Conflict Minerals: Recent Developments and Business Implications of Potentially Diverging U.S. and EU Approaches

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International Trade and Investment Alert

On April 3, 2017, the Council of the European Union approved a new regulation intended to prevent the trade in conflict minerals, which followed the approval of the European Parliament on March 16, 2017. This puts an end to the legislative procedure for the adoption of the regulation, which was developed over several years and subject to extensive debate. Although inspired at least in part by Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act – the U.S. legislation on conflict minerals – the EU regulation differs in certain key respects from the U.S. approach. The timing for the European regulation is also notable from a trans-Atlantic perspective given press reports that President Trump plans to roll back U.S. regulations in this area. Even if the Trump Administration takes such action, we expect that many companies will continue to adhere to accepted standards of supply chain due diligence even if not legally required to do so.

U.S. companies, in particular, will need to remain vigilant on the compliance front regardless of any potential easing of Section 1502. Sanctions, complex supply chain dynamics, and poor or corrupt governance often intersect in ways that can create legal and reputational risks for companies. A waiver of Dodd-Frank would ease only the securities-related reporting requirement; it would not amend or terminate U.S. laws and regulations that prohibit sourcing from certain sanctioned countries and restricted parties. Accordingly, incorporating strong compliance provisions into supply chain agreements is essential for businesses operating in these complex environments.

Key Features of the EU Regulation

The EU regulation will establish an EU-wide system for supply chain due diligence intended to prevent armed groups from trading in tin, tungsten, tantalum, gold, and their ores. Beginning on January 1, 2021, EU importers will be subject to certain mandatory obligations related to conflict minerals such as:

- setting up a management system, including incorporating their supply chain policy into contracts with suppliers and publicizing their supply chain policies;
- adopting a risk management system in which they identify and assess the risks of adverse impacts in their mineral supply chains and implement a strategy to mitigate such risks;
- carrying out independent third-party audits; and

- making the results of any third party audit available to the relevant EU Member State competent authority, and making certain supply chain due diligence information available to downstream purchasers and the public.

The EU regulation differs from Section 1502 of Dodd-Frank in certain key respects. For example, it applies to conflict minerals sourced from any country, while the U.S. provision applies only to minerals sourced from the Democratic Republic of the Congo (DRC) and nine adjacent countries. On the other hand, the EU regulation applies to a more narrowly-tailored group of businesses. It does not cover small importers, as defined by volume, or downstream purchasers. As a result, many businesses, including manufacturers of finished products that contain covered minerals, are not required to comply with the due diligence obligations. The Dodd-Frank requirements, in contrast, apply to all companies that file reports pursuant to the Securities and Exchange Act that manufacture, or contract to manufacture, products where the use of minerals is "necessary to the functionality or production" of the product.

From a sheer numbers perspective, the EU anticipates the new regulation will apply directly to between 600 and 1,000 importers and indirectly to 500 smelters and refiners, some of which are based outside of the EU. Dodd-Frank Section 1502 applies to the approximately 6,000 companies listed on U.S. exchanges.

Developments under the Trump Administration

While Europe is moving forward, the U.S. may be poised to abandon its regulatory approach to conflict minerals. Acting SEC Chairman Michael Piwowar directed his staff to reconsider the SEC's Dodd-Frank rule, noting his view that it is misguided, onerous, and ineffective. The press reports- and leaked executive order- that closely followed Dr. Piwowar's statement- indicate that President Trump may waive the requirements of Section 1502 for up to two years. While the SEC rule remains in effect and President Trump has not issued a waiver to date, the U.S. State Department, on March 27, solicited stakeholder input to "inform recommendations of how best to support responsible sourcing" of the minerals in question. It is unclear at this point how the input received by the State Department will feed into the White House process.

Even if the Trump Administration waives the Dodd-Frank requirement, many major companies will likely continue to comply with accepted standards of supply chain due diligence for conflict minerals. Some have made such significant investments in responsible sourcing that turning back the clock is no longer an option. For others, factors including customer demand signals, reputational concerns, or the trend toward responsible sourcing in the EU and among OECD nations, in particular, will incentivize continued adherence to internationally-accepted standards.

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