



# Conflict minerals

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In maintaining its social license to operate, the mining and metals sector must ensure that it has stewardship of its supply chain and that at each stage of the supply chain it fully respects human rights. There has been an increasing international focus on “conflict minerals”<sup>1</sup> emanating from illegal mining operations in the Democratic Republic of Congo (DRC) and adjoining countries in Africa, also known as “Covered Countries”. There are concerns that funds earned from the sale of minerals from some illegal mines in this region are being used by armed groups to finance regional conflicts, which have been characterized by atrocities, extreme levels of violence and an emerging humanitarian situation.

Groups such as the Organisation for Economic Co-operation and Development (OECD), the Electronics Industry Citizenship Coalition (EICC), the World Gold Council (WGC) and the Global e-Sustainability Initiative (GESI) have been working to highlight this issue and bring about change.

Two groups have now issued formal reporting regulations to combat conflict minerals, one legislated and one voluntary:

- ▶ Dodd-Frank Section 1502 and the SEC’s final rule
- ▶ Conflict-Free Gold Standard

These requirements have reporting implications for most metals producers, even if they are not producing from a conflict region, as they need to prove that they don’t come from these “Covered Countries”. The reporting requirements involve not just the assurance function, but will also have operational and financial implications in the compliance of these regulations.

## 1. Dodd-Frank Section 1502 and the SEC’s final rule

The only legislated response to date has been that of the United States Congress. The US Congress enacted legislation that requires US Securities and Exchange Commission (SEC) registrants to provide certain disclosures about the use of specified conflict minerals emanating from the Covered Countries. On 22 August 2012, the US SEC adopted a rule pursuant to Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Section 1502) that requires the implementation of the disclosure requirements of the new law.

The SEC estimates that approximately 6,000 issuers will be directly impacted by the rule and that many private companies in the supply chains of these issuers will be impacted indirectly.

The SEC expects that the costs will be substantial to both issuers and non-issuer suppliers, and estimates the initial cost of compliance to be between US\$3b and US\$4b, with annual costs thereafter of between US\$207m and US\$609m.



<sup>1</sup> Conflict minerals include cassiterite, columbitetantalite, gold, wolframite and their derivatives (limited to tin, tantalum and tungsten) and other minerals that the US Secretary of State may add in the future.

Dodd-Frank Section 1502 defines the affected countries or “Covered Countries” as follows:

- Democratic Republic of the Congo (DRC)
- Angola
- Burundi
- Central African Republic
- The Republic of the Congo
- Rwanda
- South Sudan
- Tanzania
- Uganda
- Zambia

Conflict minerals are currently defined as cassiterite, columbite-tantalite, gold, wolframite and their derivatives (limited to tin, tantalum and tungsten) and other minerals that the US Secretary of State may add in the future. According to the SEC, the Covered Countries account for 15% to 20% of the world’s supply of tantalum and smaller percentages of the other three minerals.

### Section 1502

This is applicable to all SEC “issuers” (including foreign issuers) that manufacture products where “conflict minerals are necessary

to the functionality or production” of the product, and requires companies utilizing conflict minerals in their products to disclose the source of such minerals.

The SEC does not consider an issuer that mines or contracts to mine conflict minerals to be manufacturing or contracting to manufacture those minerals unless the issuer also engages in manufacturing, whether directly or indirectly through contract, in addition to mining.

Section 1502 is a disclosure requirement only and places no ban or penalty on the use of conflict minerals. By bringing transparency to the financial interests that support the mining operations that exploit workers and are financing regional conflicts in the Covered Countries, the law is aimed at dissuading companies from continuing to do business, or sourcing minerals from suppliers who do business, with these mines.

### Effective Date

Issuers must comply with the final rule for the calendar year beginning 1 January 2013 with the first reports due 31 May 2014.

### SEC Issuer

The term “SEC issuers” refers to those companies that are required to file reports with the SEC under the Exchange Act.



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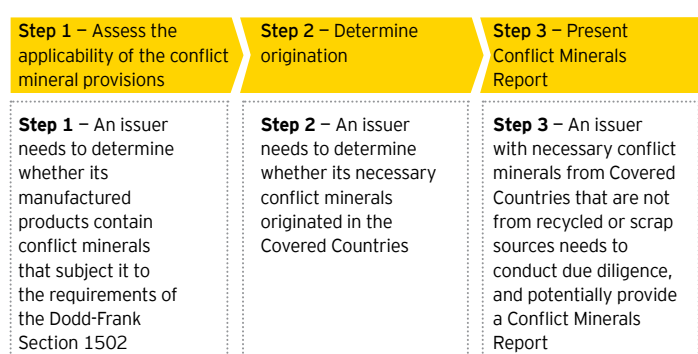
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## SEC disclosure process

The SEC final rule provides for a three-step disclosure process. The SEC has also provided a flowchart summary of the final rule to guide issuers through these steps.



At a minimum, issuers will need to undertake a thorough due diligence of each of its manufactured product and each production process. Once it is determined that the conflict minerals are utilized in the product or process, it is likely that a thorough supply chain due diligence will need to be carried out to determine the source of the minerals.

It is important to note that this legislation has wide reaching consequences – even companies that don't file with the SEC or manufacture products may need to conduct due diligence on their supply chains, if they happen to supply products that meet the criteria in Step 1 to US listed SEC registrants.

In response to this regulation, a new tag scheme is being applied by DRC authorities, with foreign help, which provides a conflict free certification that can allow mining activity to go ahead without fear of sanction. The simple “bag and tag” initiative could allow mineral exports from Congo's violent east to flow legally again. The tag certifies the tin ore is conflict-free to ensure it will not fall foul of the Dodd Frank Law<sup>1</sup>.

### Implications for mining and metals companies

In a change from the draft rule, the SEC determined that mining companies are no longer considered manufacturers (and therefore not subject to the rule's direct requirements) unless the issuer also

engages in manufacturing, whether directly or indirectly through contract, in addition to mining. However, miners will be requested by parties further down the supply chain to provide evidence of the conflict-free status of shipments. Smelters and refiners, on the other hand, are directly implicated.

**Audit considerations** – If an issuer determines that its products are conflict free (i.e., minerals may come from covered countries but they did not benefit armed groups), the company must obtain a certified independent audit of its Conflict Minerals Report and include the audit report as part of its Conflict Minerals Report.

Audits of these reports must be conducted in accordance with Government Auditing Standards (known as the “Yellow Book”) for attestation engagements or performance audits. The rule specifies that the audit's objective is to express an opinion or conclusion on whether the design of the issuer's due diligence measures conforms with the framework it used and whether the issuer's description of these measures is consistent with the process that it executed.

## 2. Conflict-Free Gold Standard

The United States' Dodd-Frank law has very quickly proven effective in its requirement of companies to track the origin of the minerals they use. Armed groups which have been unable to profit from the exploitation of tin, tungsten and tantalum, have turned instead to gold, which is easier to smuggle across borders. “Gold is very portable, you can put it in your pocket and it is easily smuggled across the border. You don't need a large quantity to make a lot of money,” said an anti-fraud agent of the border custom in Goma<sup>2</sup>.

The Conflict-Free Gold Standard hopes to close this gap. It is designed to be implemented by WGC member companies and other entities involved in the extraction of gold. It has been developed to establish a common approach by which gold producers can assess and provide assurance that their gold has been extracted in a manner that does not cause, support or benefit unlawful armed conflict or contribute to serious human rights abuses or breaches of international humanitarian law<sup>3</sup>. The Conflict-Free Gold Standard, designed to increase trust and transparency in the gold supply chain, provides further confidence that responsibly undertaken gold mining is an important source of social and economic development. The Standard will act as an

<sup>1</sup> 'Conflict-free' tags help revive DRC minerals trade, <http://www.mineweb.com/mineweb/view/mineweb/en/page72068?oid=161662&sn=Detail&pid=92730>, 9 November 2012

<sup>2</sup> Gold now top conflict mineral in Congo: Report, [http://www.msnbc.msn.com/id/49551228/ns/world\\_news-africa/t/gold-now-top-conflict-mineral-congo-report/#.UJjxz2-R0oE](http://www.msnbc.msn.com/id/49551228/ns/world_news-africa/t/gold-now-top-conflict-mineral-congo-report/#.UJjxz2-R0oE), 25 October 2012  
<sup>3</sup> Conflict-Free Gold Standard, World Gold Council, October 2012

“Industry Programme” to operationalize the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas. It is also designed to complement and integrate with other industry-led initiatives including the London Bullion Market Association's Responsible Gold Guidance<sup>4</sup>.

### Effective date for reporting

The effective start date of the Standard is for the period commencing 1 January 2013. Assurance is applicable from the first year of reporting onwards. It is recommended that the company publishes its Conflict-Free Gold Report and independent assurance report within four months, following its year-end reporting cycle.

Companies following the Gold Standard will apply the following principles:

- 1. Conformance and public disclosure** – Report publicly on their conformance via the Conflict-Free Gold Report, which will be publicly disclosed either in a company report and/or on the company website at least annually and cover activities over a 12-month period.
- 2. Management Statement of Conformance** – Provide a statement expressing management's view that the company has the appropriate systems and processes in place to ensure that all gold and gold-bearing material leaving the mine's area of control is produced in conformance with this Standard.
- 3. Links to existing public disclosure** – Include evidence of public disclosure when operating in an area assessed to be “conflict-affected or high-risk”, such as:
  1. Public commitment(s) to human rights
  2. Disclosure of payments to governments – for more detail, view Ernst & Young's report on “Disclosing government payments”
  3. Entrench processes by which local stakeholders can raise concerns
- 4. Responsibilities of implementing companies** – Implementing companies are responsible for determining their approach to conformance reflecting their own specific circumstances, which they should agree with the external assurance provider.

**5. Responsibilities of assurance providers** – External assurance is required on the Conflict-Free Gold Report, and the external assurance provider is engaged to report in accordance with recognized assurance standards on whether the company's Conflict-Free Gold Report is prepared in accordance with the Standard.

**6. Criteria for assurance providers** – The decision as to which assurance providers to use is at the discretion of an individual implementing company.

### Implications for mining and metals companies

The adoption of this Gold Standard means that companies will need to undertake a thorough review of how to integrate these principles into both their operational and assurance models. This Standard is not just a reporting exercise but entails changing the operational model to ensure that the gold in the supply chain, right from pit to port, is legitimately mined and conflict-free. While the Standard has been developed for gold, it can be applied by any metals producer seeking to avoid involvement in conflict minerals.

**Audit implications** – The scope of the assurance engagement is to provide limited or reasonable assurance on the company's Conflict-Free Gold Report.

The Independent Assurance Report addressed to the Board of Directors or Management should state the assurance provider's conclusion. The assurance report must be publicly disclosed alongside the Conflict-Free Gold Report or there should be clear sign-posting as to where it can be accessed.

For companies that already receive independent assurance over their sustainability reporting, it may be possible that assurance over the Standard is incorporated into the sustainability assurance report as an additional assurance scope area<sup>5</sup>.

### Conclusion

The implementation of these regulations means that mining and metals companies may need evidence that they do not inadvertently support the armed conflict, and that they are now part of the solution in stopping conflict minerals. And customers of mining and metals companies may request reports or assurances beyond those required by regulation. However, even though adherence to Dodd-Frank Section 1502 and the Conflict-Free Gold Standard will be both costly in terms of time and compliance, the support of the Legislation and Standard will boost an organization's social license to operate, especially in communities that will derive direct benefits from legitimate mining and metals activity.

<sup>4</sup> Conflict-free gold standard launched, <http://www.mineweb.com/mineweb/view/mineweb/en/page34?oid=160528&sn=Detail>, 19 October 2012

<sup>5</sup> Conflict-Free Gold Standard, World Gold Council, October 2012

## Ernst & Young's Global Mining & Metals Center

With a strong but volatile outlook for the sector, the global mining and metals industry is focused on future growth through expanded production, without losing sight of operational efficiency and cost optimization. The sector is also faced with the increased challenges of changing expectations in the maintenance of its social license to operate, skills shortages, effectively executing capital projects and meeting Government revenue expectations.

Ernst & Young's Global Mining & Metals Center brings together a worldwide team of professionals to help you achieve your potential – a team with deep technical experience in providing assurance, tax, transactions and advisory services to the mining and metals sector.

The Center is where people and ideas come together to help mining and metals companies meet the issues of today and anticipate those of tomorrow. Ultimately it enables us to help you meet your goals and compete more effectively. It's how Ernst & Young makes a difference.

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