LME's definition of conflict-affected and high-risk areas ("CAHRAs"); (ii) ability to leverage existing red flag assessment processes; (iii) review process; and (iv) transparency of the results. These concerns are addressed in turn in Sections 2.2.1 to 2.2.4.

A further concern related to the exclusion of cobalt and tin brands from the red flag process; these concerns are addressed in Section 2.4 below.

### **2.2.1. Report criteria**

While all respondents who addressed this issue were in favour of the LME's decision to use the OECD Guidance as the basis for its requirements, a number of respondents expressed unease about the level of detail available in this document, including confusion over identifying CAHRAs, resulting in a lack of clarity on what the LME would expect. As an example, specific requests for clarity were made in reference to the LME's requirements in respect of step one (company management systems) and step five (reporting transparency) of the OECD's 3T supplement five step framework for risk-based due diligence in supply chains. As a result, there was some concern at the prospect that the LME could see a wide per-brand variance in the form and detail supplied in the red flag assessment. Further, if the LME accepted such a variance, it would unfairly penalise those brands which invested a greater degree of time and effort into their reporting.

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<sup>2</sup> See Section 5.2, "Principles underling the LME proposal"

A secondary concern on this theme related to the applicability of the red flag assessment outlined in the 3T supplement to metals other than tin, tantalum and tungsten (the “3Ts”), the three metals at which the 3T supplement is explicitly aimed.

Finally, some respondents expressed concern about the level of detail potentially required by the LME, with a particular view to the issue of confidentiality of proprietary information, especially with regards to the LME’s subsequent transparency requirements. Those concerned suggested the LME should require reporting on the outcome of an assessment (conducted by, for example, an external auditor) rather than the assessment itself, to avoid the risk of disclosure of confidential information.

The LME is sympathetic to these concerns and agrees that for the purposes of clarity, a form of standardised reporting would be of significant benefit to listed brands, as well as for the LME. To facilitate this, the LME is proposing to introduce a template for the red flag assessment to ensure that the reporting process is as streamlined and efficient as possible for all LME-listed brands, as well as ensuring consistency of reporting across LME metals and producers. This template will include requirements for establishing strong company management systems, in line with step one of the 3T supplement five step framework, the red flag assessment reporting, and further questions to provide greater transparency around existing work undertaken by LME brands. The question of transparency is explored further in Section 2.2.4 below, and the full template has been published as part of the LME’s Responsible Sourcing Consultation as outlined above.

In creating this template, the LME has tried to explicitly address concerns as to the applicability of the 3T supplement to metals other than tin, tantalum and tungsten. While the LME accepts that this is beyond the original aim of that document, it does believe that the advantage of the relatively high-level nature of the 3T supplement means that it is possible to extrapolate a red flag assessment process that is applicable to a broader range of base metals than those envisaged in the original drafting.

Although some respondents suggested that the LME would need to provide a separate template for each metal, the LME believes that this would lead to over-complication. This was an outcome which a number of other respondents were anxious to avoid given the duplication of reporting, and consequent wasted effort, this could create. The LME would welcome feedback on whether it has achieved this aim as part of the Responsible Sourcing Consultation as outlined above.

Core to this template is the requirement for brands to assess and report on the role of CAHRAs in their supply chain, and a number of respondents were interested in how the LME would define such areas, with the strong recommendation that the LME should aim to provide as much clarity as possible.

The LME is aware that the OECD’s position on this topic is that responsibility for a CAHRA classification lies with the company making the assessment, rather than the OECD itself. The LME, similarly, is cognisant of the difficulties of one organisation (here, the LME) making this assessment unilaterally on behalf of others, and is uncomfortable electing itself to be the arbiter of such decisions. Equally, the LME is also mindful of the potential ramifications of individual producers arriving at different conclusions regarding CAHRA assessments, resulting in potentially considerable inequality across the LME’s responsible sourcing requirements.

In seeking to address this issue and find an appropriate balance, the LME has been in conversation with the OECD, as well as a number of standards bodies who have addressed similar questions and have developed, the LME believes, a number of tools to support companies in making individual assessments. For example, the LME has reviewed the risk map developed by the Responsible Minerals Initiative (“RMI”) – for its members – which provides an indicative list of CAHRAs by weighting a range of relevant risk-related resources and barometers. As a result, while the LME is proposing that its listed brands will need to make their own assessments, and the LME understands that this remains a subjective area, the LME believes that tools such as these provide a constructive framework for companies in making CAHRA assessments in their supply chain analysis.

Finally, although no respondent requested that the LME run a trial or pilot process for its red flag assessment template, a number of respondents did mention this process as one of the reasons the LME should allow a greater period of time for compliance with its responsible sourcing requirements. Thus, although the LME does not intend to conduct a pilot of the RFA, believing that this process is covered by the Responsible Sourcing Consultation, it does agree that providing more time for RFA reporting would be helpful. Its proposals in this respect are fully explicated in Section 2.5.

### **2.2.2. Leveraging existing red flag assessment processes**

As mentioned in Section 2.2.1 above, one of the questions raised in respect of the red flag assessment – and indeed on a number of other areas in the LME’s proposal – is the extent to which LME-listed brands are able to leverage existing work to fulfil requirements set by the LME. In respect of the red flag assessment, equivalence relates to two levels.

Firstly, equivalence here can refer to the RFA assessment as a whole. To the extent that other standards have a red flag assessment (understanding that they might utilise a different nomenclature for such a process), the LME understands concerns around the additional effort required for brands to undertake the LME’s process as well. However, the LME believes that having conducted a red flag, or similar, process, the relevant brand should have identified and collated all the information necessary for the LME’s process. Accordingly, completing the LME’s RFA should be straightforward.

Similarly, a number of respondents pointed out that some brands produce more than one metal per mine, when a second metal is a by-product of the primary. For simplicity, respondents requested that the RFA at a mine-site for a primary metal would also be considered eligible as part of the RFA for a by-product metal produced from the same mine. The LME already believes that the RFA template which it has produced will itself be the summary of significantly more detailed analysis which producers will have carried out; accordingly, mine sites producing feedstock for multiple LME brands will be able to leverage the same underlying diligence for two (or more) RFA templates.

Finally, the LME has received specific queries about copper produced from mines which are already complying with the LBMA requirements for gold. While the LME’s requirements do not cover its gold contracts, these are still subject to responsible sourcing requirements imposed by the LBMA and so, per the above, the LME is happy to for such brands to use the information collated as part of the LBMA process to complete the same for the LME.



### 2.2.3. Review process

The LME received a number of questions in respect of its RFA assessment approval process. Full details of this process are provided in the Responsible Sourcing Consultation; however, for ease of reference a summary is outlined below in Figure 1.

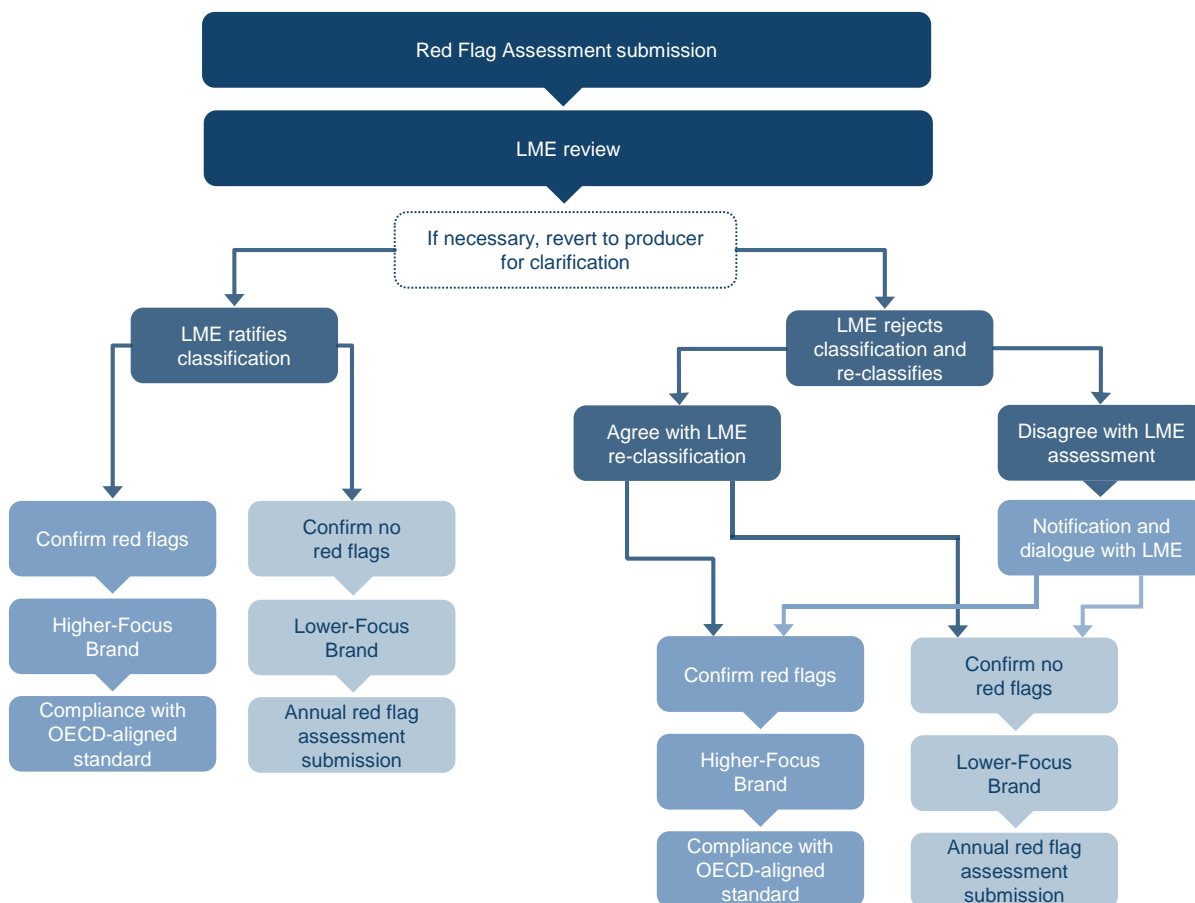


Figure 1: Red flag assessment review process

As shown in Figure 1, following the RFA self-assessment, all such assessments will be reviewed by the LME (using external expertise where necessary or appropriate) regardless of the RFA outcome. This will enable the LME to ensure consistency across both higher- and lower-focus outcomes. Following the LME’s review, the ratified results will be confirmed back to the brands. The review process is also designed to mitigate concerns from a small group of respondents who do not view self-assessment as sufficient to meet the obligations of the OECD Guidance, and will be facilitated by the production of the RFA template, as outlined above in Section 2.2.1.

Some respondents did suggest that the evaluation stage should be conducted by an independent expert; however, as outlined above, the LME’s concern here is to ensure consistency. It believes that the LME proposal would represent too great a body of work for one person to review, and as a result, more than one such expert would need to be commissioned, running the risk of a divergent set of results based on individual subjectivity. The advantage of the LME running this process is that it reduces the reliance on, and therefore also the subjectivity of, one individual. Further, the LME accepts that its role as “regulator” in respect of this process is not something that can be outsourced. As with, for example, assessments in respect of complaints or queries on warehouse network rules, the LME has to be prepared to stand behind the rules it implements and make decisions accordingly.

## 2.2.4. Results transparency

Finally, a number of respondents expressed concern around the LME’s intentions in respect of the publication of RFAs and requested further clarity on what exactly would be reported.

Suggestions varied here, with some market participants calling for full transparency from the start – including those making investment decisions on the basis of such information – and many others expressing deep concern as to the potential impact for brands which, in the interests of transparency and with the best of intentions in respect of risk mitigation, expose themselves to potential misinterpretation of risks or the value in making them public.

In the view of the LME, such risks are intrinsic to many metal sourcing supply chains, and transparency around them represents an invaluable tool in promoting the identification and mitigation thereof. It firmly believes that it is only through identifying such risks that improvements can be made over time. However, the LME has also been explicit that its aim in putting forward these responsible sourcing proposals is not to prevent, or even discourage, the sourcing of metal from higher-risk areas. As a result, the LME remains highly concerned that enforcing immediate and full transparency would unfairly penalise those making efforts to source metal responsibly from higher-risk areas and would serve as a deterrent from the kind of honesty and transparency it is aiming to promote. The LME does not want its requirements to cause its brands, in particular those working to implement these requirements, to suffer adverse effects – either through negative publicity or market perception – for doing the right thing.

As a result, the LME is proposing a phased approach in terms of its public reporting for red flag assessment results, as outlined in Figure 2. Transparency in respect of standard audit results is covered further in Section 2.3.2.

Pathway to transparency		
Date	Red Flag Assessment results	
31 December 2020	Y1	Summary statistics
31 December 2021	Y2	Summary statistics
31 December 2022	Y3	Anonymous versions
31 December 2023	Y4	Anonymous versions
31 December 2024	Y5	Attributed versions
31 December of subsequent years	Y6 and onwards	Attributed versions

Figure 2: Pathway to transparency

For the first two years post-implementation, the LME will publish only summary statistics. For the subsequent two years, the LME will publish the red flag assessments in full, but on an anonymised basis. As well as protecting those brands reporting openly on the risks they have identified in their supply chains, this will also allow brands to refer to the work undertaken in the RFA processes of other LME-listed brands, as well as providing time for the market more broadly to become familiar with the type of reporting it can expect to see and become accustomed to the idea that higher-focus does not, by definition, mean problematic.

In year five post-implementation, the LME will require all brands to publish the RFAs in full. These requirements are outlined in full in the Responsible Sourcing Consultation.

As a final point, the question was also raised as to whether the binary classification of higher- or lower-focus would be public from year one or would remain confidential, at least in the initial stages. The LME understands the concern about the market perception of brands being classified as higher-focus and, further, thinks that publishing this information in year one would be at odds with its pathway to transparency as outlined in Figure 2. As such, the percentage of higher- and lower-focus classifications will be published with the summary statistics, but the brands themselves will not be named until year five. That said, the LME would like to reiterate here its position that a classification as higher-focus is not in itself a problem. Indeed, brands which have been rigorous enough to identify such risks should be supported as they work to address those risks. The LME would underscore that its requirements are aimed at ensuring that no responsible mining practices are off limits, but is focused on the broad range of risks inherent within sourcing metals and managing those risks appropriately rather than taking an avoidant approach. The LME's timeline for communication with the market on all such issues is included with the Responsible Sourcing Consultation.

## **2.3. Considerations around responsible sourcing standards**

Feedback on this topic centred on a five key areas; namely: (i) general considerations around standard creation; (ii) the LME's alignment assessment process; (iii) considerations around compliance to a baseline standard; (iv) the use of auditors; and (v) the ISO 14001 / OHSAS 18001 certification process.

### **2.3.1. General considerations around standard creation**

In the position paper, the LME recognised that a number of highly effective industry initiatives are already in existence, and proposed that its responsible sourcing requirements should embed and support, rather than duplicate, the work already underway. Consequently, the LME's proposal was to make use of existing industry standards, provided that these appropriately embed OECD Guidance. Feedback on this proposal was overwhelmingly positive as respondents recognised the savings in time and cost that this could provide, including removing the need to duplicate work already completed. Questions did remain, however, as to how the LME would assess equivalence of standards, and the degree of transparency which would be applied to the results of these assessments – this process is addressed in Section 2.3.2. Other proponents of this approach pointed out that were the LME to create its own standard, the development of such would require a significant investment of time, money and effort which should not be underestimated. Additionally, respondents indicated that in respect of certain metals, the industry was already suffering from standard saturation and a new independent set of guidelines would likely add to the sense of overwhelming due diligence requirements.

Nevertheless, a minority of respondents disagreed with this position, suggesting a single independent LME-generated standard covering all metals and aligned fully with the OECD Guidance would be preferable. In particular, a number of producers of multiple metals were concerned about the requirement to comply with a variety of standards in order to certify and audit all the different LME brands they produce. A single LME standard, it was argued, could simplify processes and save on both time and cost, and further, the production of such a standard would be necessary regardless, given that a number of LME metals do not have existing responsible sourcing standards available.

The LME's inclination, as outlined in the position paper, is towards relying on existing standards produced by experts in this field, and it remains of the view that creating its own standard would create more problems that it would solve. Consequently, the LME does not proposed to change its position that brands which raise red flags as part of the RFA process should elect an industry standard (or an internal standard) which is aligned with OECD Guidance in order to comply with the LME's requirements. That external standard would then define the audit requirements for smelters or refiners producing more than one LME brand.

That said, the LME does have a significant degree of sympathy for those producers required to certify and audit across a range of metals, and the LME will work with these brands to make every effort to streamline their processes to minimise disruption. For metals where there is no existing standard, the LME will engage with industry, trade and standards bodies to encourage the development of such, in full collaboration with the market, to ensure core needs are met. The LME expects that, should the demand exist, a standards creator will provide the materials necessary to create a pan-metal standard. Equally, given the LME has been clear that it would be willing to accept internal standards (once appropriately alignment assessed), it would also be feasible for a metal producer to create such a standard themselves.

### **2.3.2. The LME's alignment assessment process**

As indicated in Section 2.3.1, the LME will endeavour to run a streamlined and efficient process of alignment assessment for existing standards, such that producers already working with these standards do not have that work interrupted or duplicated. As a starting point, the LME is happy to confirm that standards which have already completed the OECD alignment process will not be required to re-complete this process for the LME; instead, the LME will ask to review the existing alignment assessments and would expect that these would be consistent with the LME's requirements, thus allowing those standards to be considered alignment-assessed.

For those standards which have not yet been through the alignment assessment process, in the position paper, the LME outlined a three-step process for ensuring that a brand is aligned with the OECD Guidance as follows: (i) identify a standard, (ii) ensure the standard has undergone OECD alignment assessment by an accredited assessor, and been ratified as such by the LME, and (iii) demonstrate compliance with standard and validate this compliance with the LME.

A number of respondents asked the LME to provide further guidance on the criteria against which it would assess both internal and external standards. For this, the LME would refer respondents to both the OECD Guidance, and to its associated Methodology for the Alignment Assessment of Industry Programmes with the OECD Minerals Guidance. This document provides the methodology against which industry standards are assessed for alignment with the OECD Guidance, which – as the baseline for the scope of the LME's requirements – is the benchmark for the LME's criteria for both internal and external standards.

Subject to the agreement of the relevant standard owner, the LME intends to make clear on its website which standards have been assessed as being equivalent, although it should also be noted that this list would not be exhaustive and would be subject to change.

As a final point in respect of the alignment assessment itself, one respondent was interested in the LME's position as to a possible pragmatic approach, whereby external standards which were assessed as being consistent with the intent of the OECD Guidance (as opposed to being an exact alignment) would be considered sufficient. While the LME fully supports the value of

positive intention and fully agrees that this can be as powerful a force for positive change as exact alignment, the risk inherent in this approach would be that the LME inadvertently creates a two tier system, where some brands are fully compliant with the letter of the OECD Guidance, whilst others are working to the spirit. This has potential implications for price discovery, which are covered more broadly in Section 2.3.3 below. However, the LME does recognise that, in practice (and as demonstrated by the pilot alignment assessment processes already undertaken), it is unlikely that any standard will receive an unqualified and uncommented alignment assessment, and will ensure that its approach for recognising alignment assessment retains the pragmatism required in this regard.

Finally, some respondents suggested the use of advisory multi-stakeholder groups (“AMSG”) in assisting the LME with alignment decisions and recommended recognised experts remain involved in the evaluation process. The LME appreciates this feedback, and while in the first instance the LME intends to rely on the reports generated by the relevant auditors as outlined in Section 2.3.4, it remains aware of the potential value of external advice and fully intends to utilise this tool as necessary.

### **2.3.3. Baseline standards vs gradual improvements**

The next stage of the LME’s process dealt with the audit of brands against their chosen OECD-aligned standard, and respondents explored a number of areas of interest in relation to this process.

As outlined in the position paper, it is the LME’s intention to work with all of its producers in order to move towards a truly responsibly sourced metals and mining industry, and it is aware that this process will not be straightforward or quick, and that different brands will be at varied stages of their responsible sourcing journey. On this basis, the LME is sympathetic to the debate which emerged from responses to the position paper between achieving a minimum baseline standard across all metals, and a focus on gradual improvements over time, driven by full transparency of a brand’s supply chain mapping, risk identification and risk mitigation on an (at least) annual basis, to allow the market to track improvements over time.

Proponents of the pragmatic approach suggested that if noteworthy progress is shown, then the LME should not require formal compliance with a standard. The momentum for ongoing improvement would instead be driven by public reporting – either annually or more frequently – and the pressure to show improvement in each report would create the impetus for ongoing change.

Alternatively, it was strongly argued by a number of other respondents that the LME should not operate a policy of accepting gradual improvement over time, and instead needed to retain a focus on a minimum baseline standard with which all brands would have to comply, and which would ensure consistency across the LME brands list, thus removing uncertainty as to the standard of metal available for delivery on the Exchange.

The LME understands the significant market debate over this issue, and does understand the arguments in favour of gradual improvement over time. However, the LME remains of the view – also supported by some respondents to the position paper – that its most effective route forward lies in leveraging the complementary value of transparency (which in turn drives gradual improvement) and standards. The LME’s view on this topic is explicated fully in the Responsible

Sourcing Consultation but it worth reiterating (as outlined in the position paper<sup>3</sup>) that the LME is a seller's market, and it is the seller's choice which metal they deliver into the Exchange in settlement of an open position. This has an important consequence for the LME, in that it means that the seller is economically incentivised to deliver the least desirable metal onto the Exchange and, because the LME price is discovered on the basis of such deliveries, that price will tend to converge to the value of this brand. If brands which have made less progress in respect of their responsible sourcing work are considered to be less valuable than those which are well advanced – which would be in line with the LME's expectations – this is likely to be the metal used in delivery on the Exchange, and it therefore has the potential to mean the LME price trades at a meaningful discount to metal in the “real-world”. Given that the accuracy of price discovery is core to the LME's franchise, it is imperative that it only lists metal for good delivery which meets baseline standards in order to ensure comparability across metal stored in LME-listed warehouses. Accordingly, although the LME recognises that compliance to a standard in some cases will not be an overnight process, allowing brands that have not conformed to a baseline standard to remain listed on the LME will intrinsically weaken the LME price, as those who take delivery of such metal may be uncertain of those brands' responsible sourcing provenance. On this basis, the LME remains committed to its brands reaching a baseline standard to maintain the robustness of the LME price.

#### **2.3.4. Audits and auditors**

The position paper outlined the proposed use of audits by third party assessors in the LME's intended responsible sourcing requirements in respect of two individual processes, (i) alignment assessment audits of standards against the OECD Guidance, and (ii) assessing brand compliance with internal standards. For external standards, the LME's understanding is that, once alignment assessed, the standard body itself will define and operate the process for assessing compliance, including the frequency of audits and assessing suitable auditors and, as a result, this is out of scope for the LME.

Feedback in respect of these two audit processes largely focused on two areas: (i) clarity around the mechanisms of the audit process, and (ii) broader concerns about the dependence on audit in the assessment process.

Multiple respondents requested further clarity on the auditing process with some recommending that auditors already recognised by schemes deemed consistent with OECD Guidance (for example, the International Tin Association (“ITA”) and RMI) be automatically considered suitable for the LME's purposes. For standards which are yet to undertake the alignment process, clarification was requested in respect of how the LME would identify suitable auditors, and make these known to the market.

As outlined above, the LME maintains the view that external standards are responsible for approving and monitoring their own auditors. Given the experience of those auditors with regards to the respective processes with which they work, the LME would fully expect – on undertaking its own assessment – to find that these auditors were fully capable of undertaking audits of internal standards also. While the LME expects its listed brands electing to use internal standards to retain responsibility for the appropriateness of their responsible sourcing auditors, the LME does understand that the publication of a list of auditors whom the LME believes are fully qualified would be of use and is happy to undertake that process. A list of approved

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<sup>3</sup> See Section 5.5, “Transitional provisions for cobalt”

auditors for internal standards (who will need to apply to the LME for recognition) will therefore be published on the LME website.

More generally, some respondents focused on a broader point in respect of audits, highlighting that the OECD Guidance demands companies look beyond such audits when assessing their suppliers, and recommending caution on the over-reliance on audits. One respondent pointed out that, although a useful tool, audits should only represent one part of the overall framework of assessment, and that the importance of transparency in driving continued progress should not be overlooked. While the LME accepts that audits cannot be expected to be the whole story, as noted in Section 2.3.3, for the purposes on establishing a consistent baseline across its metals, the LME has to impose minimum set of requirements on its listed brands. This does not mean that brands cannot achieve over this minimum standard, and the LME is equally prioritising transparency (in particular, through the publication of brands' RFAs) as part of its complementary approach between transparency and standards.

### **2.3.5. Transparency**

The final section of feedback in respect of the LME's alignment assessment process addressed the degree of transparency which the LME would provide.

As outlined in Section 2.3.2, the LME is happy to be fully transparent in terms of which standards have been assessed as aligned with the OECD Guidance, and subject to the consent of the standard owner (be that internal or external) will publish a list of such names on its website.

In terms of transparency of the results of audits which assess a brand's compliance with a standard, considerations were similar (in respect of the value and risks of transparency) as those set out in Section 2.2.4 on Red Flag Assessments. In respect of transparency of the audit results, the LME believes that this should be undertaken in line with the requirements set out in Step 5 of the OECD Guidance 3T supplement five-step framework. Audits in respect of standards will be therefore be published in accordance with the requirements as set out under that standard.

### **2.3.6. ISO 14001 / OHSAS 18001 certification process**

The position paper considered the introduction of a requirement for producers to hold up-to-date ISO 14001 (environmental management) and OHSAS 18001 (occupational health and safety management systems) certification. The majority of respondents were supportive of these certifications, confirming that these are pertinent certifications but recommended that the recognition of equivalent standards in this area would also be of great use. In contrast, a minority of respondents commented that questions remained over their value and relevance. Finally, some respondents requested more clarity on how compliance with these certifications would operate.

As specified above, one respondent argued that they did not recognise the value of OHSAS 18001, likewise ISO 14001, arguing that these certifications failed to acknowledge other equally appropriate industry standards. This was a minority view from respondents with many more promoting the importance of these certifications, although agreeing that there continue to be many other equally important industry accreditations in environmental and occupational health and safety management that would be valuable.

Feedback on equivalence covered a number of issues with several respondents highlighting standards which they believed to offer equivalence, including those operating under regional governing bodies such as US Occupational Safety and Health Administration (“OSHA”), as well as industry initiatives; ASI Performance Standard for Aluminium, International Council on Mining and Metals (“ICMM”) and Towards Sustainable Mining (“TSM”) were all identified as suitable alternatives.

On a similar theme, one respondent made the argument that their internal management systems went further than the ISO 14001 or OHSAS 18001 certifications and therefore provided sufficient protection already in these areas. This respondent suggested that the LME takes this into account when it comes to compliance and equivalence. In the same vein, another respondent advocated that if a site has an internal Health, Safety, Environment and Quality (“HSEQ”) Management System that has been appropriately third party audited, then this internal HSEQ Management System should be considered equivalent.

A number of respondents requested that the LME outline what exactly would constitute compliance to these certifications, and posited a question around whether multi-site or site-by-site certification for ISO 14001 would be needed. Correspondingly, one respondent requested the LME define precisely which ISO documents would need to be submitted to establish compliance.

The LME maintains the view that ISO 14001 and OHSAS 18001 certifications are valuable qualifications in environmental and occupational health and safety management and, as such, intends to progress with the introduction of these requirements. Questions regarding the exact demands of these certifications are a matter for the relevant standards bodies.

That said, the LME also agrees that in many cases, equivalent standards exist, providing strong accreditation and governance which ensure similar management systems are in place and operational. In line with the LME’s principle of pragmatism, therefore, the LME proposes that interested parties commission an external audit to assess equivalence, and provide the results of such an assessment to the LME to review. Should the LME agree with a positive assessment, it will consider compliance with that standard to be equivalence to ISO 14001, the OHSAS 18001, or both. Should the bodies which provide those standards provide consent, the LME would also propose to publish a list of those bodies on its website, such that other market users are informed on alternative options for compliance. Full details of this are published in the LME’s Responsible Sourcing Consultation.

## **2.4. Considerations about the separate provisions for cobalt and tin**

Feedback on the classification of cobalt and tin as automatic higher-focus concentrated on the concerns around the universal classification of all brands of one metal, be that tin or cobalt. In taking such a step, it was viewed that the LME would be removing the risk-based approach it was proposing for other metals, in favour of treating all the brands of one metal as a homogenous group; a fact that was considered unlikely to be reflective of the reality. Further, although it was recognised that this proposal would mean that cobalt and tin could deliver compliance with an OECD-aligned standard on a more expedited timeframe, it would also mean that a core step for both due diligence and transparency – the red flag assessment – would be missed, and with it, a further opportunity for companies to share supply chain information, take collective responsibility, and address associated risks.



Additional concerns were raised in respect of the LME's proposed transitional provisions for cobalt which, it was felt, were unfair, anti-competitive, represented serious market risks, and did not properly allow for the complexity of identifying the risks associated with the cobalt supply chain, despite much work already undertaken to this end. A small number of participants disagreed with the LME's assessment of lower price being an indicator of risk, and felt that it was a presumption of guilt that did not properly take into account other market factors which can affect price. Conversely, others did agree that this represents a red flag, but felt instead that this should not be evaluated in isolation but as part of a detailed assessment of risk across the whole supply chain. Further to this, the concern was expressed that a focus on price could cause metal producers to overlook other red flags in non-discounted supply chains, or create a bias against artisanal and small-scale mining ("ASM").

Finally, one respondent felt that the transitional provisions were being implemented with insufficient time for planning, meaning that the scope for malicious reporting against brands was high. They felt that this could result in companies leaving cobalt mining altogether, which would negate the potential for them to make positive change.

As a general point, the LME would note that it does not think that the causal link between the sourcing of a brand and its price is solely related to the type of mining used, be that ASM or large scale mining ("LSM"); rather, that a price discount based on responsible sourcing could be related to any number of risks associated with a supply chain. ASM, in and of itself, does not represent a cause for a price to be discounted if that brand has appropriately identified and mitigated the associated risks.

However, this point aside, the LME does accept the arguments made by respondents to the position paper in respect of both the automatic classification of all its cobalt and tin brands, and the transitional provisions for cobalt, and is not proposing to include either in its revised proposal. Instead, producers of LME-listed cobalt and tin brands will be required to undertake the red flag assessment, as per other metals, and will be classified as either higher- or lower-focused brands on the basis of those results.

This does, however, have a forward impact on the timeline for cobalt and tin compliance. As observed in the position paper, the process for defining standards is considerably more advanced for some metals (including cobalt and tin) than others, and time is required for those in the latter category to define, implement and alignment assess appropriate responsible sourcing standards. Accordingly, the LME has accepted that its original timeline was too ambitious and amended it, as outlined in Section 2.5; it should be noted, therefore, that the conformance of the requirements for cobalt and tin with other metals means that their compliance with OECD Guidance will now be delivered on the same amended timetable.

## **2.5. Timeline**

Although some respondents commented that they were happy with the timeline proposed, and understood the need for the LME to take action on a timely basis in line with market demand, the far greater majority of respondents felt that the LME's proposed timeline was too ambitious, and did not leave sufficient time for, amongst other things, educating the market, alignment assessment processes, and developing standards where metals are not currently covered by existing offerings. The removal of the accelerated provisions for cobalt and tin, as outlined in Section 2.4, will mean that these two metals will also work to the amended deadlines.

As such, the LME accepts that acting precipitously could cause more problems than a swifter implementation would solve, and to this end, has outlined a new timeline in the Responsible Sourcing Consultation launched today in Notice 19/130. The LME believes that this new timeline is fair and achievable, but would welcome comments as part of the consultation.

Further, the LME also acknowledges that the original proposal did not cover the process timeline for brands listing on the LME during and following the implementation of the LME's responsible sourcing requirements. Full details have now been provided in the Responsible Sourcing Consultation and interested parties are encouraged to refer to the documents associated with that consultation for further information. These documents also cover the process for brands which originally classify as lower-focus, but subsequently – during the annual review of their RFA – are reclassified as higher-focus.

One respondent also asked about the timeline for delisting metals, should they fail to comply with any of the LME's stages of compliance, including failure to submit an RFA, or failing to gain compliance with a standard aligned with the OECD Guidance. This is addressed in full in the Responsible Sourcing Consultation and is broadly consistent with the LME's original proposal in the position paper<sup>4</sup>; however, while accepting the market's preference for certainty on this subject, the LME does believe that in order to act in a proportionate manner and to mitigate the risks of creating a disorderly market, it does need to reserve the right to make decisions on a case by case basis. On this topic, the LME is also cognisant of the views of some respondents who were concerned with the attendant uncertainty in respect of legacy stocks. Broadly speaking, the LME agrees with the prevailing opinion that unless absolutely necessary, on-warrant legacy stocks should be able to remain in warehouse until cancelled. However, and as with the delisting process, it does need to retain the ability to come to a different conclusion should the circumstances demand such an outcome.

## **2.6. Other considerations**

In addition to the five areas addressed above, a number of other topics were raised across the feedback to the position paper.

### **2.6.1. Impact of brand delistings**

Of these additional topics, probably the most prevalent were those respondents with concerns about the potential ramifications for brands if subsequently delisted, in particular the impact on their brand value.

The LME has covered, in Section 2.2.4, its views on the potential impact on brands if they are classified as higher-focus, but agrees that it is fair to consider as well the impact on brands if they are delisted from the LME.

It is worth noting here that it is wholly possible that some LME-listed brands choose to delist as a result of the introduction of responsible sourcing requirements; indeed, the LME is cognisant that in implementing the proposed responsible sourcing requirements, it is imposing a significant burden of responsibility on its brands, one which comes with concomitant requirements of time and resource. Accordingly, the LME has to accept that, despite its best efforts to ensure that these requirements are practical and user-focused, that there may be some brands for which their LME listing is no longer a sufficient priority to justify the required effort. This is likely to be

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<sup>4</sup> See Section 5.3, "LME powers"

especially true of brands which do not see the demand for responsible sourced metal from their customers. While the LME hopes that these brands would have been in touch with the LME bilaterally (or as part of the engagement process for the responsible sourcing proposals) to explain that they would be likely to delist, it has to accept that not all brands may be convinced by the merits of this journey. Given that these brands are likely to be those which do not see a high demand for responsible sourced metal, the LME believes it is fair to assume that they will not experience an undue negative impact from their choosing to delist as LME brands. This notwithstanding, to date the LME has not heard this message from any of its listed brands.

That said, the LME also believes that the international drive for greater detail and transparency on the responsible sourcing of metal (LME-listed or otherwise) is only going to gain momentum over time and, as such, would encourage its brands to consider the longer term implications of this momentum.

Perhaps a greater source of concern for the Exchange is those brands which try, but do not succeed, in meeting its responsible sourcing requirements. For the avoidance of doubt, it is the LME's aim that brands are fully compliant with the requirements within the relevant timelines. Indeed, to this end the LME has extended its deadlines as outlined in Section 2.5 above.

However, the LME also has to be clear that in order to ensure that it continues to meet its responsibilities in respect of price discovery, while maintaining an orderly market, it is imperative to achieve a baseline consistency in respect of the underlying value of the brands which are deliverable against open positions on the Exchange. To this end, the LME's ability to delist a brand should it not meet the relevant requirements has to remain a tool at the LME's disposal. The LME is fully aware to the impact that this could have on a brand – both reputationally and from a pricing perspective – but it must have the power to protect its market.

The LME, along with a number of respondents to the position paper, is also aware of the potential impact of this outcome on the LME itself, including the possible risks to the LME's orderly market, should the LME be forced to delist a brand considered "too big to fail". These are brands which constitute a significant proportion of the deliveries made in settlement against open positions on an LME contract, with the understanding that their absence would have a significant negative impact on the liquidity of that contract (or, in the worst case, mean that contract ceased trading altogether).

Firstly, the LME would highlight that the number of contracts where this could be considered a real risk would be relatively small. Secondly, in the LME's experience, market forces would act to correct the problem. As outlined in the position paper<sup>5</sup>, the "cheapest" or least desirable warrant is usually delivered against an open position and for some contracts, this warrant is often the same brand. If that brand was no longer available, by definition, a new brand would become the cheapest, and would – presumably – become the *de facto* currency for that contract.

However, the LME does not wish to pretend that this means the worst case outcome cannot happen, or that it could not have a significant impact on the liquidity of a contract, including the possibility that the contract ceases trading altogether. The LME would be ill-advised to take these risks lightly and, indeed, has spent considerable time considering such an outcome.

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<sup>5</sup> See Section 5.5, "Transitional provisions for cobalt"

However, in the final analysis, the LME has to accept that its motivations for taking action on responsible sourcing – while multi-faceted – ultimately focus on three imperatives. Firstly, there is a commercial imperative to both meet consumer demands for responsibly sourced metal, and to protect the LME franchise from the negative impact on price discovery if one or more brands are not considered to take responsible sourcing concerns sufficiently seriously, and as a result, trade at a discount to the market or “real-world” price. Secondly, there is an ethical imperative to take appropriate action in the face of very real concerns about potential negative consequences of improperly-governed extractive activity. Finally, there is an imperative for the LME to provide leadership to the global metals industry and to answer calls to provide a centralised and practical route forward to address these issues. All of these factors compel the LME to progress with its responsible sourcing proposals, and none of them are well-served in the longer-term by a decision to continue to allow the listing of a non-compliant brand in order to maintain trading on the relevant contract in the short-term. The LME will do everything within its power to mitigate these risks, but ultimately must accept that it cannot progress without acceding to the reality that it can never fully protect itself against the potential negative impacts flowing from a brand de-listing.

### **2.6.2. Grievance procedure**

As raised by a number of respondents, important to the LME’s ability to deal with the risks outlined above is an effective and robust grievance procedure. A primary concern in respect of these procedures, as raised by respondents, is the threat of malicious actors making spurious or nefarious complaints against other market participants and the LME’s ability to deal with these in a fair and unbiased way. A number of respondents also asked the LME to provide clarity on how the LME’s grievance procedure would interact with similar such procedures, for example, the OECD’s risk portal and RMI’s grievance mechanisms.

As outlined in the position paper<sup>6</sup>, the LME is accustomed to playing a compliance assessment role in respect of its rules and regulations and has a number of process set up to facilitate this. As such, the LME fully intends to investigate credible grievances which relate to the Red Flag Assessment process results. In undertaking this role, the LME is fully aware of the possible consequences, including the potential for the LME to have to run multiple investigations in parallel (as noted by one respondent), with potentially serious implications in terms of costs and resourcing. However, the LME does not believe that these risks mean that it can evade its duties in this respect. The LME is fully conscious that it will need to ensure that it has appropriate access to experts in relevant fields – depending on the focus of any complaint – and is committed to safeguarding that access.

In respect of complaints relating to audits for compliance against an OECD-aligned standard, the LME would expect to refer these back to the original auditor and / or standards body for investigation.

The LME is wholly supportive of the RMI and OECD processes, as well as broader work to develop pan-industry online platforms, and will contribute to these as appropriate. However, while the LME welcomes the idea of incorporating a broader set of stakeholders into its grievance process, it is imperative that the LME retains the independence necessary to provide the ability to investigate in line with its rules.

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<sup>6</sup> See Section 5.6, “LME decision-making and grievance procedure”

### **2.6.3. Committees**

The potential role of a responsible sourcing committee or AMSG was raised by a number of respondents, with suggestions as to a wide range of possible functions including the assessment of audit reports, advice on alignment assessments or standard development, and the ability to critically assess due diligence efforts. Respondents also focused on the composition of such a committee or committees, suggesting that it should include experts from across the metals-specific and responsible sourcing worlds (including human rights), from all points of the metals value chain, from a range of production and consumption geographies, and from independent observers.

Equally, a number of respondents, while acknowledging the potential value of such committees, cautioned that their remit and role should be properly defined, governed by transparent and democratic terms of reference. A third group recommended that such committees should be limited where possible, to avoid the imposition of new assessment and oversight structures, minimise complications and pointing out the potential costs in training and running such groups.

As outlined in Sections 2.2.3 and 2.3.2, the LME is cognisant of the value that such committees or AMSGs could provide, and will constitute such a construct should the need arise. The LME will maintain a watching brief on this topic in the interim.

### **2.6.4. Right to remedy**

One respondent was concerned that the LME's proposal does not include provisions for an individual's "right to remedy", and suggested that this right is codified under international law.

The LME notes that right to remedy can take a number of forms, including apology, review and improvements, and compensation and restitution, but would stress that its focus in respect of its responsible sourcing proposals is to ensure that they are consistent with its powers as a base metals exchange; that is, to require its brands to be compliant with international standards for responsible sourcing, and taking appropriate action against those which do not, as well as providing an effective grievance mechanism. As such, the LME believes that is operating appropriately with the confines of its relationships with the producers of LME-listed brands.

On a similar theme, one respondent was concerned that the LME's proposal had not referenced either the OECD's Guidelines for Multi-National Enterprises ("MNE Guidelines") or the United Nations Guiding Principles ("UNGPs"). The LME would note that it does not believe that it would be feasible – or representative of its role – for it to police every piece of guidance or set of requirements that have been published; indeed, the LME has spent considerable time defining its scope in line with the OECD Guidance. However, it does believe that the MNE raises interesting points about corruption which the LME believes is consistent with the OECD Guidance requirement for disclosure under the Extractive Industries Transparency Initiative ("EITI"). Given the relevance of these to the LME's priorities, the LME has built this requirement into – not only its requirements of OECD-aligned standards – but also its proposed RFA process as outlined in detail in the Responsible Sourcing Consultation.

### **2.6.5. Working with other exchanges**

One respondent asked if the LME would be willing to work with other exchanges on responsible sourcing initiatives, to ensure consistency of requirements internationally and to try to further limit the number of different sets of rules and regulations with which metal producers would need to comply. The LME would be more than happy to hold these conversations, and is prepared to

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work with any interested global exchanges to help ensure that there is consistency of requirements. That said, the LME is also conscious that the global nature of its brands list means that it is in an unique position regarding responsible sourcing and, as such, it is perhaps to be expected that the LME has progressed this initiative; other exchanges will be at diverse stages of their thinking on this topic, and the LME would not propose to delay its own timetable further to this end.

### **3. CONCLUSION**

As the feedback outlined above demonstrates, the LME's market participants have dedicated a considerable amount of their time and expertise to providing the LME with in depth and carefully thought through analysis of its proposals. The LME hopes that the above consideration of this feedback does justice to the effort involved and demonstrates the seriousness with which the LME takes all the comments received. As outlined in Section 1, the LME is now taking its responsible sourcing proposals – as amended by the above analysis and the LME's own review – through to consultation, and interested parties are encourage to refer to Notice 19/130 for further information.