SEC Conflict Minerals Rule Upheld in U.S. District Court Decision: Manufacturers are Urged to Proceed with Developing Their Conflict Minerals Programs

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Court Decision

In a July 23, 2013, decision, the U.S. District Court for the District of Columbia rejected challenges to the Security and Exchange Commission's (SEC) Conflict Minerals Rule (CM Rule) brought by plaintiffs the National Association of Manufacturers, the U.S. Chamber of Commerce, and the Business Roundtable. The CM Rule was upheld in its entirety.

The plaintiffs are considering an appeal to the U.S. Court of Appeals for the D.C. Circuit. Even if the matter is appealed, a decision from the D.C. Circuit is not expected until at least late winter or spring of 2014. Meanwhile, the CM Rule is in full force, with manufacturers of products containing the conflict minerals tin, tantalum, tungsten or gold (3TGs) necessary to the production or function of their products facing a May 31, 2014, deadline for filing the first annual report to the SEC under the rule. That first report will cover production during calendar year 2013. Therefore, time is of the essence and we are urging manufacturers of products containing 3TGs to proceed with developing their conflict minerals programs immediately.

Background and Applicability of the CM Rule

Congress directed the SEC to develop the CM Rule in the Dodd-Frank "Wall Street Reform and Consumer Protection Act" of 2010, Section 1502. Its purpose is to discourage the use of the four conflict minerals originating from mines in the Democratic Republic of the Congo (DRC) and surrounding countries ("covered countries"). Such mines are known to be sources of funding for conflicts in the region. The rule is applicable to companies that file reports with the SEC under Sections 13(a) or 15(d) of the Exchange Act (generally, publicly-traded companies) if the companies "manufacture or contract to manufacture" products containing conflict minerals "necessary to the functionality or production" of the product.

While the reporting requirements of the rule are limited to publicly-traded companies, the sweep of the rule is far greater. To meet the reporting requirements, publicly-traded companies are finding it necessary to institute complex supply chain tracing, or tracking, schemes from the finished product back to the mine/smelter/refiner. Many non-publicly-traded companies along the supply chain are

thus caught in the mineral source-tracking processes, at the insistence of their customers. This pressure up the supply chain creates demands from the customer that suppliers certify that their material is “DRC Conflict Mineral Free.”

Manufacturers, both privately held and publicly traded, who have any necessary 3TGs in their products, are impacted by the CM Rule and need to develop conflict minerals programs NOW.

Next Steps

The complexities of a full Conflict Minerals Program are beyond the scope of this Alert, but to get started, a company should:

1. Establish a company “Conflict Minerals Team” to lead the issue and to prepare a “Conflict Minerals Plan.”

2. Develop a company Conflict Minerals Policy to be posted on the company website.

3. Compile a list of products containing the 3TGs.

4. Prepare a list of customers to whom you are selling these products.

5. List the suppliers selling you these products.

6. Make initial contact with your suppliers to discuss the conflict minerals issue and to prepare for the “Reasonable Country of Origin Inquiry.”

The Reasonable Country of Origin Inquiry (RCOI) is key to the program. It is required by the CM Rule but is not clearly defined. The rule merely states that the RCOI must be performed in good faith and reasonably designed to determine if the conflict minerals originated in the DRC or other covered countries or are from scrap or recycled material. The minimum requirements for an adequate RCOI are being widely debated among those attempting to comply with the rule. It is generally agreed that it must go beyond merely asking first tier suppliers whether the minerals originated in the DRC and beyond accepting the suppliers’ answers at face value.

Depending on the results of the RCOI, further steps might be necessary. If the result is that none of the conflict minerals originated in the covered countries, then reporting companies will file a Form SD. If the conclusion is that some or all of the minerals did originate in the covered countries, a further due diligence step must be undertaken to determine if the originating mines in the covered countries are contributing to the conflict.

For more details on the RCOI and other aspects of the rule, please see the Kelley Drye & Warren Client Advisory “Securities and Exchange Commission (SEC) Approves Final “Conflict Minerals Rule,” August 29, 2012.

Conclusion

The SEC CM Rule has now undergone the first stage of judicial review and survived intact. With the first production year more than half finished, and the first reporting deadline only months away, it would not be wise for manufacturers to delay the implementation of Conflict Minerals Programs in the hope that an appeal to the U.S. Court of Appeals will delay the necessity of developing the appropriate procedures.

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