SEC Adopts Final Conflict Minerals Rules with Notable Changes

August 22, 2012

The SEC voted today to implement the Dodd-Frank Act's reporting requirements relating to "conflict minerals" – cassiterite, columbite-tantalite, gold, wolframite and other minerals determined by the U.S. government to be financing conflict in the Democratic Republic of Congo or adjoining countries, referred to as the "DRC countries" or "covered countries." Companies must comply with the final rules for the calendar year beginning January 1, 2013 with the first reports due May 31, 2014.

The final rules adopted today contain substantial changes from the **SEC's original proposal** in December 2010. Below is a summary of the changes highlighted at today's open meeting. We will provide a more in-depth analysis of the rules once we have fully analyzed the adopting release.

Companies subject to the rules.
As proposed, all reporting companies, including small businesses and foreign private issuers, would be required to make conflict minerals disclosures and conduct supply chain due diligence if they "manufacture or contract to manufacture" products that contain conflict minerals that are "necessary to the production or functionality of the product." The final rule release provides additional guidance on how to conduct this inquiry. Like the proposed rules, however, the final rules do not explicitly define what it means to "manufacture" a product and will impose reporting requirements on companies that "contract to manufacture" products, or those that have some actual influence over the manufacturing of a product, which could pick-up a wide swath of companies that are not manufacturers. The SEC has indicated, however, that a company will not be deemed to "contract to manufacture a product" if it merely:

- affixes its brand, marks, logo, or label to a generic product manufactured by a third party;
- services, maintains, or repairs a product manufactured by a third party; or
- specifies or negotiates contractual terms with a manufacturer that do not directly relate to the manufacturing of the product.

While this guidance may ameliorate some of the concern that the rules will apply to companies that don't consider themselves to be manufacturers, some of these companies may still fall within the rules' scope.

Separate reporting.
The final rules create a new form, Form SD, to be filed by May 31 of each calendar year. (This is consistent with a suggestion made in our **comment letter** on the proposed rules, the SEC originally called for conflict mineral disclosure in a company's Form 10-K or 20-F, which we believe would have increased the burden on companies during the already taxing year-end reporting period.)

Increased liability.
Form SD will be "filed" with the SEC rather than "furnished." Accordingly, any materially "false or misleading statement" in the form will be subject to liability under Section 18 of the Exchange Act. However, because the form is separate from a company's Form 10-K or 20-F, it will not be covered by those forms' CEO and CFO certifications, or automatically incorporated into a company's shelf registration statement.

"DRC conflict undeterminable" category.
The final rules will permit a company to classify minerals as "DRC conflict undeterminable" rather than not "conflict free" for up to two years (four years for smaller reporting companies) if it is unable to determine definitively whether minerals originated in a DRC country or financed or benefited armed groups in those

countries. This is a welcome modification from the proposed rules, which required minerals to be classified as not "conflict free" if the company was unable to determine the country of origin with certainty.

Commissioners Paredes and Gallagher dissented from today's vote, indicating their belief that the required cost/benefit analysis was inadequate, and suggesting that the SEC should have considered using its general exemptive authority to exempt smaller reporting companies from the rules. The U.S. Chamber of Commerce made a similar point in a **July 2012** letter to the SEC, hinting that the final rules might be challenged on this basis. A suit of this nature could stall implementation, as happened following judicial challenges to the SEC's rules mandating **proxy access** and **independence standards for mutual fund boards**.

For the adopting release containing the final rules **follow this link**

For the SEC's press release announcing today's rulemaking **follow this link**

For Chairman Schapiro's statement at today's open meeting **follow this link**

For Commissioner Aguilar's statement at today's open meeting **follow this link**

For Commissioner Gallagher's statement at today's open meeting **follow this link**

For Commissioner Paredes' statement at today's open meeting **follow this link**

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

Joseph A. Hall	**212 450 4565**	**joseph.hall@davispolk.com**
Michael Kaplan	**212 450 4111**	**michael.kaplan@davispolk.com**
Richard J. Sandler	**212 450 4224**	**richard.sandler@davispolk.com**
Richard D. Truesdell, Jr.	**212 450 4674**	**richard.truesdell@davispolk.com**
Janice Brunner	**212 450 4211**	**janice.brunner@davispolk.com**

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