

August 22, 2012

The Securities and Exchange Commission Finalizes Conflict Mineral Rules - The Reporting Countdown Begins

On August 22, 2012, the Securities and Exchange Commission (“SEC”) issued final Conflict Minerals reporting rules under Section 1502 of the Dodd-Frank Act (“Act”). The intent of the Act is to deter companies from using Conflict Minerals purchased in the Democratic Republic of the Congo (“DRC”) and surrounding areas, which may fund conflict and extreme violence in the DRC. The complexity of compliance and implementation will have a major impact on both public and private companies, both financially and in their relationships with customers and suppliers. The SEC estimates the cost of compliance to be between \$3 billion and \$4 billion, while others estimate the cost may be more than double. This Alert provides an overview of the requirements and impact of the new rules.

What Are Conflict Minerals?

Conflict Minerals are: (i) columbite-tantalite (coltan/tantalum), (ii) cassiterite (tin), (iii) gold, (iv) wolframite (tungsten), and (v) any of their derivatives. The reporting requirements focus on Conflict Minerals purchased from the Democratic Republic of the Congo (“DRC”) or adjoining nations (“DRC Conflict Minerals”). The Secretary of State may add additional minerals to the list if found to be financing conflict and violence in the DRC.

Who Must Comply?

Businesses which file reports with the SEC (“Public Companies”) and which use Conflict Minerals that are “necessary to the functionality of production of a product manufactured by such person” must comply with the new rules. In other words, compliance is required for: (i) a public company; (ii) which manufactures goods; (iii) which contain Conflict Minerals. As a practical matter, the rules will also significantly affect and burden **all** suppliers using Conflict Minerals in products sold to Public Companies, because the Public Companies must obtain information from their supply chain in order to comply with the rules. Since suppliers may not know whether they or their sub-suppliers use Conflict Minerals, they must undertake compliance efforts even if it is ultimately determined that no Conflict Minerals are used in the supply chain.

What Must be Disclosed?

Public Companies must file with the SEC an annual report disclosing:

- the products manufactured containing DRC Conflict Minerals (or that the products are DRC Conflict Mineral free);
- due diligence measures taken to determine the source and chain of custody of the Conflict Minerals; and
- a certified, independent private sector audit of its compliance methods and procedures.

In addition to its SEC filings, Public Companies must publish on its website the SEC disclosures, except for the private sector audit.

What is the Deadline for Compliance?

Public Companies must file a report for the 2013 calendar year no later than May 31, 2014. All reports will be on a calendar year basis in a new “Form SD,” rather than on a fiscal year basis as part of its Annual Report. For the first two years (four years for small businesses), Public Companies may declare Conflict Mineral origins as “undeterminable” while performing due diligence on the mineral source.

Are There Any Compliance Exceptions?

Conflict Minerals from a scrap or recycled source are subject to different reporting requirements. Reporting is required but it is sufficient to file a Conflict Minerals report stating that minerals were obtained from recycled or scrap sources and why it is believed that the minerals were from a recycled or scrapped source. Public Companies are required to exercise due diligence in determining that the Conflict Minerals were recycled or scrapped through the independent private sector audit requirement.

Although widely supported by industry groups, the rules do not provide an exception for *de minimus* or negligible use of DRC Conflict Minerals. Any use, regardless of amount used, must be reported.

Are Non-Manufacturers Required to Comply?

No, with an important exception. Non-manufacturers, such as retailers, who use contract manufacturing or private-labeling (i.e. selling products under their own brand name) are required to comply.

Are Industry Groups Preparing for Compliance?

Many industry groups are assisting member companies to comply with the law by providing a forum for information exchange and development of best practices and common protocols for compliance. These associations include:

- AIA (Aerospace Industry Association) – The AIA’s working group offers a letter for distribution to downstream suppliers
- AIAG (Automotive Industry Action Group) – The AIAG sent a letter to the automotive supply base with general compliance information and has a Frequently Asked Questions list and webinars available for review
- EICC-GeSI (Electronics Industry Citizenship Coalition and Global e-Sustainability Initiative) – The EICC-GeSI offers tools to trace Conflict Minerals through the supply chain including a due diligence reporting template and dashboard.
- OESA (Original Equipment Suppliers Association) – OESA offers member companies a forum for peer-to-peer information exchange and best practices for compliance.

What Should I Do to Prepare for Compliance?

Review your Terms and Conditions

- Evaluate whether your Terms and Conditions are sufficient to obligate your suppliers to provide you with the necessary information and otherwise allow you to satisfy your compliance obligations.

Monitor and consider participating in industry groups or other organizations in the development of common protocols and related means of most efficiently complying

Create a strong Conflict Mineral management system and policy

- Create a task force with representation from all necessary business areas to develop necessary systems and policies. Include outside advisors (e.g. legal and auditors) if necessary.
- Create a policy on Conflict Mineral management to be cascaded to lower tier suppliers.
- Internally promote compliance with all Conflict Minerals requirements.
- Engaging suppliers in compliance efforts, including allowing them to express concerns or provide feedback regarding handling documentation and auditing.

Identify components and suppliers likely to report compliance

- Analyze the Bill of Materials (BOM) to determine which components and suppliers will likely contain Conflict Minerals
- Assess the compliance risk from each of these entities
- Identify any information in purchasing or quality records regarding the country of origin for raw materials

Implement a strategy to manage at-risk suppliers

- Establish a purchasing policy to assist with any necessary supply chain changes in trade or resourcing if the risk cannot be managed

Plan for auditing

- Determine if a customer or OEM will assist in providing audit support
- Hire an audit firm

Butzel Long is prepared to assist you in complying with these new and perhaps onerous requirements. For assistance, please contact your Butzel Long attorney or the authors of this Client Alert.

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