Blog: Product compliance update on proposed EU conflict minerals rules - European Parliament seeks to include downstream users

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What's this about?

The growth of compliance legislation concerning supply-chain due diligence continues.

Proposed EU legislation on conflict minerals recently came a step closer to becoming law when at the end of May the European Parliament voted through an amended version of a draft 2014 EU Regulation.

This proposed new regime will impose mandatory compliance requirements on importers of certain metals and minerals into the EU from conflict areas in the world, and, if finally adopted in the Parliament's version, on downstream businesses too.

What is the purpose of the proposed rules?

These proposed rules aim at stopping armed groups in conflict-affected and high risk areas around the globe (such as the Democratic Republic of Congo) from financing their activities through mining and trading minerals. The aim is to stop this trade funding armed conflicts and/or fostering human rights violations. OECD guidelines in this area already exist, which the proposed EU rules follow and extensively incorporate, and, in the US similar rules exist in the Dodd-Frank Act (Section 1502). The driving idea behind the proposed rules is essentially to break the link between conflict and the sourcing of the metals and minerals in question by addressing the risk of financing armed groups and security forces and mitigating other adverse impacts including serious abuses associated with the extraction, transport or trade of the metals and minerals in question.

Which products are affected?

Last year the European Commission proposed a short draft Regulation setting up an EU *voluntary* self-certification system for importers of the following metals and minerals:

- Tin - ores and concentrates; unwrought; bars, rods, profiles and wires; and, other articles;
- Tungsten - ores and concentrates, oxides and hydroxides; carbides; powder; unwrought, including bars and rods obtained simply by sintering; wire; and, bars and rods, other than those obtained simply by sintering, profiles, plates, sheets, strip and foil, and other (sic);
- Tantalum - ores and concentrates; carbides; unwrought including bars and rods, obtained simply by sintering; powders; and, bars and rods, other than those obtained simply by sintering, profiles, wire, plates, sheets, strip and foil, and other (sic); and,
- Gold - ores and concentrates; and, unwrought or in semi-manufactured forms, or in powder form.

The Parliament is seeking for certification to be *mandatory*, but the scope of the proposed list of metals and minerals has not been changed.

What are the compliance obligations?

EU importers who submit to the system are obliged to integrate OECD standards in their management system by:

- Maintaining a system of controls and transparency over the mineral supply-chain, including having in place a specific whistle-blowing early-warning risk awareness mechanism so that concerns can be voiced about mineral extraction, trade, handling and export in conflict-affected and high risk areas;
- Identifying and assessing risks in the supply-chain against the OECD model supply chain;
- Designing and implementing a strategy to respond to identified risks, which may include disengaging with suppliers:

- Obtaining independent third-party audit assurances of the supply-chain; and,
- Annually reporting publicly on supply-chain due diligence - EU Member State regulators will also be able to carry out ex-post checks to ensure that importers are meeting their obligations.

EU importers would be required to annually disclose (by 31 March of each year at the latest) to the relevant EU Member State regulatory authority the identity and geographical location of the smelters/refiners in their supply-chains. Based on this, an EU list of responsible smelters/refiners established in or supplying to the EU will be drawn up.

The Commission estimates that some 400 importers would be affected - the EU market is supposedly one of the most significant for the metals and minerals in question. However, the Parliament has proposed a radical and potentially very high impact change to the draft rules in that it has put forward amendments to include *downstream users*, i.e EU firms that use tin, tungsten, tantalum and gold in manufacturing consumer products - the estimates are that there are some 880,000 downstream users who would be affected by the proposed EU rules. On the basis that metal smelters and gold refiners are the last point at which the origin of minerals can be effectively traced, the Parliament is proposing amendments that go beyond the Commission's proposed self-certification system so that smelters and refiners undergo a *compulsory*, independent, and third-party audit to check their due diligence practices.

What are the penalties?

Because this legislation is in the form of a Regulation, it is for the (28) EU Member States to individually decide at their discretion which sanctions will apply for infringement of the rules. Therefore, generally-speaking a wide range of penalties can be expected which might include criminal sanctions. But the Regulation also stipulates that EU Member State regulators have to issue to importers "a notice of remedial action to be taken" by the importer - failure to comply with this will mean that a regulator must issue to an importer a "notice of non-recognition" of the importer's certificate.

What are the next steps?

In an unusual move, although the Parliament has voted on the proposed rules, according to its press release, it "decided not to close the first reading position and to enter into informal talks with the Member States to seek agreement on the final version of the law." Because of the Parliament's controversial proposed amendments this discussion can expect to be heated. In the normal course of events the proposed draft Regulation should then next go to the (EU) Council of Ministers (consisting of all 28 EU Member States) for their consideration to be followed by final agreement with the European Parliament, but it is not clear what the impact will be on this process given the Parliament's move to start informal talks.

Once agreement is eventually reached and the Regulation has been finalised, it will enter into force within less than a month of being officially published - it is impossible to say at this stage when this might occur.

Comment

Needless to say, affected companies will have to structure their internal management systems to support supply-chain due diligence and also set up risk assessment processes in order to meet the requirements of the rules. Tracing and obtaining reliable information will not be without its challenges. Should the Parliament not get its way and a voluntary system eventually prevails, those who don't conform to it face reputational risk.

These proposed new rules come at a time of increased transparency requirements for some industries. The UK already has transparency legislation in place for the extractive industries which we have reported about here and here. The interaction with other laws should also not be underestimated. Work in challenging countries like those likely to be in scope for these new laws can also attract the attention of anti-bribery enforcement authorities including the UK's Serious Fraud Office (whose activities and cases we have reported on here) which is understood to be looking at cases involving the extractive industries too. These transparency obligations will also aid their intelligence efforts.

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