CSRwire®
The Corporate Social Responsibility Newswire
Wednesday, April 16, 2014

Conflict Minerals:

Why SEC Compliance Should Be the Least of Your Worries

It would be shortsighted for companies to take comfort in relative obscurity. And the DC Circuit's April 14, 2014 ruling doesn't mean "game over."

By Jane C. Luxton

Clark Hill attorney **Jane C. Luxton**

If your social media circle hasn't favored you with a less than glamorous photo of your face pasted atop some ridiculous character and posted online using the faceinhole app or website, count yourself lucky. Maybe it's the crowd I hang around with, but trust me, some people find this hilarious, and it never seems to get old.

Businesses that are addressing conflict minerals issues don't have to worry that they will look silly on Facebook with their corporate logos superimposed on the body of an elf or cartoon figure, but the analogy isn't as far off as it may sound.

Nintendo Slammed on Conflict Minerals

Consider what happened when the Enough Project, an activist group whose stated mission is to "prevent, mitigate, and resolve crises of genocide and crimes against humanity," published its 2012 rankings of the largest electronics companies, rating 24 multinational companies on the actions they were taking to "contribute to the creation of a clean minerals trade in Congo." In short order, as detailed in a June 19, 2013 article in the Washington Post, another social justice group, called Walk Free, rolled out a full-fledged campaign to spotlight the lowest-ranked company on the list, deploying multimedia varieties of adverse publicity.

Timed for maximum coverage just before Nintendo's annual shareholders meeting, the campaign included a massive Nintendo-conflict-mineralsletter-writing operation, a podcast discussing conflict minerals issues, in-person protests at retail outlets, and a video game spoofing the company's iconic Mario Brothers video game. Nintendo released a statement saying: "We take our social responsibilities as a global company very seriously and expect our production partners to do the same. We ban the use of conflict minerals and also prohibit our production partners from using any conflict minerals from the Democratic Republic of Congo and adjoining countries."

But this was not enough, according to follow-up press accounts, which quoted a Walk Free spokeswoman as saying other electronics companies are "looking at conflict-free devices by end of year" or have "policies to source from conflict-free smelters," including identifying the smelters they use or publicizing their supply chain diligence verification programs.

No Company Invulnerable to Reputational Risk

When I point out this example to clients, some say they are not exposed to this degree of reputational risk because they are not as prominent as the global electronics companies or their products are not front and center on consumer and shareholder activist radar screens.

But it would be short-sighted to take comfort in relative obscurity: The Enough Project's 2012 rankings page noted the group's intention to move on to rank industry sectors beyond electronics, such as automotive, jewelry, mining, industrial machinery, and retail; further, the site urges consumers as a general practice to "send messages to companies you purchase from, reminding them how important conflict-free from Congo is to you."

The Competitive Advantage—and a New Court Ruling

On the other side of the coin, companies at the top of the rankings have found this distinction a powerful competitive

continued on page 2

continued from page 1

advantage, as downstream customers that may be very sensitive to consumer pressure seek assurances that their upstream supply chain is conflict-free.

The April 14, 2014 decision by the US Court of Appeals for the DC Circuit, invalidating the portions of the SEC's final rule that required issuers to report their products to the SEC and on their websites as "DRC conflict free" or not, only delays the inevitable: competitively useful information that will soon be widely available in the form of government reports.

The court upheld all other parts of the rule, including the SEC's decision against allowing a de minimis exemption. The SEC should have little difficulty in revising the rule to follow the court's direction to more "narrowly tailor" the reporting obligation. In fact, the court broadly hinted that requiring issuers to "use their own language to describe [the conflict minerals status of] their own products" would pass muster.

Or, the court, suggested, the SEC could compile "its own list of products that it believes are affiliated with the Congo war, based on information that the issuers submit to the Commission."

It is doubtful the SEC will want to get into the game of compiling lists of suspect products, but it's a good bet that a new rule will soon require reporting companies to reveal their products' conflict minerals particulars, and pressure from competitors, customers, and watchdogs, eagerly reviewing these reports, will do the rest.

The situation, however, is anything but "game over."

EU Conflict Minerals Legislation

And the SEC's conflict minerals regime is, of course, not the only presence on the field. The EU has proposed its own conflict minerals legislation, which is both narrower and broader than the US version. As proposed, the EU law would be voluntary and apply only to direct importers of tin, tantalum, tungsten or gold (the "3TGs").

At the same time, its geographic reach extends well outside the nine Central African countries covered by the final SEC rule to "conflict-affected and high risk areas" worldwide, an open-ended approach rife with implementation uncertainties. Activists have criticized the proposal's voluntary nature, but as a contributor to The Guardian suggests, public procurement contracts requiring conflict-free materials, brand vulnerability risks, customer and investor demand, and similar business pressures will drive companies to adopt transparency standards on conflict minerals usage, even without a mandatory reporting obligation.

US States and Cities Passing Conflict Minerals Laws

US states and cities are also getting into the action.

California SB 861, for example, passed in 2011, bars state officials from awarding procurement contracts to companies that have failed to comply with the SEC's conflict minerals rule. Maryland has adopted similar legislation, and Massachusetts is considering a comparable proposal. Two cities – Pittsburgh and St. Petersburg – have passed resolutions urging companies to remove conflict minerals from their supply chains and favoring conflict-free materials in procurement decisions.

And perhaps in a sign of things to come, at least one state is pushing the supply chain diligence approach even further, creating additional anxiety for companies that are vigilant about protecting their brands. US companies that do business in California, a term that is broadly defined, have been subject since January 1, 2012, to the California Transparency in Supply Chains Act (SB-657). This law requires businesses to post on their websites the nature and scope of their corporate efforts to eliminate human trafficking, slavery, and child labor conflict-mineralsfrom their supply chains.

CSRwire, among others, is monitoring business response to this disclosure obligation – see the CSRwire Feb. 12, 2014 update on CA Supply Chain Transparency Act compliance. And, just as with conflict minerals transparency, watchdog groups are making it easy for socially conscious investors and customers to check on a particular company's performance and compare it to its competitors.

Reputational Risk Is Serious Business

While many, including the new Chair of the SEC, Mary Jo White, have questioned the wisdom of effecting foreign policy or social justice goals through enforceable securities law reporting requirements, and others challenge the view that such programs are effective in achieving anticipated objectives, it appears that conflict minerals requirements are here to stay.

But, as we approach the first SEC conflict minerals reporting deadline, and even if it slips a bit in time and specifics, it is important to place this particular driver in the proper perspective. Reputational risk is no laughing matter – just ask the apple farmers who lived through the Alar scare in the 1990s.

For any business, brand protection is the big-ticket concern. While important, SEC compliance is really only one item on a larger list of worries ahead.

Jane C. Luxton is a member of Clark Hill's Environment, Energy, and Natural Resources Practice Group based in the Washington, DC office. Jane has extensive experience in environmental regulatory, policy, and litigation matters, including federal and state environmental laws, as well as international environmental regimes. **Contact her at: jluxton@clarkhill.com or 202-572-8674.**