

Time to get started

Conflict minerals

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What are conflict minerals?

In August 2012, the SEC approved its final rule on conflict minerals. The rule, mandated by the Dodd-Frank Act, requires public companies to disclose whether they use conflict minerals (tantalum, tin, tungsten, and gold) and whether the minerals originated in the Democratic Republic of the Congo (DRC) or adjoining countries (covered countries). It addresses concerns that conflict minerals mined in covered countries help finance armed groups that are responsible for violence in those countries. The disclosures are intended to promote the strengthening of custody controls surrounding conflict minerals and thereby reduce funding for the armed groups.

Conflict minerals can be found in hundreds of products ranging from cell phones and laptop computers to jewelry, golf clubs, drill bits, and hearing aids. Due to this widespread use, an estimated 6,000 companies that are SEC issuers will have to provide new disclosures under the rule. Approximately another 275,000 private companies that are part of the issuers' supply chains are also affected. The SEC estimates compliance costs at \$3-4 billion initially and over \$200 million annually thereafter.

Companies must first comply with the disclosure requirements on May 31, 2014 for 2013 calendar year

operations. An issuer that is unable to determine whether its conflict minerals are conflict-free is allowed a temporary two-year period (four years for smaller companies) to describe its minerals as "DRC conflict undeterminable." During that temporary period, however, the issuer is still required to perform due diligence and file an unaudited Conflict Minerals Report (CMR) with additional disclosures, including steps taken to improve due diligence and mitigate the risk that its conflict minerals benefit armed groups.

This means that companies should act now to prepare for the 2014 disclosure requirements. But companies have many open questions as to what the new rules mean to them and how they can comply with the rules. This article is intended to assist companies in getting started by taking a practical approach, identifying components of a compliance program, and reviewing some considerations for success based on our observations.

Getting started

There are clearly challenges to adhering to the SEC requirements, but companies can take a proactive approach. They should consider how they will ascertain which products may be impacted by the rules, navigate the complexity of their supply chains to determine whether their products are conflict free, and leverage

other industry efforts to increase collaboration and reduce the burden of compliance.

To assist with understanding the SEC requirements, the ruling can be summarized in a decision tree with a few possible outcomes, each carrying unique challenges (*see Figure 1*).

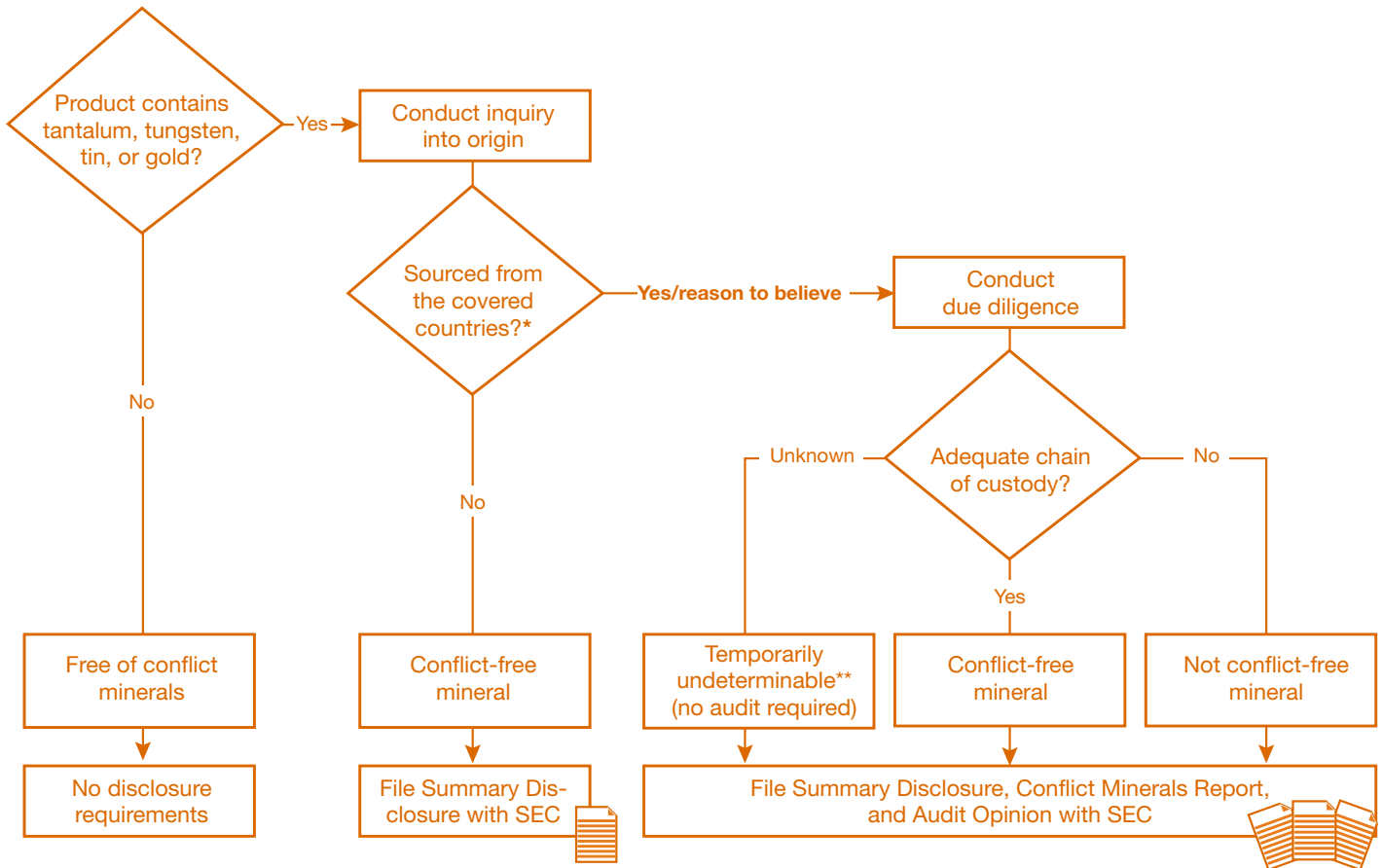
Based on the decision tree outcomes, companies can determine the next steps to ensure compliance with the SEC rules. Once a company determines that S1502 applies, stakeholders can begin to identify how the requirements will impact the company. The SEC requires companies to:

1. Examine their products to determine whether and to what extent Section 1502 applies;
2. If applicable, perform reasonable country of origin inquiry (RCOI) to determine whether minerals are sourced from covered countries; and
3. If applicable, perform due diligence and report (e.g., Form SD, CMR, independent private sector audit)

What a conflict minerals program looks like

Given the complexity of the new rules, many companies are not sure where to start or how to break down the rules into actionable items. The best approach is to view the rules as three main tasks. First, determine product

Figure 1. Conflict minerals decision tree



* Covered countries are the Democratic Republic of the Congo, Angola, Burundi, Central African Republic, the Republic of the Congo, Rwanda, South Sudan, Tanzania, Uganda, and Zambia.

** Companies would reach this conclusion if they cannot determine whether their conflict minerals benefited armed groups. But this option is only available for the first two years.

and supplier scope. Next, understand the source of minerals and chain of custody. Finally, report on conflict mineral status. A practical approach, as illustrated in the following figure, that is well planned out and easy to comprehend, can help companies navigate the ruling (*see Figure 2*).

A successful conflict minerals program consists of various moving parts. By referring to the program overview in Figure 2, companies can begin to identify any gaps in their programs. Once companies determine where they are within the program, they can carefully plan an approach to address the breadth of Dodd-Frank Section 1502 requirements.

Considerations for a successful conflict minerals program

For many companies, compliance will be the sole objective; others may want to capitalize on the opportunity to drive value in the supply chain. Based on our experience, the following are some considerations that contribute to a successful program.

Take a broader view by focusing on your customers, and determine how compliance may add value

- Market expectations will change, and stakeholders may ultimately compare companies' information. Those stakeholders will influence the market importance of conflict status, and companies that get ahead of the rules and move quickly to become "conflict-free" may enjoy competitive advantage.

- While companies may not agree with or approve of this rule, they may be able to drive value from their compliance efforts. New sourcing initiatives could contribute to improved corporate alignment or ethical sourcing; sustainable supply chain efforts could lead to reputational advantages.

Develop your philosophy; set goal posts

- Establishing a comprehensive conflict minerals compliance philosophy from the initiative's onset will provide a guiding light for your compliance program and a basis for your conflict minerals policy. Development of the company's policy statement is critical, as it becomes the basis for internal and external stakeholder expectations and setting of responsibilities. Where the philosophy becomes the guidance, the policy becomes the implementation roadmap.

Take a phased approach: Start sooner than later and take advantage of the transition period

- Develop and sequence your implementation roadmap logically and realistically based on available resources. Following a practical and phased method while leveraging any one of several risk-based approaches will be important. While meeting annual requirements, a multi-year approach that leverages evolving industry and regional developments can help the company progress.

Dedicate resources to successful program execution

- Conflict minerals compliance requires a coordinated effort among various functions across the company. Effective orchestration by the program manager will maximize each function's contribution so that skills, experiences, and knowledge are leveraged but invested time is minimized.
- Selection of the company's executive officer who will sign the Form SD is an important activity as he or she will set the tone for this initiative's success; they usually become the executive sponsor.

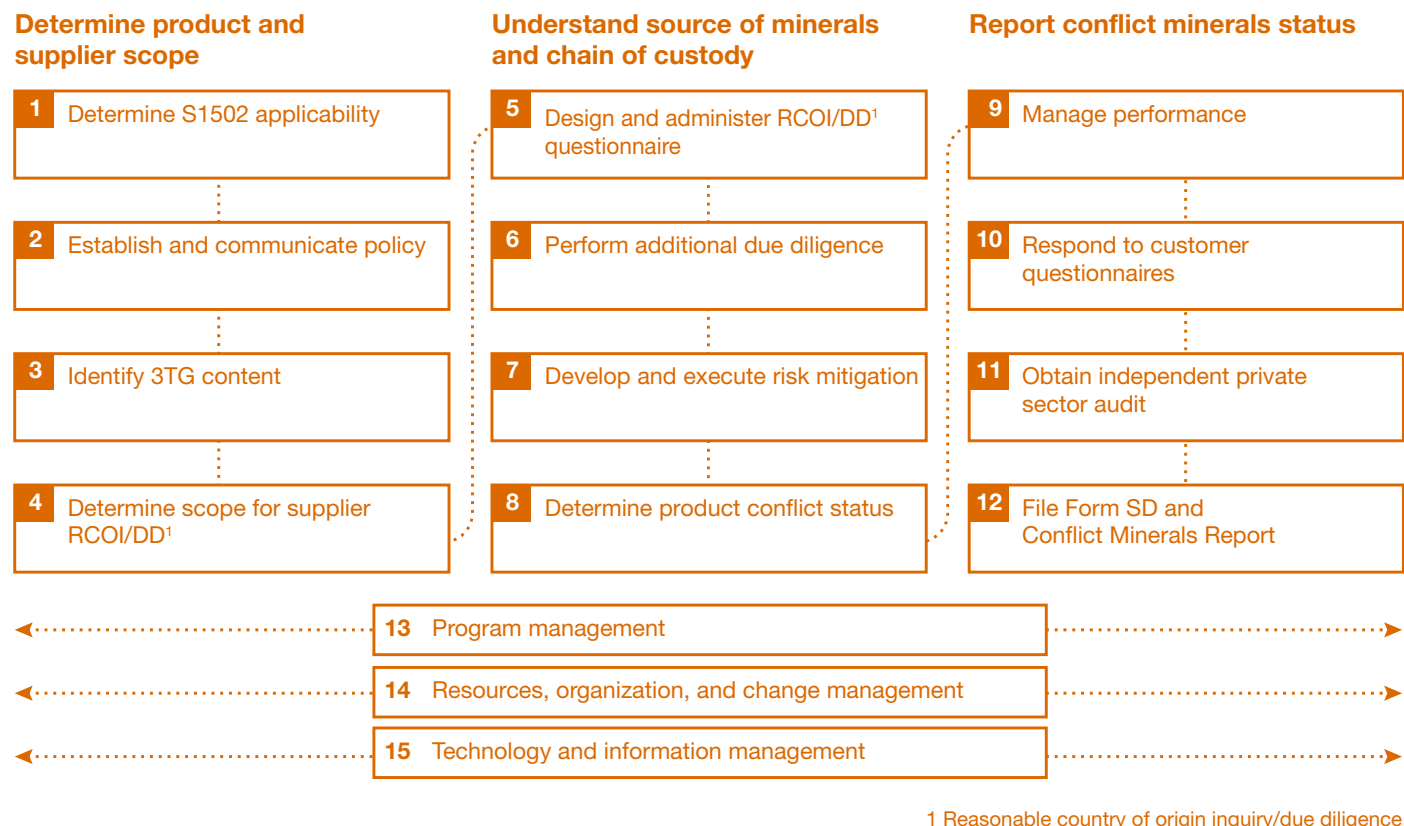
Leverage other efforts where applicable

- Leverage existing compliance or supply chain visibility-enhancing initiatives (REACH, RoHS, COI, etc.), as many program requirements are similar. Your goal should be to have one established backbone architecture where additional requirements may attach; new legislative requirements should not always necessitate a new program.

Focus on supplier engagement early and often throughout the program

- By engaging with your suppliers early, even those who may not be contacted for further due diligence, you are communicating your company's compliance intentions well in advance of any formal or informal requests for information.

Figure 2. PwC's framework for S1502 compliance, based on OECD guidance & SEC requirements



- The actions of the external supplier population will dictate how successful your initiative will be. You will not be able to reach compliance without adequate supplier engagement.
- Communicate your expectations—for both sourcing and cooperation in the process.

Use technology to support the process

- Leverage and incorporate existing internal technologies for all aspects of your program implementation, not just survey management. Governance, risk and compliance (GRC), workflow, and supply chain management (SCM) tools help facilitate product analysis, risk mitigation, and supplier management—all critical aspects of conflict minerals due diligence.

Engage your auditor early

- Select your CMR auditor early and engage them in the evaluation of your processes while they are still being developed.

Leverage internal audit

- The internal audit function has broad visibility into existing risk tolerance and control plans across the organization. Seek their counsel when developing the due diligence approach to help identify process risk, standardize key responses, and implement business controls.

Document as you go

- Document your key decisions, processes, and outcomes, beginning from the start of your compliance program. This includes not only supplier surveys, but also decisions like product/supplier scope, and other key judgment calls around interpreting the rule.

Monitor the issue

- Existing conflict minerals guidance is evolving due to legal challenges and scoping interpretations. Stay current to ensure due diligence activities are correctly focused on in-scope products. Leverage industry associations and external advisors for assistance in validating items in the ‘grey space.’

Use risk assessment to channel your resources and create a multi-year plan

- Prioritizing your supplier base initially allows you to understand which suppliers are most important to your compliance efforts. Many other risk factors such as supplier

performance metrics and ‘red flags’ help you assess the quality of supplier responses and align resources to manage critical relationships. Use risk assessment as a continuous process that evolves over time—it is not a discrete activity.

Establish sponsorship and supporting team

- Build the team—involve legal/compliance, sustainability, internal audit, finance, IT, supply chain, and engineering. Be clear on who is accountable (start with identifying who will be signing the Form SD) and identify day-to-day project managers.

Start at the end

- Envision—even draft a preliminary version of – your first Form SD/CMR. This will help you formulate your comprehensive data collection plan, data management strategy, internal validation process, and stakeholder communications.

A slow start may leave you behind

Preparation activities to-date vary by company and sector. Some companies are still in the early stages and have not taken action beyond general research, while other companies have already completed pilot programs of their supply chain due diligence.

Regardless of where a company is in the process, it is clear the activities required to achieve compliance take time. There are multiple aspects of a successful conflict minerals program, as outlined above. For companies that have not initiated action, focusing on these five items is the best way to get started.

- Build the team
- Create a plan where people are accountable
- Identify applicable products and suppliers
- Consider drafting a Form SD / CMR to understand your end goal
- Document decisions as the company moves through the required steps

It's impossible to gauge the scope, time, and cost of the activities until you get started. Delaying compliance preparations may leave companies without adequate time to meet the May 2014 deadline.

Companies should begin now, taking a proactive, practical approach to move their compliance efforts forward.

***To have a deeper conversation about
how this subject may affect your business,
please contact:***

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