WSGR ALERT

DECEMBER 2010

SEC PROPOSES RULES RELATING TO SPECIALIZED DISCLOSURE OF USE OF CONFLICT MINERALS

On December 15, 2010, the Securities and Exchange Commission (SEC) proposed rules to implement Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), which requires new disclosures by reporting issuers concerning their use of conflict minerals (generally tantalum, tin, gold, or tungsten) that originated in the Democratic Republic of the Congo or an adjoining country. The proposed rules are available at http://www.sec.gov/rules/proposed/2010/34-63547.pdf.

Section 1502 of the Dodd-Frank Act amended the Securities Exchange Act by adding a new Section 13(p), which requires the SEC to promulgate disclosure and reporting regulations regarding the use of conflict minerals from the Democratic Republic of the Congo and adjoining countries (together, the DRC Countries). According to the Dodd-Frank Act, the extreme levels of violence in the eastern Democratic Republic of the Congo financed by the exploitation and trade of conflict minerals originating in the DRC Countries led Congress to enact this provision.

Overview

The SEC's proposed rules would require any reporting issuer for which conflict minerals are necessary to the functionality or production of a product manufactured, or contracted to be manufactured, by that issuer to disclose in its annual report whether its conflict minerals originated in a DRC Country. If so, the issuer would be required to furnish a separate report as an exhibit to its annual report that includes, among other things, a description of the measures taken by the issuer to exercise due diligence on the source and chain of custody of its conflict minerals. The issuer would also be required to have an independent private sector audit of the issuer's report conducted in accordance with standards established by the Comptroller General of the United States. The report would be required to include a certification that such audit has been completed, as well as include a copy of the audit report. These reports would be made available to the public on the issuer's website.

Analysis of Whether Disclosure Is Required

The first step in analyzing whether disclosures would be required under the proposed rule is to determine whether a company is a reporting issuer that manufactures or contracts to manufacture products for which conflict minerals are necessary to such product's functionality or production.

Applicable to reporting issuers only

The SEC's proposed rules would only apply to issuers that file reports (i.e., Forms 10-Q, 10-K, and 8-K) with the SEC under Securities Exchange Act Sections 13(a) or 15(d). The proposed rules would apply to domestic companies, foreign private issuers, and smaller reporting companies.

What are conflict minerals?

The proposed rules define "conflict minerals" as the following:

- Cassiterite, a metal ore that is most commonly used to produce tin and is used in alloys, tin plating, and solders for joining pipes and electronic circuits;
- Columbite-tantalite, a metal ore from which tantalum is extracted (tantalum is used in electronic components, including mobile telephones, computers, video-game consoles, and digital cameras, and as an alloy for making carbide tools and jet engine components);
- Gold, which is used for making jewelry and is also used in electronic, communications, and aerospace equipment;
- Wolframite, a metal ore used to produce tungsten, which is used for metal wires, electrodes, and contacts in lighting, electronic, electrical, heating, and welding applications; and
- Other minerals determined by the Secretary of State to be financing conflict in the DRC Countries.

Due to the many uses of these conflict minerals, the proposed rules would likely apply to many companies and industries.

What does it mean to "contract to manufacture a product"?

An issuer would be deemed to "contract to manufacture a product" if (1) it has any influence over the manufacturing of the product or (2) it offers a generic product under

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its own brand name or a separate brand name, regardless of whether it has any influence over the manufacturing specifications of the product, provided that the issuer has contracted to have the product manufactured specifically for itself.

The proposed rules would not apply to retail issuers that sell only the products of third parties if those retail issuers have no contract or other involvement regarding the manufacturing of those products, or if those retailers do not sell those products under their brand name or a separate brand they have established and do not have those products manufactured specifically for them.

When are conflict minerals "necessary" to a product?

The proposed rules do not define "necessary to the functionality or production," but the SEC noted that if a mineral is necessary, the product would be covered under the proposed rules regardless of the amount of the mineral involved. If a 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 included anywhere in the final product, the product would be covered under the proposed rules.

If a company is not a reporting issuer that manufactures or contracts to manufacture products for which conflict minerals are necessary to such product's functionality or production, no disclosure or other action would be required pursuant to the proposed rules.

Determining Whether Conflict Minerals Originated in the DRC Countries

If conflict minerals are necessary to the functionality or production of a product manufactured by a reporting issuer, the proposed rules would require the issuer to disclose whether those conflict minerals originated in the DRC Countries. An issuer would be required to make a reasonable country-of-origin inquiry as to whether its conflict minerals originated in the DRC Countries.

If the conflict minerals did not originate in the DRC Countries, then the issuer would be required to disclose this fact in its annual report and on its website. The issuer would also be required to disclose in the annual report the reasonable country-of-origin inquiry that it undertook to determine that its conflict minerals did not originate in the DRC Countries and maintain reviewable business records to support its determination. In addition, the issuer's annual report would be required to disclose the Internet address on which the disclosure is posted and retain the information on the website at least until the issuer's subsequent annual report is filed with the SEC.

If an issuer determined through its reasonable country-of-origin inquiry that its conflict minerals originated in the DRC Countries, or if the issuer was unable to determine after a reasonable country-of-origin inquiry that its conflict minerals did not originate in the DRC Countries, then the issuer would be required to disclose this in its annual report and disclose that a Conflicts Mineral Report is furnished as an exhibit to the annual report. The issuer would also be required to make available its Conflict Minerals Report on its website, disclose in its annual report that the Conflict Minerals Report is posted online, and disclose in its annual report the Internet address at which the Conflict Minerals Report is located.

Conflict Minerals Report

The Conflict Minerals Report would be required to include the following:

- a description of the due diligence measures that the issuer undertook on the source and chain of custody of its conflict minerals or diligence measures that the issuer undertook in determining that the conflict minerals came from recycled or scrap sources, which would include a certified independent private sector audit of the Conflict Minerals Report conducted in accordance with the standards established by the Comptroller General of the United States;
- a certification by the issuer that it obtained such an independent private sector audit;
- a description of the issuer's products that are not "DRC conflict free" (those products that do NOT contain conflict minerals that directly or indirectly finance or benefit armed groups in the DRC Countries), the facilities used to process those conflict minerals, the country of origin of those conflict minerals, and the efforts to determine the mine or location of origin with the greatest possible specificity; and
- the audit report prepared by the independent private sector auditor, which would identify the entity that conducted the audit.

Proposed Effective Date

The Dodd-Frank Act requires that Section 1502 be implemented by April 2011. The proposed rules would require issuers 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 the SEC's final rules. Assuming the rules are adopted in April 2011, as required, a December 31 fiscal year-end issuer would first have to provide conflict minerals disclosure or a Conflict Minerals Report after the end of its December 31, 2012, fiscal year. An issuer with a May 31 fiscal year-end, however, would have to provide the conflict minerals disclosure or a Conflict Minerals Report in its annual report for the fiscal year that encompasses the period from June 1, 2011, through May 31, 2012.

What You Should Do Now

There are several steps companies can take now to prepare for the upcoming disclosures:

- Working with your operations team, make a preliminary assessment of whether your company manufactures or

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contracts to manufacture products that contain the conflict minerals specified above, and if so, whether the conflict minerals are "necessary to the functionality or production" of the product.

- If the results of your preliminary assessment indicate that your company uses conflict minerals that are necessary to the functionality or production of a product, conduct a preliminary assessment of the country of origin of the conflict minerals used.

- Consider commenting on the proposed rules before the January 31, 2011, deadline.

For any questions or more information on these or any related matters, please contact your regular Wilson Sonsini Goodrich & Rosati contact or any member of the firm's corporate and securities practice.

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