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SEC Adopts Rules Under Dodd-Frank Requiring Disclosure Regarding Use of Conflict Minerals

On August 22, 2012, the SEC adopted its final rule implementing Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which we refer to as the "Conflict Minerals Rule" or the "final rule." Section 1502 added Section 13(p) to the Securities Exchange Act of 1934, as amended (the "Exchange Act"), which required the Commission to promulgate rules requiring companies that (1) file reports with the SEC under the Exchange Act ("issuers") and (2) use conflict minerals[1] necessary to the functionality or production of a product manufactured by the issuer, to disclose annually whether any of those conflict minerals originated in the Democratic Republic of the Congo or an adjoining country (the "Covered Countries"). If an issuer's conflict minerals originated in the Covered Countries, Section 13(p) requires the issuer to submit a report to the SEC that includes a description of the measures it took to exercise due diligence on the conflict minerals' source and chain of custody, including an independent private sector audit of the report (a "Conflict Minerals Report"). Section 13(p) requires that the Conflict Minerals Report include a description of the products manufactured or contracted to be manufactured that are not "DRC conflict free,"[2] the facilities used to process the conflict minerals, the country of origin of the conflict minerals and the efforts to determine the mine or location of origin, and that the information contained in the Conflict Minerals Report be published on the issuer's website.

The final rule includes significant changes to the original rule proposal, including:

- determining that mining or contracting to mine conflict minerals is not "manufacturing" or "contracting to manufacture" conflict minerals and, therefore, an issuer engaged in mining will not be subject to the Conflicts Mineral Rule unless the issuer also engages in manufacturing of conflict minerals, whether directly or indirectly through contract;
- providing an exemption from the final rule's disclosure requirements for any conflict minerals that are "outside the supply chain" prior to January 31, 2013;
- requiring conflict minerals disclosure to be made on the basis of a calendar year, beginning with calendar year 2013, regardless of an issuer's fiscal year end;

[1] The term "conflict mineral" is defined as (A) 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); or their derivatives; or (B) any other mineral or its derivatives determined by the Secretary of State to be financing conflict in the Democratic Republic of the Congo or an adjoining country.

[2] "DRC conflict free" is defined as a product that does not contain conflict minerals that directly or indirectly finance or benefit armed groups in the Covered Countries.

- requiring issuers to file any conflict minerals disclosure on a new form, Form SD, by May 31 of each year, beginning on May 31, 2014; and
- providing a temporary transition period of two years (four years for smaller reporting companies), during which time issuers may describe their products as "DRC conflict undeterminable" and will not be required to have their Conflict Minerals Reports audited with respect to such "DRC conflict undeterminable" products.

The disclosure requirements under the Conflict Minerals Rule are divided into three steps:

- determining whether an issuer is subject to the final rule;
- conducting a country of origin inquiry; and
- providing a Conflict Minerals Report and conducting supply chain due diligence.

Step One – Issuers Subject to the Final Rule

Issuers That File Reports Under the Exchange Act. The final rule applies to "issuers," that is, companies that file reports with the SEC under Section 13(a) or 15(d) of the Exchange Act, including U.S. domestic issuers and foreign private issuers. Canadian issuers that file reports with the SEC under the U.S.-Canada Multi-Jurisdictional Disclosure System ("MJDS") are also subject to the final rule. Foreign private issuers that are exempt from Exchange Act registration under Rule 12g3-2(b) are not subject to the final rule.

Manufacture or Contract to Manufacture Products. If conflict minerals are *necessary* to the functionality or production of a product manufactured by an issuer or contracted by an issuer to be manufactured, such issuer is subject to the Conflict Minerals Rule and must perform, at a minimum, a reasonable country of origin inquiry regarding such conflict minerals. If conflict minerals are <u>not</u> necessary to the functionality or production of a product manufactured by an issuer or contracted by an issuer to be manufactured, such issuer is not required to perform any inquiry, file any report or perform any due diligence with respect to such conflict minerals.

Whether an issuer will be considered to "contract to manufacture" a product depends on the degree of influence it exercises over the materials, parts, ingredients or components to be included in any product that contains conflict minerals or their derivatives.

An issuer will not be considered to "contract to manufacture" a product if its actions involve no more than:

- specifying or negotiating contractual terms with a manufacturer that do not directly relate to the manufacturing of the product (unless the issuer specifies or negotiates taking these actions so as to exercise a degree of influence over the manufacturing of the product that is practically equivalent to contracting on terms that directly relate to the manufacturing of the product);
- affixing the issuer's brand, marks, logo, or label to a generic product manufactured by a third party without additional involvement by the issuer; or

- servicing, maintaining or repairing a product manufactured by a third party.

Mining is not Manufacturing. The final rule clarifies that the SEC does not consider an issuer that mines or contracts to mine conflict minerals to be manufacturing or contracting to manufacture those minerals unless the issuer also engages in manufacturing, whether directly or indirectly through contract, in addition to mining.

Outside the Supply Chain. The final rule exempts from the disclosure requirements thereunder any conflict minerals that are "outside the supply chain" prior to January 31, 2013. Under the final rule, "outside the supply chain" means (1) after conflict minerals have been smelted (in the case of tantalum, tin or tungsten) or refined (in the case of gold), or (2) if not smelted or refined, the conflict minerals are physically located outside of the Covered Countries, in each case prior to January 31, 2013.

When Conflict Minerals Are Necessary to a Product. The determination of whether a conflict mineral is deemed "necessary to the functionality" or "necessary to the production" of a product depends on the issuer's particular facts and circumstances.

The SEC provided the following guidance to assist issuers in making their determination:

- in determining whether a conflict mineral is "*necessary to the functionality*" of a product, an issuer should consider: (1) whether the conflict mineral is intentionally added to the product or any component of the product and is not a naturally-occurring by-product; (2) whether the conflict mineral is necessary to the product's generally expected function, use or purpose; and (3) if the conflict mineral is incorporated for purposes of ornamentation, decoration or embellishment, whether the primary purpose of the product is ornamentation or decoration; and
- in determining whether a conflict mineral is "*necessary to the production*" of a product, an issuer should consider: (1) whether the conflict mineral is intentionally included in the product's production process, other than if it is included in a tool, machine or equipment used to produce the product (such as computers or power lines); (2) whether the conflict mineral is included in the product; and (3) whether the conflict mineral is necessary to produce the product.
- For a conflict mineral to be deemed necessary to the production of a product, the mineral must be both contained in the product and necessary to the product's production. If a conflict mineral is merely used as a catalyst to produce the product but is not contained in that product, then the conflict mineral is deemed <u>not</u> necessary to the production of the product.

Step Two -- Country of Origin Inquiry

Issuers for which conflict minerals are necessary to the functionality or production of a product manufactured by that issuer, or contracted by that issuer to be manufactured, are required to conduct a "reasonable country of origin inquiry" regarding the origin of its conflict minerals. To satisfy this requirement, an issuer must conduct a good faith inquiry that is reasonably designed to determine whether any of its conflict minerals originated in the Covered Countries or are from recycled or scrap sources.

Reasonable Inquiry. An issuer will satisfy the reasonable country of origin inquiry requirement if the issuer seeks and obtains reasonably reliable representations indicating the facility at which its conflict minerals were processed and demonstrating that those conflict minerals did not originate in the Covered Countries or came from recycled or scrap sources. In determining the reliability of the representations, an issuer must take into account any applicable warning signs or other circumstances indicating that its conflict minerals may have originated in the Covered Countries or did not come from recycled or scrap sources.

The final rule states that an issuer will have a reasonable basis to believe that representations of a supplier are true if the supplier has a "conflict-free" designation from a recognized industry group that requires an independent private sector audit or if the supplier obtained an independent private sector audit that is made publicly available.

The final rule also states that an issuer is not required to receive representations from all of its suppliers as the standard focuses on reasonable design and good faith inquiry.

The final rule does not require an issuer to retain reviewable business records to support the conclusion of its reasonable country of origin inquiry.

Disclosure Requirements. Under the final rule, an issuer that determines that its conflict minerals did not originate in the Covered Countries or did come from recycled or scrap sources is required to disclose its determination and briefly describe the reasonable country of origin inquiry and the results of the inquiry on a Form SD filed with the SEC.

Step Three – Content of Conflict Minerals Report and Supply Chain Due Diligence

Content of Conflict Minerals Report. The final rule requires any issuer that, after its reasonable country of origin inquiry, knows or has reason to know that its conflict minerals originated in the Covered Countries and did not come from recycled or scrap sources to provide a Conflict Minerals Report describing the measures the issuer has taken to exercise due diligence on the source and chain of custody of those conflict minerals. In either case, such issuer must also, subject to the temporary transition period described below, obtain an independent private sector audit of the Conflict Minerals Report, and such Conflict Minerals Report must certify that the issuer has obtained such audit (such certification need not be signed by an officer), identify the auditor and include the audit report.

In addition, unless an issuer's products are "DRC conflict free," the Conflict Minerals Report must include a description of the products manufactured or contracted to be manufactured that have not been found to be "DRC conflict free," the facilities used to process those conflict minerals, the country of origin of those conflict minerals and the efforts to determine the mine or location of origin with the greatest possible specificity.

An issuer is not required to submit a Conflict Minerals Report if, during the exercise of its due diligence, it determines that its conflict minerals did not, in fact, originate in the Covered Countries, or it determines that its conflict minerals did, in fact, come from recycled or scrap sources. Such an issuer is still required to submit a Form SD disclosing its determination (including a brief description of its inquiry and its due diligence efforts) and demonstrating

why the issuer believes that the conflict minerals did not originate in the Covered Countries or that they did come from recycled or scrap sources.

Temporary Transition Period. For a temporary transition period of two years (four years for smaller reporting companies), an issuer may describe its products as "DRC conflict undeterminable" if it is unable to determine whether the minerals in its products originated in the Covered Countries or financed or benefited armed groups in those countries. Issuers with products that may be described as "DRC conflict undeterminable" are not required to have their Conflict Minerals Report with respect to their "DRC conflict undeterminable" products audited. Such issuers, however, must still file a Form SD, including a Conflict Minerals Report describing the issuer's due diligence investigation, and must additionally include a description of the 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 they have taken or will take, if any, since the end of the period covered in their most recent prior Conflict Minerals Report, to mitigate the risk that their necessary conflict minerals benefit armed groups, including any steps to improve their due diligence.

Supply Chain Due Diligence. An issuer's due diligence must follow a nationally or internationally recognized due diligence framework, such as the OECD's "Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas".[3] An issuer may also use any nationally or internationally recognized due diligence framework, as long as such framework has been established by a body or group that has followed due-process procedures and is consistent with the criteria established by the Government Accountability Office ("GAO") in its existing Government Auditing Standards ("GAGAS").

Independent Private Sector Audit Requirements. The final rule established the objective for independent private sector audits of Conflict Minerals Reports. The objective of the audit is to express an opinion or conclusion as to whether the design of the issuer's due diligence measures as set forth in the Conflict Minerals Report, with respect to the period covered by the report, is in conformity with, in all material respects, the criteria set forth in the nationally or internationally recognized due diligence framework used by the issuer, and whether the issuer's description of the due diligence measures it performed as set forth in the Conflict Minerals Report, with respect to the period covered by the report, is consistent with the due diligence process that the issuer undertook.

Recycled and Scrap Minerals. 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. The definition includes excess, obsolete, defective and scrap metal materials that contain refined or processed metals that are appropriate to recycle in the production of tin, tantalum, tungsten

[3] The OECD's "Due Diligence Guidance" can be found at: http://www.oecd.org/daf/internationalinvestment/guidelinesformultinationalenterprises/46740847.pdf

and/or gold, but excludes minerals partially processed, unprocessed or a byproduct from another ore.

The final rule requires issuers conducting due diligence regarding whether their conflict minerals are from recycled or scrap sources to conform such due diligence to a nationally or internationally recognized due diligence framework, if one is available for a particular recycled or scrap conflict mineral.

A gold supplement to the OECD's due diligence guidance has been approved by the OECD. This gold supplement is presently the only nationally or internationally recognized due diligence framework for any conflict mineral from recycled or scrap sources and the SEC anticipates that issuers will use the OECD gold supplement to conduct their due diligence for recycled or scrap gold.

Issuers are still required to exercise due diligence in determining whether conflict minerals were from recycled or scrap sources with respect to conflict minerals for which there is not a nationally or internationally recognized due diligence framework.

Location, Timing and Status of Conflict Minerals Information

Form SD. The final rule requires an issuer to provide the conflict minerals disclosure in the body of a new form, Form SD, to be filed with the SEC. An issuer required to provide a Conflict Minerals Report will provide that report as an exhibit to Form SD. An issuer must also make the information contained in its conflict minerals disclosure or the Conflict Minerals Report itself available on the issuer's website for one year and include the address of its website in the Form SD.

Timing. The final rule requires that the conflict minerals disclosure and/or Conflict Minerals Report included in Form SD cover the calendar year from January 1 to December 31 regardless of an issuer's fiscal year end. The first Form SD will cover calendar year 2013. The final rule requires that an issuer's Form SD, including its Conflict Minerals Report if applicable, be filed with the SEC no later than May 31 reporting on the preceding calendar year, with the first Form SD being filed no later than May 31, 2014. An issuer must provide its required conflict minerals information for the calendar year in which it completes the manufacture of a product that contains any conflict minerals or in which the issuer's contract manufacturer completes the manufacture of a product that contains any conflict minerals.

Merger and Acquisition Exception. The final rule permits an issuer that obtains control over a company that manufactures or contracts for the manufacturing of products with necessary conflict minerals and that previously had not been obligated to provide conflict minerals disclosure to delay reporting on the acquired company's products until the end of the first reporting calendar year that begins no sooner than eight months after the effective date of the acquisition.

"Filed" not "Furnished." The final rule requires Form SD, including any Conflict Minerals Report provided as an exhibit to the form, to be "filed" with the SEC and therefore subject to potential liability under Section 18 of the Exchange Act. However, the Form SD will not be

subject to CEO and CFO certifications and will not be automatically incorporated by reference in an issuer's registration statement.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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