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Long road ahead for conflict minerals regulation

The financing of armed groups and security forces through mineral proceeds in conflict-affected and high-risk areas is likely to become subject to EU regulation. However, the exact content of this regulation – and the extent of the obligations on companies affected – is uncertain, amid ongoing debate.

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The current draft law, which aims to support and promote responsible sourcing practices of companies operating in the EU in relation to tin, tantalum, tungsten – and their ores – and gold (3TG minerals), was amended by the European Parliament (EP) Committee on International Trade (INTA) in April and then substantially changed again by the EP the following month.

Photo: Enough Project

Gold is one of the 3TG minerals included under the draft conflict minerals legislation

Current draft law

Under the current draft legislation, amended by INTA, "conflict minerals" are 3TG minerals originating in "conflict-affected and high-risk areas", which are defined as "areas in a state of armed conflict, fragile post-conflict as well as areas witnessing weak or non-existent governance and security, such as failed states, and widespread and systematic violations of international law, including human rights abuses."

The proposed legislation provides for mandatory certification of EU smelters and refiners importing conflict minerals, and voluntary certification for importers and downstream operators. Smelters and refiners that are required, as well as other companies which choose, to join the scheme are required to exercise due diligence in line with the Organisation for Economic Co-operation and Development (OECD) guidance.

Furthermore, an annual list of responsible smelters and refiners will be published in order to increase public accountability, boost supply chain transparency and incentivise responsible sourcing.

This draft of the regulation also recognises existing industry initiatives. This means that certification schemes, to which companies already belong, are brought into the EU system without imposing any additional burdens upon them. It also provides for technical and financial assistance to small and medium-sized enterprises (SMEs) that choose to take up the self-certification initiative.

European proposals

In a plenary vote on May 20, 2015, MEPs voted to overturn the current (INTA) legislative proposal and requested mandatory compliance for all importers into the EU that source 3TG minerals in conflict areas.

Under the EP proposals, there will be mandatory certification for EU importers of 3TG minerals, and smelters and refiners will have to undergo a compulsory, independent, third-party audit to check their due diligence practices.

Downstream companies will have to provide information on the steps they take to identify and address risks in their supply chains for the 3TG minerals concerned. Micro-businesses and SMEs will be eligible under the scheme for financial support under the EU's Competitiveness of Enterprises and SMEs (COSME) programme.

Reviews of the regulation will be more frequent, with a review two years after it is applied and every three years thereafter, instead of after three and six years, respectively, as previously proposed by the European Commission (EC).

The slim majority in the EP for these proposals highlighted divisions and pushed members of the European Parliament (MEP) to opt for quick negotiations with the Council and the Commission before making their formal decision during the first reading.

This unusual procedure, together with the divisions at the EP level, suggests that the draft legislation is facing a complicated negotiation process. The proposed regulation needs to be adopted under the ordinary legislative procedure, which means that both the EP and the Council, being co-legislators, will have to adopt the same final text.

As the EP has decided not to adopt its first-reading position yet, it will continue its informal trialogue talks with the Council and the Commission to seek agreement on the final version of the regulation. According to

"Companies must report on the due diligence measures taken to determine the source and chain of custody of the minerals used"

BUSINESSEUROPE – a lobby group representing enterprises in the EU – these talks "may start soon."

Comparison with the US regime

In July 2010 the Dodd-Frank Wall Street Reform and Consumer Protection Act was enacted into US law with the purpose of restructuring the financial regulatory system to restore public confidence following the 2008 financial crisis and to prevent another crisis from occurring.

Under Dodd-Frank all US-listed companies are required to disclose annually (on a Form SD) whether they and their suppliers use conflict minerals, which are defined as cassiterite – a tin oxide mineral – columbite-tantalite – from which tantalum is derived – gold and wolframite – an ore of tungsten – and their derivatives – originating from the Democratic Republic of the Congo (DRC) or an adjoining country.

Although the group of minerals covered by Dodd-Frank and the draft EU legislation are similar, the latter has a much broader geographic scope given that it does not focus solely on the DRC.

If the metals do come from the DRC, or if the source is unknown, companies must trace the supply chain for the source using a national or international due diligence standard.

Companies must report on the due diligence measures taken to determine the source and chain of custody of the minerals used, including an independent audit of this information and a description of the products that use or contain conflict minerals, where the minerals were processed and from which country the minerals originated.

This information must be filed with the US Securities and Exchange Commission (SEC) and posted on the companies' websites.

Commercial implications and initial responses

The EU is one of the world's largest markets for 3TG minerals, with more than 400 importers, and the draft law approved by the EP could affect some 880,000 European manufacturers using the metals in auto parts, electronics, packaging, lighting, aerospace, construction, jewellery and other industries.

Medef (Mouvement des entreprises de France – the largest employer federation in France) contacted MEPs before the plenary session to warn them of the potentially costly consequences of a binding system covering the whole supply chain, on the grounds that it would be "inefficient, impracticable and unreliable".

"Online retailers would have to certify every product available on their websites that contains 3TG minerals"

Medef warned that the proposed system would engender significant costs, particularly for small businesses, which would be disproportionate to the expected results.

The American Chamber of Commerce (AmCham), the EU, the European Committee of Domestic Equipment Manufacturers (CECED), DIGITALEUROPE, the IPC, Japan Business Council in Europe (JBCE), the Japan Electronics and Information Technology Industries Association (JEITA), the Korea Electronics Association (KEA), Semiconductor Equipment and Materials International (SEMI) and the Trans-Atlantic Business Council (TABC) also support concentrating on upstream supply chain operators on the ground that this leverages the appropriate point in the supply chain, is consistent with the OECD guidance and industry initiatives, and complements Dodd-Frank.

Beyond the pinch point of smelters and refiners, the group thinks that it becomes exponentially more difficult to identify the origins of metals. The group also supports the acknowledgment of existing industry schemes, since schemes such as the London Bullion Market Association Gold Standard, the Responsible Jewellery Council Certification Programme and the Conflict-Free Sourcing Initiative focus on the same point in the global metal supply chain and use independent third-party audits to certify smelters and refiners.

By including provisions to allow for the accreditation of these schemes, this avoids duplication of effort, administrative and financial burden on companies and SMEs, and confusion in the global marketplace.

Downstream users will be challenged to prove the products they use are conflict-free, particularly as many companies use various 3TG minerals from various sources, as well as half-products. For example, as part of their engineering operations, aircraft manufacturers use thousands of components containing 3TG minerals, for which they would have difficulty certifying every single part.

Online retailers would have to certify every product available on their websites that contains 3TG minerals. Even Fairphone, a social enterprise smartphone developer, which relies on being conflict-mineral-free is its USP, acknowledges that it cannot yet trace every single mineral in its phone back to its source.

It is also questionable whether it would be possible to effectively audit and check a mandatory scheme. The differences between capacities of EU member states would further complicate this obligation and potentially cause fragmentation within the internal market.

Some commentators use Dodd-Frank as evidence that a fully mandatory scheme is not a realistic or effective option. In the US, many companies have decided to opt for DRC-free minerals, rather than 'conflict-free' and the legal export of minerals from the DRC dropped by 90% when Dodd-Frank was implemented. This has substantially damaged the legitimate trade in minerals in the region, hurting both the local economy and population.

BUSINESSEUROPE supports this view and has criticised the EP's proposal as it "fails to acknowledge the negative effects of fully mandatory due diligence schemes – as experience from the US Dodd Frank Act section 1502 has already shown – both on the ground with de facto trade embargoes as well as at the level of business operations with significant compliance costs."

The ongoing debate over conflict minerals, and the distance between the various proposals and positions, demonstrates that there is likely still a long way to go before any form of agreement on the final draft of the legislation can be expected.

Indeed, critical issues still need to be resolved, namely the origin of minerals to be regulated, whether obligations will be extended to importers and downstream entities, and the mandatory or voluntary nature of the obligations. We must now wait for conclusions from the trialogue discussions in order to see how regulation develops in this area.

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