The SEC's Delayed Rule-Making and Implications for Corporate Conflict Minerals Reports

January 16, 2012 by Sarah A. Altschuller

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The U.S. Securities and Exchange Commission ("SEC") failed to issue a final rule on conflict minerals regulations before the end of 2011, and companies still await clear guidance on the scope of Section 1502 and the nature of the relevant reporting requirements. In an announcement regarding "upcoming activity" related to the implementation of Dodd-Frank, the SEC has now indicated that the final rule for Section 1502 will be adopted between January and June 2012. Notably, the SEC's announcement indicates that "this is an estimated timeline and may be subject to change." The final rule was originally scheduled to be issued no later than April 15, 2011.

The Conflict Minerals Report Requirement

Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act requires companies that utilize tin, tungsten, tantalum, and gold to conduct and disclose due diligence on their supply chains in order to identify whether the those minerals originated in the Democratic Republic of Congo ("DRC") or adjoining countries. If an issuer either determines that its conflict minerals originated in the DRC countries, or cannot conclude that the conflict minerals did not originate in the DRC countries, the issuer will be required to disclose this information in its annual report. The issuer must then furnish a Conflict Minerals Report ("CMR") as an exhibit to the annual report, and must disclose the Internet address at which this exhibit is available.

The CMR must describe the due diligence that the issuer conducted on the source and chain of custody of its conflict minerals. Issuers will be required to describe: products that are not "DRC conflict free"; the country of origin of those conflict minerals; the facilities used to process those minerals; and efforts taken to locate the mine or source of the minerals with the greatest possible specificity.

The Reporting Timeframe

Section 1502 requires impacted issuers to submit their first disclosures regarding their first full fiscal year which begins after the promulgation of the final rule. With a final rule now delayed again, issuers currently subject to the legislation must evaluate how to prepare for the future disclosure requirements.

Looking ahead, and based on previous experience, it is most likely that the SEC will introduce a phased approach for disclosures, whereby certain initial disclosures will be required in the first reporting year that will need to be augmented in subsequent years. Many stakeholders have urged

the SEC to adopt a phased approach in comments to the proposed regulations issued in December 2010.

Groups calling for a phased approach include the U.S. Chamber of Commerce, the National Association of Manufacturers, and the House Financial Services Committee. This could logically take the form of requiring larger issuers to fully comply in the first year following the issuance of the final rule, while giving smaller issuers the benefit of more time to comply. This approach has been used in several prior instances, including: the requirement for the inclusion of XBRL (eXtensible Business Reporting Language) data files in corporate filings; and the requirement, pursuant to Section 404 of the Sarbanes-Oxley Act, for an independent auditor's report on the effectiveness of internal controls over financial reporting (although the requirement for smaller companies was eliminated by Dodd-Frank).

If the rule is issued in the next few months, issuers with fiscal years beginning in March/April or June/July would be required to issue their first reports in early to mid-2013. Issuers may fear being required to report on due diligence efforts undertaken during a time period unguided by final regulations, but that appears unlikely based on the language of Section 1502. That said, however, issuers with fiscal years beginning soon should be prepared to hit the ground running and ideally will have identified appropriate internal groups or departments who would be charged with collecting the required information in order to facilitate full compliance.

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