Impact On
Disclosures Related to Use of “Conflict Minerals”

April 2011

Introduction

While the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank, or “the Act”) is predominantly focused on financial regulatory reform, it also includes a number of corporate governance and disclosure requirements that are designed to achieve other public policy objectives. Among these is Section 1502, which requires new procedures and disclosures by all issuers (domestic and foreign) who use so-called “conflict minerals” in their products or manufacturing processes. Section 1502 defines conflict minerals as cassiterite (a primary tin ore), columbite-tantalite (a.k.a. coltan, the mineral from which tantalum is extracted), gold, wolframite (a tungsten ore), and any other minerals determined by the Secretary of State to be financing conflict in the Democratic Republic of the Congo and its adjoining countries (collectively, “DRC countries”). These minerals are used in the production of numerous products across many industries, including technology, telecommunications, aerospace, automotive, electronics, industrial products, and jewelry manufacturing.

The Act intends to shine a light, via public disclosures, on companies that use minerals from DRC countries in their products, with the hope that such increased transparency will encourage sourcing decisions that prevent the funding of rebel groups associated with conflicts and extreme violence in that region.
**What will companies need to do?**

The significant challenge for companies who use these minerals, given the current lack of transparency into the metals supply chain, will be demonstrating that their minerals are not sourced from DRC countries—or, if they are sourced from DRC countries, demonstrating an adequate chain of custody out of the region. The sheer number of intermediaries and the degree of intermingling of these minerals along the supply chain adds considerable complexity. Companies will need to:

- Examine the products they manufacture (or contract to manufacture) to create an inventory of products for which the minerals are “necessary to the functionality or production of those products”;
- Examine their procurement processes and supply chain information and communicate with suppliers to understand the extent of sourcing and the chain of custody data for their minerals;
- Develop due diligence policies, procedures, and documentation surrounding the source and the chain of custody of the minerals used;
- Engage an independent private-sector firm to audit the due diligence procedures and findings included in the Conflict Minerals Report (if required to prepare and furnish such a report); and
- Use the information sourced from these processes to comply with the disclosures required by the Act (described in more detail below).

**New disclosure requirements will impact a large population of companies**

On December 15, 2010, the Securities and Exchange Commission (SEC) proposed rules to implement Section 1502. The proposed rules would require companies to:

1. Disclose annually whether they use conflict minerals that are “necessary to the functionality or production” of a product they manufacture, or contract to be manufactured on their behalf;
2. Disclose whether or not any of their conflict minerals originate from a DRC country, and the methods used to make such a determination; and
3. Furnish an audited Conflict Minerals Report as an exhibit to their annual report filed with the SEC, if they determine their conflict minerals originate from a DRC country or if they are unable to determine the origin of such minerals.

Initial disclosures and, if necessary, an audited Conflict Minerals Report will be required after the first full fiscal year following promulgation of final SEC rules (see “Timing,” below).

---

1 75 FR 80948 (Dec. 23, 2010). Section 1502 of the Act amends the Securities Exchange Act of 1934 ("Exchange Act") by adding Section 13(p). Section 13(p) sets forth the defined terms and reporting requirements related to conflict minerals, discussed *infra*. 

www.pwcregulatory.com
The SEC has estimated that the proposed rules will impact approximately 6,000 issuers, regardless of company size or the extent of use of conflict minerals. Companies will need to develop policies, procedures, applicable controls, and documentation in order to comply with the new disclosure requirements. It can take months, or in some case years, from the time minerals are mined to the point that they end up in a finished product. Verification of sourcing may need to begin in early 2011 to facilitate reporting for 2012 annual periods.

Companies that are unable to determine whether any of their conflict minerals originate from the DRC countries would nonetheless need to identify those products as “not DRC conflict free” in their Conflict Minerals Report. Potentially affected companies should begin to strategically plan now by examining their procurement processes. Companies may wish to conduct early feasibility studies to determine whether supply chain information is available, including possible smelter, refiner, or supplier certifications and declarations.

Given the current state of mineral supply chain transparency and custody information, many companies may be unable to determine the origin of their minerals and will be required under the proposed rules to disclose that such minerals are "not DRC Conflict Free". This may result in the unintended consequence of creating a de facto deterrent toward all material sourced from the region, potentially harming the business of valid suppliers who exercise strong custody controls as well as the livelihood of native employees and artisanal miners.

**Timing**

In April, the SEC announced that the issuance of final rules will be deferred to the August to December 2011 timeframe, a delay from the original April 15, 2011 deadline mandated by Dodd-Frank. The rules as proposed would require a December 31 year-end issuer to first provide the required disclosures (and audited report if necessary) in its annual report on Form 10-K (or Form 20-F for a foreign private issuer, or Form 40-F for an eligible Canadian issuer) ("annual report") for the year ended December 31, 2012.

The SEC requested comment on sixty-nine different issues, and the comment period closed on March 2, 2011.

The SEC has acknowledged they have limited expertise in the area of conflict minerals, supply chain risk and transparency which is reflected in the number of topics requested for specific comment in the proposal. Several issuers have highlighted their perceived difficulties in meeting the proposed reporting timeline. It is unclear whether the delay in issuance of final rules will impact the timing of first reporting.

**Summary of the SEC proposal**

**What are conflict minerals and where are they typically used?**

Conflict minerals are defined as cassiterite, columbite-tantalite, gold, wolframite, or their derivatives; or any mineral or its derivatives determined by the Secretary of State to be financing conflict in a DRC country.
Cassiterite is the metal ore that is most commonly used to produce tin, which is used in alloys, tin plating, and solders for joining pipes and electronic circuits.

Columbite-tantalite is the metal ore from which tantalum (also known as coltan) is extracted. Tantalum is used in electronic components, including mobile telephones, computers, videogame consoles, and digital cameras, and as an alloy for making carbide tools and jet engines components.

Gold is used for making jewelry and, due to its superior electric conductivity and corrosion resistance, is also used in electronic, communications, and aerospace equipment.

Wolframite is the metal ore used to produce tungsten, which is used for metal wires, electrodes, and contacts in lighting, electronic, electrical, heating, and welding applications.

These minerals are essential to a wide range of products, and thus the SEC anticipates that the rules will apply to a significant number of companies across multiple industries. The mining industry is clearly at the forefront in terms of impact. The DRC countries are extremely rich in natural resources and are the source of approximately 80 percent of known coltan reserves. Accordingly, technology companies are expected to be significantly impacted due to their use of coltan and the likelihood that those coltan supplies originated in the DRC countries (which would trigger the requirement to furnish an audited Conflict Minerals Report—see Step 3 below). Automotive and many other manufacturers will be similarly impacted.

Determining whether a company is subject to conflict minerals provisions, and level of disclosure

In its proposal, the SEC framed the disclosure requirements in a three-step process:

**Step 1: Determining whether the issuer is subject to Section 1502**

The proposed rules would apply to any issuer that:

- Files reports with the SEC under the Exchange Act; and
- Is one for whom conflict minerals are “necessary to the functionality or production of a product manufactured by such person.”

The provision applies both to issuers that directly manufacture products and to issuers that contract for the manufacturing of their products. Mining entities are considered manufacturers within this definition. An issuer may be considered “contracting to manufacture” a product if:

- It has any influence regarding the manufacturing of those products.
It sells generic products under its own brand name, or a separate brand name, regardless of whether it has any influence over the manufacturing specifications of those products, as long as it has contracted with another party to have the product manufactured specifically for itself.

The proposed rules would not apply to a retail industry issuer that sells only the products of third parties if the retailer has no contract or involvement regarding the manufacturing of those products and the products were not manufactured specifically for the retailer.

The SEC did not propose to define “necessary to the functionality or production of a product.” However, it noted that if a mineral is considered necessary, the product is subject to the disclosure provisions regardless of the amount of the mineral involved. It is also important to note that the SEC intended to scope in products if the conflict mineral is intentionally included in a product’s production process and is necessary to that process, even if that conflict mineral is not ultimately found anywhere in the final product. This indicates that the intention was to be very comprehensive, and that detailed, scientific analysis may be necessary in the case of certain products or production processes.

**Step 2: Determining whether conflict minerals originated in DRC countries, and resulting disclosure**

Under the proposed rules, an issuer would be required to disclose in its annual report whether its conflict minerals originated in a DRC country. This disclosure would be based on a reasonable country of origin inquiry.

If, after a reasonable country of origin inquiry, the issuer concludes that its conflict minerals did not originate in the DRC countries (and were thus “DRC conflict free”), the issuer would disclose this determination in its annual report, along with the reasonable country of origin inquiry it undertook to make the determination. The issuer would also be required to:

- Make the disclosure regarding this determination available on its website;
- Provide the Internet address of that site in its annual report; and
- Maintain reviewable business records to support its determination that its conflict minerals did not originate in the DRC countries.

The SEC did not set forth what constitutes a reasonable country of origin inquiry. However, its proposal did note that the steps necessary to constitute a reasonable country of origin inquiry will depend on the available infrastructure at a given point in time. This implies that the reasonable standard may evolve over time as supply chain processes and reporting around conflict minerals continue to develop. The SEC stated that it did not believe there is any single manner for issuers to conduct this inquiry. However, it stated that “we would view an issuer as satisfying the reasonable country of origin inquiry standard . . . if it received reasonably reliable representations from the facility at which its conflict minerals were processed that those conflict minerals did or did not originate in the DRC countries.”

---

2 “DRC conflict free” is defined in Exchange Act Sections 13(p)(1)(A)(ii) and 13(p)(1)(D) as products that do not contain minerals that “directly or indirectly finance or benefit armed groups” in the DRC countries.
The SEC noted that a “reasonableness standard” is not the same as an “absolute standard.” The staff’s stated expectation is that issuers “would have to conduct a thorough investigation” to meet the standard and that this burden could be “significant.” Depending on the ultimate end-product, the supply chain for these minerals may be lengthy and involve multiple parties along the chain of custody. It may be challenging for some companies to satisfy even a “reasonable” inquiry standard. Companies may wish to conduct early feasibility studies to determine whether such supply chain information—including possible smelter, refiner, or supplier certifications and declarations—is available.

If an issuer concludes that its conflict minerals did originate in the DRC countries, or is unable to conclude that its conflict minerals did not originate in the DRC countries, the issuer would make this disclosure in its annual report and disclose that the audited Conflict Minerals Report is furnished as an exhibit to its annual report (see Step 3, below).

**Step 3: Conflict minerals report’s content and supply chain due diligence**

Any issuer that determines its conflict minerals originated in the DRC countries, or that is unable to determine the origin of its conflict minerals, would be required to exercise due diligence on the source and chain of custody of its conflict minerals and prepare a Conflict Minerals Report.

The Conflict Minerals Report would include:

- A description of the measures taken by the issuer to exercise due diligence on the source and chain of custody of its conflict minerals;
- A certified independent private-sector audit of the Conflict Minerals Report that identifies the auditor and is furnished as part of the Conflict Minerals Report;
- A description of the products manufactured or contracted to be manufactured containing conflict minerals that are not DRC conflict free, as defined in the rules;
- A description of facilities used to process those conflict minerals;
- The country of origin of those conflict minerals;
- Efforts to determine the mine or location of origin with greatest possible specificity; and
- If applicable, a description of any of the issuer’s products that contain conflict minerals that the issuer has been unable to determine did not directly or indirectly finance or benefit armed groups in the DRC countries, and thus identify those products as not DRC conflict free.

The proposed rule provides only a high-level outline of the required content and form of the Conflict Minerals Report. The proposal states that the descriptions listed above should be based on facts and circumstances so that the description sufficiently identifies the products or categories of products, suggesting a degree of flexibility. For example, an issuer may disclose each model of a product, each category of a product, specific products that were produced during a specific time period, etc.

---

3 “Certified” means that the issuer certifies that it obtained such an audit. The SEC is not proposing that anyone sign the certification, but has asked for comments on this point.
**Supply chain due diligence**

The proposed rules would require issuers to exercise due diligence on the source and chain of custody of their conflict minerals and to disclose the due diligence they used in making their determinations, such as whether they used any nationally or internationally recognized standards or guidance for due diligence.

**Due diligence standards:** The SEC proposals do not dictate the standard for, or otherwise provide guidance concerning, due diligence that issuers must use in making their supply chain determinations. However, the SEC expressed an expectation that “most affected issuers will contribute to and rely on an industry wide due diligence process as part of their overall compliance.”

The proposed rule references the Organisation for Economic Cooperation and Development’s OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas (“OECD standard”), published in 2010. The OECD standard uses a five-step framework for risk-based due diligence programs and also provides a model responsible supply chain policy for minerals from conflict-affected and high-risk areas. This standard may provide a good starting point for companies looking to create new supply chain monitoring programs or supplement existing ones.

**Independent audit requirement:** The proposed rule states that the independent private-sector audit would constitute a critical component of due diligence in establishing the source and chain of custody of conflict minerals. The audit should be conducted in accordance with the standards established by the Comptroller General of the United States. Staff of the Government Accountability Office (GAO) advised that they preliminarily believe no new standards need to be promulgated, and that certain auditing standards that are currently part of the Government Auditing Standards will be applicable, such as the standards for attestation engagements or the standards for performance audits (see GAO-07-731G). The GAO staff has not indicated the type of evaluation criteria required for an attestation engagement, if any.

The OECD standard references International Organization for Standardization ISO 19011: 2002, *Guidelines for Quality and/or Environmental Management Systems Auditing*. ISO-certified firms with appropriate expertise may be able to perform the independent audit, in addition to accounting firms registered with the Public Company Accounting Oversight Board (PCAOB).

Regardless of the type of independent firm engaged, issuers will need to establish policies, procedures, and applicable controls over their conflict minerals due diligence process in order to form the basis for an assertion that can be audited. The extent and level of detail for these policies and procedures will vary greatly among issuers depending on their use of conflict minerals and the nature of their supply chains. Issuers will need to strategically plan to provide adequate time to develop, document, and assess policies in advance of the first conflict minerals period subject to reporting.

**Disclosure of Conflict Minerals Report**

Under the proposed rules, an issuer’s Conflict Minerals Report, including the independent private-sector audit report, would be furnished as an exhibit to its annual report, rather

---

than filed with the SEC, and thus would not be subject to liability under Section 18 of the Exchange Act, unless the issuer explicitly states that the Conflict Minerals Report is filed under the Exchange Act. These documents would be treated in the same manner as other disclosures furnished to the SEC. In addition, the issuer would:

- Make the Conflict Minerals Report available on its website;
- Disclose in its annual report that the Conflict Minerals Report is posted on its website; and
- Provide the Internet address of that site in its annual report.

Issuers would be required to provide their initial conflict minerals disclosure—and, if necessary, their initial Conflict Minerals Report—after their first full fiscal year following the promulgation of final rules.

**Recycled or scrap sources**

If an issuer obtains conflict minerals from a recycled or a scrap source, the issuer would be required to disclose in its annual report and in its Conflict Minerals Report that its conflict minerals were obtained from recycled or scrap sources and that they are considered “DRC conflict free.” In addition, the issuer would describe the measures taken to exercise due diligence in determining that its conflict minerals came from recycled or scrap sources. An issuer would not need to provide in its Conflict Minerals Report a description of the recycled or scrap conflict minerals’ processing facilities or country of origin, nor would it be required to describe its efforts to determine the mine or location of origin with greatest possible specificity. The Conflict Minerals Report would be subject to the independent private-sector audit requirement.

**PwC’s decision tree assists in complying with the new regulation**

- **Do you file reports with the SEC under s13(a) or s15(d) of the Exchange Act?**
  - No → No s13(g)2 reporting obligation
  - Yes → **Do you manufacture or contract to manufacture products?**
    - No → **Are minerals that could have been sourced from conflict areas necessary to the functionality of the product?**
      - No → No s13(g)2 reporting obligation
      - Yes → **Conduct a 'reasonable country of origin' inquiry**
        - **Based on inquiry, did conflict minerals originate in DRC countries?**
          - No → Disclose determination and country of origin inquiry process company undertook in company’s annual report, make disclosure available on company’s website, and maintain reviewable business records to support its determination
          - Yes → **Have you exercised due diligence on source and chain of custody of conflict minerals and prepared a Conflict Minerals Report?**
            - **Based on inquiry, did conflict minerals originate in DRC countries?**
              - Yes → Disclose findings to include due diligence used and a description of products that are ‘NOT DRC Conflict Free’ in annual report and furnish, as exhibit, Conflict Minerals Report with certified independent private sector audit report
              - No → **Conduct due diligence of supply chain, prepare Conflict Minerals Report and obtain certified independent private sector audit**
            - **Unsure** → Disclose determination and country of origin inquiry process company undertook in company’s annual report, make disclosure available on company’s website, and maintain reviewable business records to support its determination
  - Yes → Disclose findings to include due diligence used and a description of products that are ‘NOT DRC Conflict Free’ in annual report and furnish, as exhibit, Conflict Minerals Report with certified independent private sector audit report

- Post the Conflict Minerals Report on the company’s website and disclose that report is posted on website.
While Dodd-Frank will have an impact on all companies that use these types of minerals, many implementation issues are currently unclear and the SEC will need to fully digest comments received from constituents before promulgating final rules. PwC will continue to monitor developments and provide you with updates, which will be available at www.pwcregulatory.com.

**Additional information**

If you would like additional information about the matters discussed in this *A Closer Look*, please contact:

- Raymond Beier  
  Dodd-Frank Industries Leader  
  646 471 2634  
  raymond.beier@us.pwc.com  
  Laura Laybourn  
  Director, Corporate Intelligence  
  703 918 1430  
  laura.m.laybourn@us.pwc.com  
  Teresa Fabian  
  Sustainable Business Solutions – UK  
  teresa.fabian@uk.pwc.com

- Doug Dean  
  Sustainable Business Solutions – Industrial Products Leader  
  412 355 8095  
  douglas.k.dean@us.pwc.com  
  Kathy Nieland  
  Sustainable Business Solutions Leader – US  
  504 558 8228  
  kathy.nieland@us.pwc.com  
  Michael Werner  
  Sustainable Business Solutions – Germany  
  michael.werner@de.pwc.com

- Sara DeSmith  
  Partner, Transaction Services  
  973 236 4084  
  sara.desmith@us.pwc.com  
  Glenn Ware  
  Managing Director, Corporate Intelligence  
  703 918 1555  
  glenn.ware@us.pwc.com  
  Scott Williams  
  Sustainable Business Solutions – Japan  
  scott.s.williams@jp.pwc.com

If you would like additional information on other aspects of Dodd-Frank or about PwC’s Financial Services Regulatory Practice, please contact:

- Dan Ryan  
  FS Regulatory Practice Chairman  
  646 471 8488  
  daniel.ryan@us.pwc.com  
  Gary Meltzer  
  FS Regulatory Practice Managing Partner  
  646 471 8763  
  gary.c.meltzer@us.pwc.com  
  John Garvey  
  FS Advisory Practice Leader  
  646 471 2422  
  john.garvey@us.pwc.com