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EU Adopts Final Regulation On Importation Of Conflict Minerals

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Conflict Minerals

On March 16, 2017, following a lengthy legislative process, the European Parliament approved a final regulation implementing a new due diligence and reporting regime for "conflict minerals" (i.e., tin, tantalum and tungsten, their ores, and gold) imported in the EU. The regulation will enter into force 20 days after formal approval by the Council of Ministers and publication in the Official Journal of the European Union. The regime will be applicable as from January 1, 2021. The adopted text can be found here.

The regulation comes after three years of debate and negotiations among the EU institutions, over which Covington reported regularly. (See in particular: Alert March 11, 2014; Alert June 6 , 2014; Alert November 5, 2014; Blog Post April 21, 2015; Alert May 22, 2015; Law 360 June 1, 2015; Alert June 27, 2016)

Background

For a number of years, the international community has pursued strategies to address the extraction of conflict minerals in conflict-affected areas under conditions which violate human rights, and profits of which serve to sustain armed groups in such areas. Public and private initiatives have pushed for more transparency and due diligence for companies sourcing minerals from conflict-affected areas in general, and the Great Lakes region of Africa in particular. Since 2002, the UN expert group on illegal exploitation of natural resources of the Democratic Republic of Congo has highlighted the link between the illegal exploitation of mineral resources and the conflict in that country. But, until now, the only mandatory diligence and reporting regime was found in the United States - i.e., Section 1502 of the 2010 Dodd Frank Act and the rules implemented thereunder by the U.S. Securities and Exchange Commission.[1]

The New EU Regulation

While the new EU regulation may have been inspired by the U.S. legislation and covers the same minerals, it is less stringent, as it will impose no mandatory requirements on 'downstream' operators (i.e., companies that manufacture components or finished products for sale). Rather, only direct importers, including smelters and refiners, will be covered by the regulation. However, the geographical scope is wider than that of the 2010 Dodd Frank Act: not

1 Ironically, just as the EU regulation comes into force, the Trump Administration has signaled that it may pursue the suspension or repeal of Section 1502 of the Dodd-Frank Act and/or the SEC's conflict minerals rules.

only does it apply to the Great Lakes region of Central Africa, but it covers conflict minerals extracted in all ‘conflict affected and high-risk areas’ in the world.

The main elements of the EU regulation can be summed up as follows:

- Direct importers in the EU will be required to conduct supply chain due diligence when they import any of the four specified minerals, or specified metals containing or consisting of such minerals, from any conflict-affected and high-risk area in the world. This obligation will also apply to smelters and refiners processing such minerals inside the EU. The regulation will not apply to the ‘smallest importers’ - i.e., where such importers’ annual imports are below specified volume thresholds (as may be the case, for example, for importers of minerals or metals used for dentistry or jewelry).

- Recycled metals, existing EU stocks (i.e., those created before February 1, 2013), and by-products are excluded from the regulation.

- Generally, the due diligence obligations imposed by the regulation are established with reference to the due diligence procedures set out in the OECD Guidance for responsible supply chains of minerals from conflict-affected and high-risk areas. More specifically, companies subject to the regulation will be required, among other things, to (i) adopt and communicate to their suppliers and the public their supply chain policy for minerals and metals possibly originating from conflict-affected areas, (ii) structure their internal management systems to support supply chain due diligence and maintain records of such systems for at least five years, and (iii) operate a supply chain traceability system that provides information regarding each mineral or metal, the suppliers of such minerals or metals, the minerals’ country of origin, quantities and dates of extraction of minerals (if available), the smelters or refiners in the company’s supply chain, and, where the minerals originate from conflict-affected and high-risk areas or other supply chain risks are present, other information in accordance with the OECD Guidance.

- Covered companies will also be required to identify and assess the risks of adverse impacts in their supply chain and implement a strategy to respond to such risks, including adopting appropriate risk management systems.

- Covered companies must also carry out independent third-party audits of their supply chain due diligence systems to ascertain conformity with the requirements of the regulation (importers of metals will be exempt from this audit requirement if they can demonstrate that all smelters and refiners in their supply chain comply with the regulation).

- The regulation imposes certain disclosure and reporting requirements on covered importers, including obligations to provide downstream purchasers with all supply chain due diligence information the importer has, and to publicly report (including on the internet) on the steps taken by the importer to fulfill its obligations under the regulation.

- The Member States’ authorities will be responsible for ensuring that companies comply with their obligations, and for imposing penalties where appropriate. The Commission will draw up a list of responsible smelters and/or refiners supplying the EU.

- The regulation defines 'conflict affected and high risk areas' as 'areas in a state of armed conflict or fragile post-conflict, as well as areas witnessing weak or non-existent governance and security, such as failed states, and widespread and systemic violations of international law, including human rights abuses.' The Commission, together with the European External Action Service and the OECD, will set up a handbook to help companies identify which areas of the world meet this definition, and are, thereby, covered by the regulation.

- The regulation also encourages EU firms with more than 500 employees making or selling goods containing conflict minerals to report (voluntarily) on their sourcing practices based on a new set of performance indicators to be developed by the European Commission.

More on the Legislative History

In the European Commission's initial proposal for a conflict minerals regulation, the whole regime was supposed to be voluntary. The Commission feared that imposing strict obligations would discourage industry from using any mineral from the Great Lakes region, which risked seriously affecting the local economy. The initial proposal created a voluntary 'self-certification' system for importers of tin, tantalum, tungsten and gold who choose to import 'responsibly' in the Union; those opting in would have needed to implement the OECD due diligence guidance, provide audit assurances and disclosure information to the Member states competent authorities.

When the European Parliament concluded its deliberation on the Commission's initial proposal in May 2015, very radical amendments had been introduced, the most far reaching on the last day of the debate in plenary. Their effect was to make reporting mandatory for all actors, including the 'downstream' users of the minerals. This position was strongly supported by NGOs but criticized by governments and industry for imposing an excessive burden on the 800,000 companies concerned in the downstream side of the trade.

The Council of Ministers only started discretely considering the proposal in September 2015, careful not to give the impression of being less concerned than the European Parliament with the harm caused by the mining of the minerals in conflict-affected areas. Nonetheless, the Council was keen to avoid the excessive burden that the implementation of the European Parliament's position would have caused on industry.

After some very difficult meetings in 'trilogue' with the delegation of the European Parliament, and thanks to major efforts by the Dutch rotating presidency of the Council, finally in June 2016 a compromise was reached and the final regulation came into focus. The final regulation makes use of existing industry control schemes, in order to avoid double burdens, but the Parliament ensured that these schemes will be regularly checked so as to ensure that the high international standards of the OECD Guidance will be maintained.

The Parliament also obtained the inclusion of a review clause, requiring the Commission to report, two years after its entry into force, on the 'effectiveness of the regulation, 'taking into account both its impact on the ground and compliance by EU firms.' If the conclusions are negative, the EU should 'consider additional mandatory measures.'

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