# SEC Adopts Final Rule Pursuant to the Dodd-Frank Act for Disclosing the Use of Conflict Minerals

*September 12, 2012*

On August 22, 2012, the Securities and Exchange Commission ("SEC") adopted a new rule pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act requiring public companies to make disclosures of "conflict minerals" in their products.[1] The rule is designed to reduce the funding of armed groups engaged in conflict in the Democratic Republic of Congo ("DRC") by mandating additional disclosure requirements on the use and source of certain minerals whose exploitation and trade Congress believed are contributing to significant human rights abuses in the DRC.

## COMPANIES COVERED BY THE RULE

Any reporting company that files reports with the SEC under Sections 13(a) and 15(d) of the Securities Exchange Act of 1934 ("Exchange Act"), including foreign private issuers, emerging growth companies and smaller reporting companies. It appears that voluntary filers are not subject to the rule.

## COMPLIANCE DATE

Reporting companies must comply with the rule for the calendar year beginning January 1, 2013, with the first reports due May 31, 2014.

## "CONFLICT MINERALS"

"Conflict minerals" include columbite-tantalite (also known as coltan), cassiterite, gold, wolframite, tantalum, tin, and tungsten.

- *Columbite-tantalite* is the metal ore from which tantalum is extracted. *Tantalum* is used in electronic components, including mobile telephones, computers, videogame consoles, and digital cameras, and as an alloy for making carbide tools and jet engine components.
- *Cassiterite* is the metal ore that is most commonly used to produce tin. *Tin* is used in alloys, tin plating, and solders for joining pipes and electronic circuits.
- *Gold* is used for making jewelry and is used in electronic, communications, and aerospace equipment.

[1] Final rule: Conflict Minerals, Release No. 34-67716 (August 22, 2012), available at http://www.sec.gov/rules/final/2012/34-67716.pdf.

- *Wolframite* is the metal ore that is used to produce tungsten. *Tungsten* is used for metal wires, electrodes, and contacts in lighting, electronic, electrical, heating, and welding applications.

Based on the many uses of these minerals, the SEC has indicated that it expects the rule to apply to approximately 6,000 reporting companies.

## APPLICATION OF THE RULE

The SEC adopted a three-step process to determine the conflict mineral disclosure requirements and procedures for reporting companies covered by the rule, which is summarized below. In addition, attached as Appendix A is a flow chart summary of the application of the rule prepared by the SEC and included in the adopting release.

### STEP 1 – DETERMINE WHETHER CONFLICT MINERALS ARE NECESSARY TO THE FUNCTIONALITY OR PRODUCTION OF A PRODUCT

A reporting company is required to file a new Form SD report for a given calendar year by May 31 of the following year if it determines that conflict minerals are necessary to the functionality or production of a product it manufactured or contracted to be manufactured in the applicable calendar year, including conflict minerals contained in a component of a product. The rule exempts any conflict minerals that were smelted, refined or already removed from a covered country (as defined below) prior to January 31, 2013.

*"Manufactured or Contracted to be Manufactured"*

- The SEC chose not to define "manufacture" for purposes of the rule as it believed that the term is generally understood. The rule, however, does not treat a company that mines conflict minerals as manufacturing those minerals unless the company also engages in manufacturing.
- Whether a company is considered to have "contracted to manufacture" a product (including a component of a product) depends on the degree of influence it exercises over the materials, parts, ingredients, or components to be included in the applicable product. A company will not be viewed as contracting to manufacture a product if its actions involve no more than:
    - (i) specifying or negotiating contractual terms with a manufacturer that do not directly relate to the manufacturing of the product; or
    - (ii) affixing its brand, marks, logo, or label to a generic product manufactured by a third party; or
    - (iii) servicing, maintaining, or repairing a product manufactured by a third party.

*"Necessary to the Functionality or Production of a Product"*

- The SEC did not define but rather provided guidance on when a conflict mineral is necessary to the functionality or production of a product. Under this guidance, a company should base this determination on the applicable facts and circumstances and consider:
    - (i) whether a conflict mineral is contained in and intentionally added to the product or any component of the product and is not a naturally-occurring by-product;
    - (ii) whether a conflict mineral is necessary to the product's generally expected function, use, or purpose; or
    - (iii) if a conflict mineral is incorporated for purposes of ornamentation, decoration or embellishment, whether the primary purpose of the product is ornamentation or decoration.
- The rule does not include a *de minimis* threshold based on the amount of conflict minerals used in a particular product.
- The inclusion of a conflict mineral in the manufacturing process but not in the final product, or in a tool or machine used to produce a product, are not considered necessary to the functionality or production of a product and therefore not covered by the rule.

If a reporting company determines that no conflict minerals are necessary to the functionality or production of any product it manufactured or contracted to be manufactured during the period in question, it would not be required to move to Step 2 below, take any action or submit any disclosures pursuant to the final rule.

## STEP 2 – COUNTRY OF ORIGIN INQUIRY

If a reporting company determines that conflict minerals are necessary to the functionality or production of a product it manufactured or contracted to be manufactured, it must then conduct in good faith a reasonable country of origin inquiry to determine whether any of the necessary conflict minerals originated in the DRC or an adjoining country (the "covered countries")[2] or are from recycled or scrap resources.

The adopting release indicates that this inquiry depends on the particular facts and circumstances and the rule does not prescribe any required elements or bright-line test. The inquiry standard may be satisfied if the company seeks and obtains reasonably reliable representations indicating the facility at which the necessary conflict minerals were processed and demonstrating that those conflict minerals did not originate in the covered countries or came from recycled or scrap sources. The inquiry standard does not require a company to determine to a certainty that all its conflict materials did not originate in the covered countries or came from recycled or scrap sources.

[2] The countries adjoining the DRC are Angola, Burundi, Central African Republic, the Republic of the Congo, Rwanda, South Sudan, Tanzania, Uganda, and Zambia.

- Representations may come directly from the facility or indirectly through the company's immediate suppliers, but the company must have reason to believe these representations are true given the facts and circumstances surrounding those representations.
- Conflict minerals are considered to be from recycled or scrap sources if they are from recycled metals, which are reclaimed end-user or post-consumer products, or scrap processed metals created during product manufacturing.

If, as the result of such inquiry, the company:

- determines that the necessary conflict minerals did not originate in a covered country or has no reason to believe that its necessary conflict minerals may have originated in a covered country, or
- determines or reasonably believes that the necessary conflict minerals came from recycled or scrap sources,

then it must disclose, on its publicly available Internet website and in a Form SD report to be filed not later than May 31 of the following calendar year (commencing with May 31, 2014), its determination and briefly describe the reasonable country of origin inquiry it undertook in making its determination and the results of the inquiry it performed. If the company cannot make this determination, it is required to move to Step 3 below.

**STEP 3 – SOURCE AND CHAIN OF CUSTODY DILIGENCE; CONFLICT MINERALS REPORT**

*Source and Chain of Custody Diligence*

If the reporting company, based on its reasonable country of origin inquiry, knows that any of its necessary conflict minerals originated in a covered country and are not from recycled or scrap sources, or has reason to believe that its necessary conflict minerals may have originated in a covered country and has reason to believe that they may not be from recycled or scrap sources, the company must exercise due diligence on the source and chain of custody of such necessary conflict minerals in conformity with a nationally or internationally recognized due diligence framework, if such a framework is available for the conflict mineral.

- While the rule does not mandate a particular framework, the SEC notes that the only nationally or internationally recognized due diligence framework currently available is the due diligence guidance approved by the Organisation for Economic Co-operation and Development ("OECD").[3]

[3] See OECD, OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas (2011), available at http://www.oecd.org/daf/internationalinvestment/guidelinesformultinationalenterprises/46740847.pdf.

- A company is also required to use a recognized due diligence framework with respect to recycled or scrap conflict minerals. The SEC is not aware of a framework for recycled or scrap conflict minerals other than for gold.[4]

- In circumstances where a nationally or internationally recognized due diligence framework becomes available for a conflict mineral for which no nationally or internationally recognized due diligence framework previously existed, reporting companies will be required to utilize that framework. Otherwise, due diligence must be conducted without the benefit of a nationally or internationally recognized framework.

If, as a result of the required due diligence investigation, the company determines that its necessary conflict minerals did not originate in a covered country or that its necessary conflict minerals did come from recycled or scrap sources, the reporting company must disclose, on its publicly available Internet website and in a Form SD report, its determination and briefly describe the reasonable country of origin inquiry and the due diligence efforts it undertook in making its determination. Otherwise, the reporting company must file a Conflict Minerals Report as an exhibit to its Form SD report as described below.

*Conflict Minerals Report*

If, as a result of the company's due diligence investigation, it either (i) determines that its necessary conflict minerals did originate in a covered country and did not come from recycled or scrap sources or (ii) cannot determine the source of its conflict minerals, then the company is required to file a Conflict Minerals Report as an exhibit to its Form SD report.

The Conflict Minerals Report is required to include the following information:

- A description of the measures the company has taken to exercise due diligence on the source and chain of custody of those conflict minerals.

- A description of the company's products manufactured or contracted to be manufactured containing necessary conflict minerals that are not "DRC conflict free,"[5] the facilities used to process the necessary conflict minerals in those products, the

[4] See OECD, OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas: Supplement on Gold (2012), available at http://www.oecd.org/corporate/guidelinesformultinationalenterprises/FINAL%20Supplement%20on%20Gold.pdf.

[5] The rule provides that "DRC conflict free" means that a product does not contain conflict minerals necessary to the functionality or production of that product that directly or indirectly finance or benefit armed groups in a covered country. Conflict minerals that a company obtains from recycled or scrap sources are considered DRC conflict free. The rule defines an armed group as an armed group that is identified as a perpetrator of serious human rights abuses in the annual Country Reports on Human Rights Practices under sections 116(d) and 502B(b) of the Foreign Assistance Act of 1961 (22 U.S.C. 2151n(d) and 2304(b)) relating to a covered country.

country of origin of the necessary conflict minerals in those products, and the efforts to determine the mine or location of origin with the greatest possible specificity.

- A copy of a report prepared by an independent private sector auditor that expresses an opinion or conclusion as to whether the design of the due diligence measures as set forth in the Conflict Minerals Report is in conformity with, in all material respects, the criteria set forth in the due diligence framework used by the company, and whether the company's description of the due diligence measures it performed is consistent with the due diligence process that the company undertook.

*DRC Conflict Undeterminable*

If a company is unable to determine, after exercising due diligence as required by the rule, whether or not a product it manufactured or contracted to manufacture qualifies as DRC conflict free, it may avail itself of a transition period for a "DRC conflict undeterminable" product.

- The transition period is two years for all reporting companies and four years for smaller reporting companies.

- During the transition period, reporting companies will temporarily not be required to obtain an independent private sector audit of their Conflict Minerals Report with respect to those minerals that are DRC conflict undeterminable.

- A company that avails itself of this designation must still file a Conflict Minerals Report describing its due diligence, and must additionally describe the steps it has taken or will take, if any, to mitigate the risk that its necessary conflict minerals benefit armed groups, including any steps to improve its due diligence.

## DISCLOSURE LIABILITY

Conflict minerals information provided on a Form SD report, including the Conflict Minerals Report and the independent auditors reports, will be considered "filed" with the SEC and therefore will be subject to liability under Section 18 of the Exchange Act. Section 18 of the Exchange Act creates liability for "[a]ny person who shall make or cause to be made any statement in any application, report, or document … which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable…" Section 18 provides for a private right of action to investors who can prove they were harmed by relying on the misstatement. Section 18, however, does not create strict liability for filed information and provides that a company will not be liable for misstatements in a filed document if it can establish that it "acted in good faith and had no knowledge that such statement was false or misleading."

The information provided on a Form SD report, including the Conflict Minerals Report and the independent auditors reports, would not be deemed to be incorporated by reference into a reporting company's filings under the Securities Act of 1933 unless it specifically elects to do so.

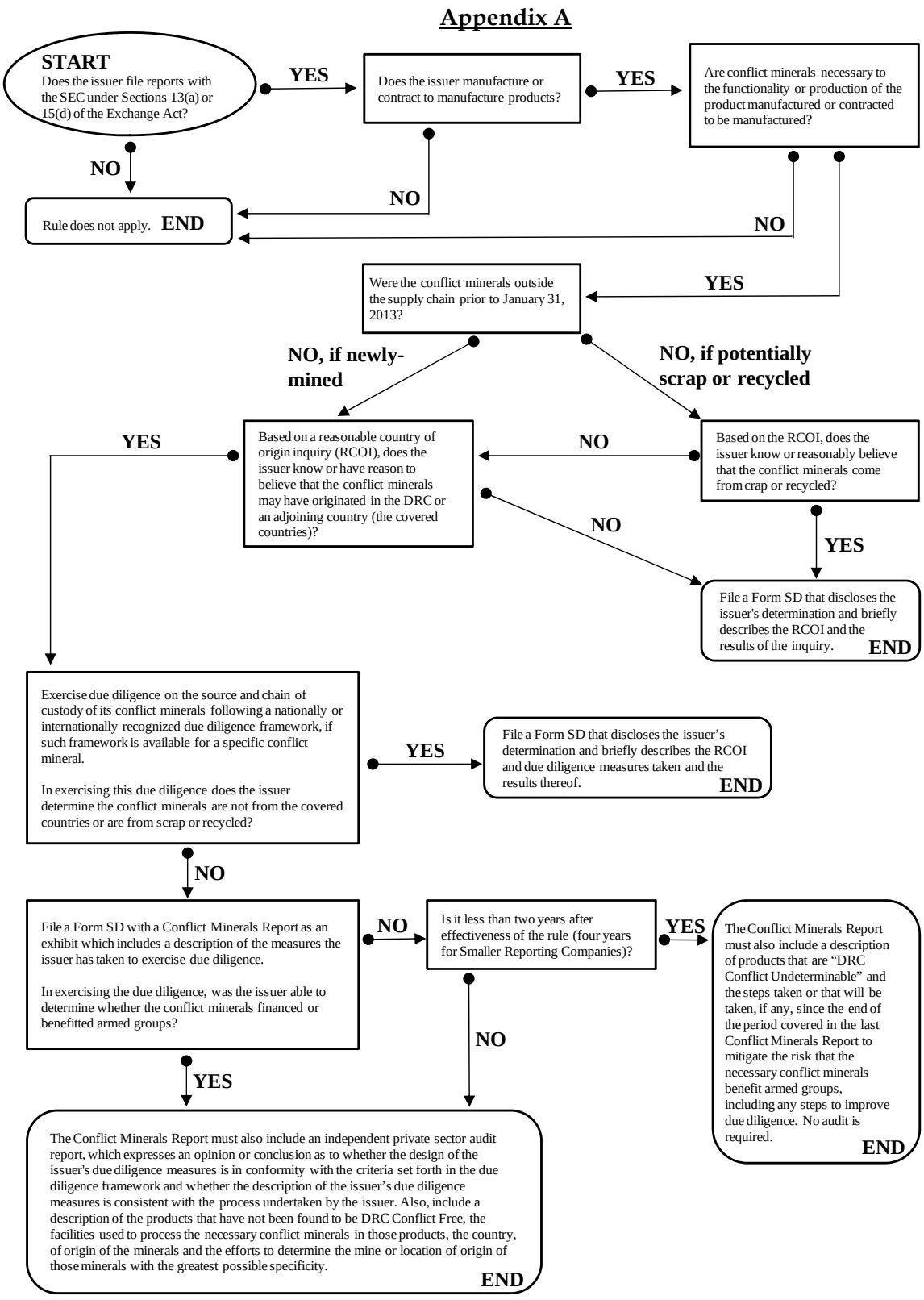
Unlike a reporting company's Annual Report on Form 10-K or Quarterly Report on Form 10-Q, the disclosures in a Form SD report would not be subject to officer certifications.

## CONCLUSION

The rule is complicated and different than any other rule under the federal securities laws. There are many provisions of the rule where the SEC has elected to allow reporting companies to make their own determinations as to interpretation and application and, as a result, we believe that industry specific practices will develop on how to comply with the rule. Given that the first reporting period commences on January 1, 2013, we recommend that companies make a determination as to the rule's applicability based on their specific facts and circumstances utilizing a broad based team consisting of internal procurement, legal and financial teams, outside legal counsel and other consultants and professionals.

*This memorandum is for general information purposes and should not be regarded as legal advice. Please contact your relationship partner if we can be of assistance regarding these important developments. The names and office locations of all of our partners, as well as our recent memoranda, can be obtained from our website, www.simpsonthacher.com.*

## Appendix A




Source: Securities and Exchange Commission, Conflict Minerals, Release No. 34-67716 (August 22, 2012)

## UNITED STATES

**New York**
425 Lexington Avenue
New York, NY 10017
+1-212-455-2000

**Houston**
2 Houston Center
909 Fannin Street
Houston, TX 77010
+1-713-821-5650

**Los Angeles**
1999 Avenue of the Stars
Los Angeles, CA 90067
+1-310-407-7500

**Palo Alto**
2550 Hanover Street
Palo Alto, CA 94304
+1-650-251-5000

**Washington, D.C.**
1155 F Street, N.W.
Washington, D.C. 20004
+1-202-636-5500

## EUROPE

**London**
CityPoint
One Ropemaker Street
London EC2Y 9HU
England
+44-(0)20-7275-6500

## ASIA

**Beijing**
3919 China World Tower
1 Jian Guo Men Wai Avenue
Beijing 100004
China
+86-10-5965-2999

**Hong Kong**
ICBC Tower
3 Garden Road, Central
Hong Kong
+852-2514-7600

**Tokyo**
Ark Mori Building
12-32, Akasaka 1-Chome
Minato-Ku, Tokyo 107-6037
Japan
+81-3-5562-6200

## SOUTH AMERICA

**São Paulo**
Av. Presidente Juscelino Kubitschek, 1455
São Paulo, SP 04543-011
Brazil
+55-11-3546-1000