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SEC Adopts Final Conflict Mineral Reporting Rules Mandated by Dodd-Frank Act

Conflict Minerals – How the Final Rules Are Different From the Proposed Rules

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On August 22, 2012, the US Securities and Exchange Commission (SEC) adopted final rules regarding disclosure of the use of conflict minerals that originate from the Democratic Republic of the Congo or adjoining countries (now referred to as "covered countries"). Reporting companies must file their first reports with the SEC on newly promulgated Form SD by May 31, 2014, which will cover calendar year 2013. Annual filings will be required thereafter by May 31.

- The final rule applies to any issuer (referred to here as "issuer") that files reports with the Commission under Section 13(a) or Section 15(d) of the Exchange Act and that manufactures or contracts to manufacture products that contain conflict minerals that are necessary to the production or functionality of the product. The SEC provided limited interpretive guidance, but did not define "manufacture," "necessary to the functionality," or "necessary to production."
- Conflict minerals include cassiterite, columbite-tantalite, gold, wolframite, or their derivatives, or any other minerals or their derivatives determined by the Secretary of State to be financing conflict in the covered countries. Unlike the proposed rules, the only derivatives currently covered by the final rules are tantalum, tin, tungsten and gold.
- The rules do not apply to any conflict minerals that are outside of the supply chain before January 31, 2013. So, any conflict minerals that are located outside of the covered country by that date or smelted or refined by that date do not need to be included in any inquiry or due diligence review.
- Issuers must conduct a reasonable inquiry regarding the origins of the conflict minerals it uses (referred to as a "reasonable country of origin inquiry"). Precise steps required for the reasonable country of origin inquiry are not prescribed in the rule. But, the inquiry must be carried out in good faith and must be "reasonably designed" by the issuer to determine if the minerals originated in the covered countries or are from scrap or recycled sources.
- If an issuer determines that its conflict minerals did not originate in the covered countries or the issuer has no reason to believe that the minerals may have originated in the covered countries, then the issuer is required to disclose that determination and provide a description of the reasonable country of origin inquiry and results of the inquiry on Form SD, which must also be posted on the issuer's website.
- If an issuer determines that its conflict minerals are from scrap or recycled sources or the issuer has no reason to believe that the minerals are not from scrap or recycled sources, then the issuer is required to disclose that determination and provide a description of the inquiry and results of the inquiry on Form SD.
- If an issuer knows or has reason to believe that its minerals may have originated in the covered countries or that its minerals may not be recycled or scrap, the issuer is then required to conduct supply chain due diligence to determine if the conflict minerals benefited armed groups in the covered countries.

- If, as a result of the required supply chain due diligence, the issuer determines that (a) the conflict minerals are not, or there is no longer any reason to believe that they are, from the covered countries or (b) the conflict minerals are from recycled or scrap sources, then the issuer is not required to file a Conflict Report. In that case, the issuer must file the Form SD which must describe the reasonable country of origin inquiry and the results of that inquiry.
- If, as a result of the required supply chain due diligence , the issuer determines that the conflict minerals are from the covered countries but did not benefit armed groups, then the minerals are "DRC conflict free." In that case, the issuer must file the Conflict Minerals Report, as an exhibit to the Form SD, stating that conclusion along with a private sector audit certifying that the Conflict Minerals Report was audited and providing the name of the auditor.
- If, as a result of the required supply chain due diligence, the issuer determines that the conflict minerals are not DRC conflict free, or cannot reasonably conclude that they are DRC conflict free, then the issuer must file a Conflict Minerals Report which must include a private sector audit of the Conflict Minerals Report along with descriptions of the following:
  - facilities used to process the conflict minerals
  - the country of origin of the conflict minerals
  - the issuer's efforts to determine the mine(s) from which the conflict minerals originated
  - the issuer's products that are not conflict free
- If, as a result of the required supply chain due diligence, the issuer (a) cannot conclude the conflict minerals are conflict free, or does not have reason to believe that they are conflict free or (b) cannot conclude that the conflict minerals are from recycled or scrap sources, or does not have reason to believe that they are from recycled or scrap sources, then the issuer may conclude that they are "DRC conflict undeterminable" and shall file a Conflict Minerals Report which must include a description of the following:
  - facilities used to process the conflict minerals
  - country of origin of the conflict minerals
  - issuer's efforts to determine the mine(s) from which the conflict minerals originated
  - steps that issuer has taken or will take to mitigate the risk of benefit to armed groups

  In this case, no private sector audit is required. Issuers may state the "DRC conflict undeterminable" determination for up to 2 years (up to 4 years for small issuers).
- Under the new rule, an issuer's supply chain due diligence must be consistent with an existing nationally or internationally recognized due diligence framework, if any exists. Presently, the only nationally or internationally recognized due diligence framework available is the due diligence guidance approved by the Organisation for Economic Co-operation and Development.
- When a Conflict Minerals Report is required, it must be audited by a third-party auditor to determine whether existing nationally recognized or internationally recognized due diligence framework (if any) was used and whether the issuer actually undertook the due diligence described in the report. No Conflict Minerals Report is required if the issuer concludes that its conflict minerals are "DRC conflict undeterminable." It is worth noting that the independent auditor is not required to determine whether due diligence was effective or whether the supply chain is conflict free.

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- The final rules contain no exemptions for small to medium-sized issuers, no phase-in periods (other than the transition period for "DRC conflict undeterminable" described above) and no de minimis exceptions. There is also no exemption for existing long-term supply contracts.
- In the Release, the SEC provided a Flowchart Summary of the Final Rules and a Form SD.