SUTHERLAND

First Steps Toward Building a Conflict Minerals Compliance Program

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On Aug. 22, 2012, the U.S. Securities and Exchange Commission (SEC) adopted rules that are likely to impact the operations of thousands of companies whose securities are traded in the United States. The rules, widely referred to as the "Conflict Minerals Rules," apply to any company that files reports with the SEC under Sections 13(a) or 15(d) of the Securities Exchange Act of 1934, and manufactures, or contracts to manufacture, a product containing tin, tungsten, tantalum or gold (the so-called "Conflict Minerals"). If any of these minerals are necessary to the functionality or production of a product manufactured or contracted to be manufactured by the company, then the company must submit a new disclosure form (Form SD, a/k/a the "Specialized Disclosure Report") to the SEC on an annual basis.

The first Forms SD must be filed with the SEC no later than May 31, 2014, covering a company's use of Conflict Minerals during calendar year 2013.

First year compliance costs for companies covered by the Conflict Minerals Rules are estimated by the SEC to be as high as $4 billion. In view of these costs and for other reasons, it is incumbent upon companies to be as efficient as possible when designing their response to the rules. To assist companies with this process, this article discusses some of the initial steps a company should take to prepare for filing its first Form SD.

Tone at the Top

First, a company must secure "buy in" from the highest levels of the organization, i.e., the chief executive officer; the chief operating, financial and legal officers; and the board of directors. To achieve this buy in, companies are advised to develop strong internal education programs built around some of the most important elements of the rules. Senior management should understand the effective dates of the rules, be educated about specific company products that contain Conflict Minerals, and discuss budgets for compliance with the rules. Because the rules provide a private right of action to persons alleging harm, it is imperative that senior management also understand the potential liability a company faces if it is proved to have violated the rules. This education process should result in a "tone at the top" message that the company intends to use its best efforts to comply with the rules.

External Communication

The second step is closely related to the first: companies need to develop a clear external communication plan. The development of an external communication plan serves multiple purposes. In addition to crystalizing a company's position with respect to the rules much like a mission statement, a communication plan also can act as a catalyst for developing in-house compliance programs. External communications also are vital because compliance with the SEC's rules requires the cooperation of multiple third parties, specifically the vendors and suppliers who provide the company with Conflict Minerals, or products containing them.

In fact, rules compliance cannot be achieved without vendor cooperation. Compliance depends upon each supplier in the chain of custody being clear about the source of its Conflict Minerals. It is also worth observing that the rules have been closely reported on by certain industries, as well as humanitarian and other groups. Accordingly, it should be expected that at least some consumers will make purchasing choices based on their perceptions of a company's compliance with the rules, and these perceptions may

be shaped for good or for ill by the company's public statements. The Conflict Minerals Rules themselves require disclosure of certain information on the company's public web site, and the reports filed by the company with the SEC must provide links to that site.

Timing

Third, a company needs to develop an action plan – now. There may be some SEC regulations that can be complied with by asking the company's General Counsel to just "do it." These are not those rules. The Conflict Minerals Rules are exceedingly complex; they require companies to undertake a top to bottom review of all of the company's products that *may* contain a Conflict Mineral. Where did the minerals originally come from? Can the company identify the mine they were supplied from and the refiners that processed them? Can the company certify the chain of custody? These are just a few of the questions posed by the Conflict Minerals Rules. In a non-complex organization, answering these questions would take a significant effort. In a complex, multinational manufacturing company, the effort is likely to require a dedicated team that works with the company's suppliers over a long period of time, until compliance with the rules is assured.

This brings us to the last point: compliance with the rules is likely to require on-going efforts by each reporting company long after the company files its first Form SD. In response to numerous challenges from groups and individuals involved in the rulemaking process, the SEC will permit companies filing in 2014 and 2015 to equivocate a bit when making determinations regarding the source of their Conflict Minerals. If a company is unable to determine that a product does not contain Conflict Minerals, then it may file a Form SD stating that its product(s) are "DRC (Democratic Republic of the Congo) conflict undeterminable" for its first two reporting years (smaller reporting companies as defined by the rules get a break for the first four calendar years after the rules' effectiveness). After that, the company's Conflict Minerals Compliance Program must be up to the task of ensuring compliance with all aspects of the rules.

This article began by referring to a phrase commonly used to describe how a company instills a desired ethic among its employees – tone at the top. Compliance with the SEC's new Conflict Minerals Rules will require that – and much more.