

## Conflict Minerals Disclosure Guidelines

September 28, 2012

### Client Advisory

September 28, 2012 by Steven J. Glusband, Guy P. Lander, Bruce A. Rich and Gideon Even-Or

On August 22, 2012, the Securities and Exchange Commission ("SEC") adopted final rules to implement the reporting requirements relating to "conflict minerals" under Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. On the same date the SEC also adopted rules requiring resource extraction issuers to disclose information relating to their commercial development of oil, natural gas or minerals. For more information about these rules, see our client advisory dated September 28, relating to Resource Extraction Issuers.

The new reporting requirements relating to "conflict minerals" apply to all issuers that file annual reports with the SEC under the Exchange Act, including small businesses and foreign private issuers. Under the new disclosure requirements, issuers must file an annual conflict minerals report on new Form SD. The Form SD will be filed by all such issuers, regardless of their fiscal year-end, for the first time on May 31, 2014 (for the 2013 calendar year) and annually on May 31 for each calendar year thereafter.

Even though there is still time until the first required filing of the Form SD, issuers must start preparing for this disclosure promptly. Each issuer must determine whether disclosure is required, and if so, the extent of that disclosure. This process includes the following three stages:

#### 1. Are conflict minerals necessary to the production or functionality of a product?

Companies must determine if they "manufacture or contract to manufacture" products, of which conflict minerals<sup>[1]</sup> are "necessary to their production or functionality." Companies concluding that no conflict minerals are necessary to the functionality or production of any of their products are not subject to the new conflict mineral disclosure requirements. Nevertheless, it is advisable that such a decision will be made affirmatively by the authorized organs of the company and be documented appropriately.

The final rules impose reporting requirements on companies that either "manufacture" or "contract to manufacture" products. The rules do not give extensive guidance on what is a product and do not explicitly define what it means to "manufacture" a product. Companies that have some actual influence over the manufacturing process may fall within the scope of the rule. The SEC has indicated, however, that a company will not be deemed to "contract to manufacture a product" if it merely:

- affixes its brand, marks, logo, or label to a generic product manufactured by a third party;
- services, maintains, or repairs a product manufactured by a third party; or
- specifies or negotiates contractual terms with a manufacturer that do not directly relate to the manufacturing of the product.

In addition, the final rule does not define the meaning of "necessary to the functionality or production." The meanings of these terms will be subject, then, to the facts and circumstances of each company. The SEC noted, however, that to meet this standard, the conflict mineral needs

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to be necessary for a product's generally accepted use, function or purpose and actually contained in the product. Accordingly, conflict minerals used as catalysts in production would not be included unless the conflict material is also contained in the final product.

It should be noted that the SEC did not provide a "*de-minimis*" exemption. A company will be subject to the regulations and disclosure requirements if conflict minerals in any amount are necessary to the functionality or production of a product manufactured or contracted to be manufactured by such company.

## **2. A Reasonable country of origin inquiry.**

Companies concluding that conflict minerals are necessary to the functionality or production of any of their products must conduct a good faith "reasonable country of origin inquiry" with regard to those minerals. This inquiry must be reasonably designed to determine whether any of its minerals originated in a covered country<sup>[2]</sup> or are from scrap or recycled sources.

An issuer that either knows that the minerals did not originate in a covered country or are from scrap or recycled sources or has no reason to believe otherwise, is required to (i) file a Form SD that discloses that determination, provides a brief description of the inquiry it undertook, and the results of the inquiry; and (ii) make the description of its inquiry available on its website and provide the Internet address of its website disclosure in its Form SD.

## **3. Due diligence on the necessary conflict minerals source and chain of custody.**

A company that knows or has reason to believe that the minerals may have originated in the covered countries and that the minerals may not be from recycled or scrap sources, must (i) undertake "due diligence" on the source and chain of custody of its conflict minerals; (ii) file a Conflict Minerals Report as an exhibit to its Form SD; (iii) make the Conflict Minerals Report publicly available on its website; and (iv) provide the Internet address of that website in its Form SD.

Following this due diligence, an issuer's disclosure obligations will depend on whether its products are "DRC Conflict Free," "Not 'DRC Conflict Free,'" or "DRC Conflict Undeterminable."

### *A. "DRC Conflict Free"*

If an issuer either determines that its minerals (i) may have originated from the covered countries but did not finance or benefit armed groups; or (ii) derived from recycled or scrap sources, then the issuer will be required to:

- obtain an independent private sector audit of its Conflict Minerals Report to confirm whether the due diligence framework conforms to a nationally or internationally recognized due diligence framework; and whether the company actually performed the due diligence as described in the Conflict Minerals Report;
- certify that it obtained such an audit;
- include the audit report as part of the Conflict Minerals Report; and
- identify the auditor.

### *B. "Not 'DRC Conflict Free'"*

If the minerals are not DRC Conflict Free, in addition to the abovementioned requirements, the company must describe the following in its Conflict Minerals Report:

- the products manufactured or contracted to be manufactured that have not been found to be “DRC Conflict Free;”
- the facilities used to process the conflict minerals in those products;
- the country of origin of the conflict minerals in those products; and
- the efforts to determine the mine or location of origin with the greatest possible specificity.

*C. “DRC conflict undeterminable.”*

The final rules will permit a company to classify minerals as “DRC conflict undeterminable” rather than “not conflict free” for up to two years (four years for smaller reporting companies) if it is unable to determine definitively whether minerals originated in a DRC country or financed or benefited armed groups in those countries. In these instances, the company will be required to describe the following in its Conflict Minerals Report:

- its products manufactured or contracted to be manufactured that are “DRC conflict undeterminable;”
- the facilities used to process the conflict minerals in those products, if known;
- the country of origin of the conflict minerals in those products, if known;
- the efforts to determine the mine or location of origin with the greatest possible specificity; and
- the steps it has taken or will take, if any, since the end of the period covered in its most recent Conflict Minerals Report to mitigate the risk that its necessary conflict minerals benefit armed groups, including any steps to improve due diligence.

For those products that are “DRC conflict undeterminable,” the company will not be required to obtain an independent private sector audit of the Conflict Minerals Report regarding the conflict minerals in those products.

Conflict minerals that are outside the supply chain prior to January 31, 2013 are exempt from the disclosure requirements. Therefore, issuers still have a four months window to adjust their products or vendors, if they do not want them to be a part of their process during the disclosure period.

**Liability for “false or misleading statement”**

As the new Form SD will be “filed” with the SEC, any materially “false or misleading statement” in the form will subject the company to liability under Section 18 of the Exchange Act. However, because the form is separate from a company’s annual report on Form 10-K, Form 20-For Form 40-F, it will not be covered by the CEO and CFO certifications accompanying these forms, or automatically incorporated into a company’s shelf registration statement.

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**Endnotes**

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[1] For purposes of the new disclosure requirement, the term “conflict minerals” is defined to include: Columbite-Tantalite, also known as coltan (the metal ore from which tantalum is extracted); Cassiterite (the metal ore from which tin is extracted); Gold; Wolframite (the metal ore from which tungsten is extracted); and any other mineral or its derivatives as subsequently determined by the Secretary of State. [2] The Democratic Republic of Congo or any of its adjoining countries (Angola, Burundi, the Central African Republic, The Republic of Congo, Rwanda, Sudan, Tanzania, Uganda and Zambia).

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