

## Conflict Minerals: The What & Why

*New SEC filing rule has unexpected consequences for distributors*

*The first filing deadline for the conflict minerals provision of the Dodd-Frank Act is fast approaching. While the provision – requiring disclosure of the use of tungsten, tin, tantalum and gold sourced in and around the Democratic Republic of the Congo – only directly applies to public manufacturers, the actual impact is much broader than anticipated, and many distributors aren't sure of the steps they need to take to comply.*

*This article examines the conflict minerals rule and how its effects are being felt all along the supply chain. It also provides practical information on how distributors can prepare for helping customers comply with the new rule.*

### By Jenel Stelton-Holtmeier

In 2010, the U.S. Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act in response to the financial crisis that many say sparked the Great Recession. Included in the law's numerous points, Section 1502 established a U.S. Securities and Exchange Commission filing requirement for public manufacturers related to the use of four minerals sourced from regions of Africa in and around the Democratic Republic of the Congo, or so-called "conflict minerals."

While the provision is relatively specific with regards to whom it applies and which minerals are covered, the impact of the requirement is much broader. Because many manufacturers don't source directly from the mines, they have to reach out to their suppliers – often distributors – to trace the material back to its origin.

### The Conflict Minerals Rule

Section 1502 requires public companies to determine if any of the products they manufacture with the identified conflict minerals – tungsten, tin, tantalum and

### Conflict Minerals Overview

**Included minerals:** tantalum, tin, tungsten and gold

**Common products:** electronic goods, automotive components, tools, jewelry, machinery, wiring, alloys

**Conflict area:** Democratic Republic of the Congo and surrounding countries: Congo, Central African Republic, Angola, Southern Sudan, Uganda, Rwanda, Tanzania, Malawi, Zambia.

### Resources:

The Conflict-Free Sourcing Initiative  
<http://www.conflictreesmelter.org>

SEC Final Rule on Conflict Minerals  
<http://www.sec.gov/rules/final/2012/34-67716.pdf>

NAED Conflict Minerals Forum  
[http://forum.naed.org/forum.asp?FORUM\\_ID=80](http://forum.naed.org/forum.asp?FORUM_ID=80)

gold – were sourced from mines in the Democratic Republic of the Congo or the surrounding area. Materials from scrap or recycled material are not considered to be from the conflict zone.

These materials are commonly used in many products or components, including smartphones and other electronics, tools, automobiles and jewelry.

The concern, according to the text of the final bill, is that the trade of these materials is "helping to finance conflict characterized by extreme levels of violence in the eastern Democratic Republic of the

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Congo.” Of particular concern are sexual- and gender-based violence and the prominence of child labor used in many of the mines.

The rule applies only to companies that are required to file reports with the SEC and who manufacture goods in which the conflict minerals are necessary to the functionality of the product, according to an advisory released by law firm Covington & Burling LLP. Packaging, unless that is the manufactured product, is not considered a functional element.

Companies that contract to manufacture may also be subject to the requirement, even if they do not directly manufacture the product themselves, depending on the “degree of influence” the company has over the manufacture of the product, according to the SEC. As such, some distributors who offer private label products that go beyond affixing a brand to a generic product – in other words, if they are involved in the design and composition of the products – may be included in the filing requirements, although no specific threshold of “influence” has been established.

Companies that are covered by the rule will have to file an annual report with the SEC detailing the steps taken to determine the origin of the conflict minerals, including a private sector audit of the report, and if the minerals were sourced from the conflict region.

The first filing deadline is May 31, 2014, and reporting covers Jan. 1-Dec. 31, 2013. For companies not on a calendar fiscal year, the filing period includes the first full fiscal year following the release of the final rule in August 2012.

## Broader Impact

The SEC, based on comments it received before issuing the final rule, estimated that while fewer than 6,000 companies will be directly impacted by the filing rule, about 278,000 may be indirectly affected due to supply chain relationships. This includes distributors who supply components to public manufacturers.

“Though legally it doesn’t apply to them, practically it does apply to them because they’re the ones who have to do the legwork for customers who have to file the reports,” says Ed Orlet, vice president of government affairs for the National Association of Electrical Distributors.

Many are already being asked if the products they sell contain any conflict minerals. “We probably get a dozen letters a week from various customers wanting to know if the products

we’re selling them contain conflict minerals,” says Jim Scardina, senior vice president of distributor Bearing Headquarters Company, Broadview, IL.

Scardina says Bearing Headquarters had its lawyers draft a letter for responding to the customer requests that are already rolling in. “We tell them, first, that we’re not a manufacturer, and secondly, we don’t believe that any of the manufacturers we represent are in conflict,” he says. “But we still need to go that step further and get that confirmation in writing.”

Not doing so, he says, would likely result in some customers deciding to not do business with the company. “They just don’t want to take that risk,” he says.

It’s never wise to tell customers “it’s not my problem,” Orlet says. So while distributors can’t be held liable for the actual filing, they should be preparing to respond to requests from customers.

## Creating a Game Plan

Currently, no standard exists for how to deliver the required information to customers. Some accept a broad-based letter, such as the one created at Bearing Headquarters, but most of the requests, according to Scardina, are tied to specific products.

Smaller distributors that provide a limited number of SKUs may have an easier time complying with these requests, Orlet says. But what about companies that offer tens of thousands of SKUs from hundreds of suppliers?

And what qualifies as due diligence? The SEC has advised that it views the “supplier engagement” element of the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas, which instructs suppliers to actively engage with their supply chain partners to assure accurate information, to be reasonable. But how do you make sure you’re talking to the right people?

“I’m very involved in supply chain relationships here, and I have direct contacts for our top 200 suppliers,” Scardina says. “But when I get down to, say, number 500, I don’t know who to call.”

The Electronic Industry Citizenship Coalition and the Global e-Sustainability Initiative created the Conflict-Free Sourcing Initiative to help companies downstream provide covered companies with the necessary information,

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including a reporting template and other training materials. But there's still a lot of confusion about where to begin, Orlet says.

"It is complicated," says Joel Pekay, director of sales and marketing for Intertek, a global auditing, inspection, quality assurance and training solutions provider. "But it doesn't have to be that complicated." Pekay has been working on the conflict minerals requirements for three years.

"It begins with creating a game plan."

Businesses today are already complying with a number of chemical reporting and usage requirements, he says. For example, California's Proposition 65 requires all companies that do business in California to determine if the products contain any of approximately 800 chemicals and provide a "clear and reasonable" warning about those chemicals.

"In the case of conflict minerals, they're minerals but we can look at them like chemicals," Pekay says. "Rather than separating it out as a standalone policy, our recommendation is to integrate the compliance into your everyday processes."

Don't just focus on the issue as a legal or compliance concern, he advises. Instead, make sure to include people at every level of the company that may encounter the requests – from sales to purchasing to legal.

"When legal writes up a supplier contract, are they including that the supplier will meet your compliance needs for all requirements, including conflict minerals? When purchasing places an order, is it for compliant materials? When receiving receives materials, are they checking for compliance?" Pekay says. "We really need everyone to be together."

Once that consistent strategy has been established, begin assessing your products. Pekay simplifies the process into four steps.

**1. Assess the product for likelihood of conflict minerals.** "Matrices exist to help with this, and there are some products that we know there's a likelihood," he says. For example, computer systems are likely to have tantalum, tin or gold; tools may have tantalum, tin or tungsten. And many of your products may not have any of these materials at all.

**2. Contact the supplier.** For the products that have a likelihood of containing conflict minerals, reach out to the suppliers to request sourcing information. If they value the relationship, they'll be willing to work with you, Pekay says. Get solid data on the source of the materials or

why the information isn't available.

**3. Assess your risk.** "If the data says it's from a conflict-free zone, you're good. If the data is unavailable, you are at risk," he says. And if you can't get the information to provide to your customers, you have to assess the impact that will have on your customer relationship.

#### **4. Report the results.**

"As an industry, we should be trying to go beyond just a signed sheet of paper," he says. "You need to have confidence in what you're signing."

There will still be challenges, including talking to the right people, but if the process is ingrained in a company's overall strategy, more people should be aware and be able to provide an accurate and data-backed response to requests.

#### **Unintended Consequences**

There are some unintended consequences of the new requirement already being discussed.

The rule does not outlaw the use of conflict materials; it just requires reporting if these materials come from the impacted region and/or conflict mines. This may open the door for "shame propaganda" against companies who may ultimately get their materials from that region.

"It could turn into a PR nightmare if your competitor can say you have ties to child labor," Pekay says.

In addition, the instability of the region means that mines that are currently "conflict-free" may have control wrested away by militant groups in the future, according to the Electronic Industry Citizenship Coalition and the Global e-Sustainability Initiative.

As a result of these challenges, some companies may decide that sourcing from that region at all may not be worth the risk, Orlet says, a result that may actually inhibit positive development in the region that could overcome the ongoing conflict.

Because it's a new regulation, the full impact likely won't be felt for a few years, Pekay says. "But the first question we all have to ask is: Why are we doing this?" he says. "Yes this is an SEC requirement that executives and management need to meet, but there's also a corporate responsibility that we all have to keep in mind."

*To access online resources on conflict minerals, visit this article at [www.mdm.com](http://www.mdm.com).*