



**RCS GLOBAL**  
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# RCS GLOBAL IPSA INDUSTRY GUIDANCE NOTE

A STATUS UPDATE ON IPSA AND WHY THE AUDIT  
CONTINUES TO BE A CRITICAL TOOL IN  
CONFLICT MINERAL COMPLIANCE

## ABOUT THIS PAPER

A status update on IPSA and why the audit continues to be a critical tool in conflict mineral compliance

- The ambiguity around Dodd-Frank Section 1502 has led many companies to fail to take adequate due diligence measures in their supply chain
- Reporting requirements for companies sourcing 3TGs remain “under-review”
- But industry take-up of Independent Private Sector Audits (IPSA) – the audit required to declare that supply chains are ‘DRC conflict free’ – is increasing year-on-year
- This increase is paralleled with increased regulatory and public scrutiny of the conflict minerals space in 2016
- Companies are urged to prepare for and implement an IPSA now if they want to report their supply chain as ‘DRC conflict free’
- For listed or unlisted companies situated in the downstream that do not wish to declare ‘DRC conflict free’ status, the CFSI Downstream Program provides a suitable alternative to independently validate their conflict minerals program.



## BACKGROUND BRIEFING

It has been four years since Section 1502 of the Dodd-Frank Act (DF1502) was finalised by US lawmakers. For SEC issuers producing products containing tantalum, tin, tungsten and gold (3TG) the law requires them to make efforts to determine if those materials came from the Democratic Republic of Congo (DRC) or an adjoining country.

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The law affects approximately 6000 SEC Issuers, specifically manufacturers who produce or contract to produce anything containing 3TG. These companies include large consumer brands seen in every shopping mall.

If the 3TG minerals are found to be from ‘covered countries’ which means from the DRC or 9 surrounding countries, manufacturers are obliged to carry out a “due diligence” review of their supply chain to determine

The Law affects

**6000**  
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whether their mineral purchases are funding armed groups or contributing to serious human rights abuse in the covered countries.

Initial reporting began in 2013 but the parameters on how and what to report have been inconsistent. In April 2014 the US Court of Appeals for the District of Columbia partially upheld an appeal by US business groups who claimed full disclosure of their manufacturing inputs was unconstitutional on First Amendments Grounds.

The Court of Appeal decision confirmed that Dodd-Frank Section 1502 was still in effect but that the disclosure requirements were, in essence, under review. In the interim SEC issuers are no longer by law required to declare if their supply chains are 'DRC conflict free' or not. Issuers are free to describe their conclusions of their supply chain due diligence as they wish.

As a result, an independent private sector audit (IPSA) of a company's due diligence is only required for those that volunteer to describe products containing 3TG as "DRC conflict free."

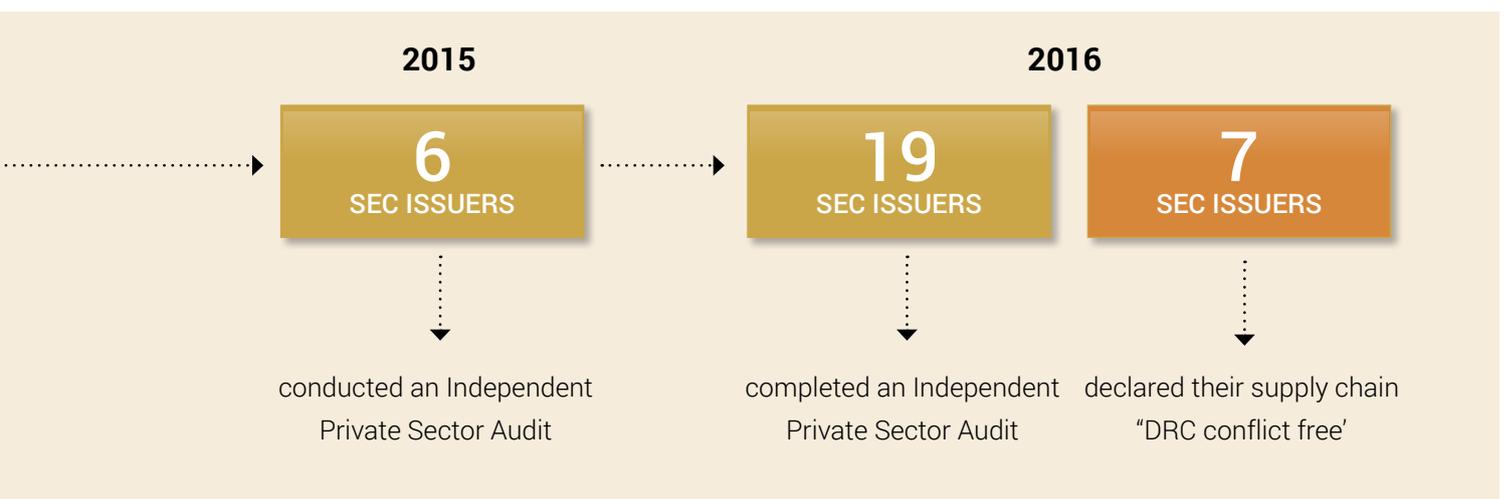
As it stands the decision on how Section 1502 should be interpreted and implemented remains with the US Court of Appeals for the District of Columbia.

It is unclear when Issuers can expect clarity from the SEC on this uncertainty and as such it is down to the companies to decide how to describe the outcome of their supply chain due diligence for conflict minerals. With no penalty foreseen in the law, disclosure requirements in conjunction with the independent audit provide the main enforcing mechanism for Section 1502. INGOs have pointed out that the removal of the conflict free declaration opens the possibility that the level of due diligence compliance companies are obliged to meet is not as high as if under an audit.

In 2016 only nineteen SEC Issuers completed an Independent Private Sector Audit and only seven of these companies fulfilled the original aim of Section 1502 and declared their supply chain "DRC conflict free".

While this number is an increase on 2015's IPSAs conducted (six in total), with 6000 SEC issuers subject to DF1502, activists would have certainly been hoping for more IPSA audits than nineteen.

Nevertheless, we believe an independent validation of company's due diligence efforts is likely to increase year on year. This independent validation is a core reason that IPSAs remain valuable for companies – as external scrutiny from activists and the public is unlikely to wane.



## WHY IPSAS ARE STILL VALUABLE

Since the inception of Dodd-Frank, RCS Global has become one of the leading suppliers of IPSA Audits including for clients who decided not to declare conflict free – and preferred to use the process to the robustness of their due diligence program.

So in the light of the stagnation in the legal imperative for IPSAs what is the utility of an IPSA or an IPSA readiness audit?

We decided to ask some of our clients.

### CONFLICT FREE SUPPLY CHAINS ARE NOT PURELY A US CONCERN

**The most directly useful result of an IPSA or IPSA readiness audit is that it gives companies an independent 3rd party review of their due diligence design against the OECD Due Diligence Guidance.**

This point has become even more relevant over the last two years as the OECD Guidance is the reference point for regulations and guidelines being elaborated in Europe and China.

In November 2016, the EU Parliament formally adopted mandatory due diligence for 3TG importers when they relate to conflict and high-risk areas. The EU also foresees an EU registry for large downstream companies (500 employees or more) to report voluntarily on their due diligence practices.



### REPUTATIONAL AND POLITICAL RISK COULD OVERTAKE LEGAL RISK

Media stories related to conflict mineral free supply chains have become a staple of the mainstream and, especially, the trade press. Equally, INGOs and pressure groups continue to put significant scrutiny and pressure on US and European manufacturers vis-à-vis their 3TG supplies. Similarly, company rankings are published on an annual basis covering both due diligence programs as well as disclosures. IPSA verification can validate and acknowledge best practice – shining a light on “good” companies while a lack of accreditation can leave a company open to negative media and advocacy pressure whether warranted or not.

### IPSA READINESS FOCUSES THE MINDS OF COMPLIANCE MANAGERS

Another useful result of the IPSA process has been to provide insight to compliance officers of the discipline required when undergoing the audit process.

**Fundamentally, the IPSA tests against two aspects of the company’s due diligence program: firstly, is the program designed in conformance with the OECD Due Diligence Guidance; and secondly, has the company done what it has stated it does in its conflict minerals report to the SEC?**

It is this second aspect that can trip companies up. Broad statements are pinpointed by auditors and proof is asked and sometimes lacking. The readiness process identifies these issues and enables compliance managers to draw a direct link between the CMR and their activities, ensuring all statements in the CMR are auditable.

Due to the fact that DF1502 requires a report lodged with the SEC, some company’s due diligence programs are led by the legal department. But the most successful companies combine their legal compliance with effective cooperation with their sales, quality and purchasing departments. This is especially due to the fact that the IPSA audit will check statements made in the CMR, against activities carried out.

## WHAT OTHER OPTIONS ARE THERE?

While full IPSA verified supply chain audits are currently not mandatory – a rapidly growing number of SEC issuers are voluntarily auditing their suppliers – or are themselves undergoing an audit - as part of a risk-based approach to due diligence.

The key difference of such audits are that they test the actual implementation – as opposed to just the design – of the due diligence program to ensure that it is aligned with the OECD Due Diligence Guidelines. Secondly, such audits also review the systems in place to gather and review supply chain mapping information that is commonly collected using the EICC Conflict Minerals Reporting Template (CMRT).

The OECD Guidance elaborates a risk based approach towards due diligence. While effective supplier programs are crucial, they need to form part of a rational and reasonable approach that has measured the risks in the company's supply chain and then responded to the risks identified.

Most often, companies are too busy delving into the details that they fail to step back and take a look – what are the key risks in the supply chain – how should I best respond?

The most significant example of this type of risk we see is the blind over-reliance on the CMRT declaration from suppliers. However, if your program is fully reliant on the information in the CMRT, the danger is that inaccuracy of this information is one of your biggest risks.

For some companies who have identified this danger, RCS Global has developed an audit to validate the supplier's conformance with the OECD Due Diligence Guidance as well as to assess the process in place to gather and review CMRT information. We have conducted over 50 such audits globally since 2013 and in 2016 the CFSI has adopted our audit as their new Downstream Audit recognized by all major industries.

The CFSI Downstream Audit provides a mechanism for companies to obtain independent validation of responsible sourcing practices in alignment with the OECD Due Diligence Guidance for Responsible Mineral Supply Chains from Conflict-Affected and High-Risk Areas. The audit reduces the need for 3TG suppliers to undergo multiple audits by different customers each year to respond to requests for independent assurance. This is a voluntary, market-driven program that was developed in response to multiple requests for a centralized platform to provide an assurance mechanism for downstream companies. The key difference to an IPSA is that the CFSI Downstream Audit is not linked to the company's Conflict Minerals Report including in the filing to the SEC.

Our audits reveal that often suppliers do not understand their requirements, and that the data in the CMRT can be unreliable. Improvements do come. Correcting this requires sustained pressure from their clients, training and sometimes more direct interventions.

**In other words – the IPSA or other conflict minerals audits are not just as a way to test compliance, but also an opportunity for the client to take a bird's eye view of their actions and develop responses that bring them closer towards more responsible supply chains.**



## WHICH AUDIT IS RIGHT FOR MY COMPANY?

	IPSA	CFSI DOWNSTREAM
Certifies “Conflict-free” status	■	■
Proves alignment with OECD Guidelines	■	■
Validates best (ethical) practice	■	■
Linked to SEC-Reporting	■	■
“Toolkit” for compliance managers to improve due diligence	■	■
Consolidates all downstream auditing into one	■	■
Published audit reports which can be publicised	■	■
Public listing of successful audit	■	■

## IS IT POSSIBLE FOR YOUR COMPANY TO DECLARE CONFLICT FREE?

### The short answer is yes.

There is a clear path for companies to declare conflict free and pass an IPSA audit. The steps needed – when broken down into their component parts – can be addressed coherently. On a broad level, the companies that have audited benefit from a similar pattern of adoption:

- A program designed in compliance with the OECD Guidance;
- An understanding of risks in their supply chain;
- The company has begun to respond to the risks and adapted its due diligence program accordingly;
- Accurate record keeping
- The company has reported accurately

## WHAT IS THE PROCESS OF IPSA READINESS?

Many issuers are reticent to commission an IPSA partly because of the perceived cost, capacity and bureaucracy involved. But, as mentioned above, actually the process can be completed efficiently and quickly. The requirements are clear as is the process that needs to take place to deliver the completed audit.

**An IPSA must be conducted in conformance with the US Generally Accepted Government Auditing Standards (GAGAS) relating to performance audits. In terms of the objectives of the audit itself – these are defined in Section 1502 of the Dodd Frank Act and require the auditor to conclude whether:**

1. The design of the issuer's due diligence framework conforms with all the criteria set forth in the nationally or internationally recognised due diligence framework used by the issuer. This is the OECD Due Diligence Guidance.
2. The issuer's description in the Conflict Minerals Report of the due diligence measures it performed in the period covered is consistent with the due diligence process the issuer actually undertook

**To achieve these ends issuers go through a pre-audit process and are then given an in-depth onsite audit which includes reviews of:**

- Policies and procedures describing the design of the due diligence process
- Evidence of internal and information systems controls
- Relevant sample documents such as supplier contracts, mailings, Conflict Mineral Reporting Templates (CMRTs)
- Risk assessment and mitigation plans for addressing conflict minerals in the supply chain
- Testimonial interviews with management and employees responsible for supply chain due diligence
- Third party evidence from recognised industry initiatives or service providers amongst others

The process itself then yields an IPSA report which includes the audit results including findings, conclusions, and recommendations; a statement about the auditors' compliance with GAGAS and a summary of the views of responsible officials.



## WHAT HAS BEEN THE EXPERIENCE AUDITING CONFLICT MINERALS SUPPLY CHAINS?

**RCS Global has worked with numerous companies to conduct OECD Due Diligence gap assessments, IPSAs as well as CFSI Downstream Audits evaluating due diligence programs. We found consistently that audited companies benefit from the third-party validation with:**

- Increased understanding of the OECD Due Diligence Guidance for suppliers
- Identification of opportunities for efficiencies and cost-savings in conflict minerals programs
- Improved understanding of company policies and internal programs by implementing staff
- Ability to provide targeted support to suppliers on key risks identified in the supply chain.

As much as an audit, IPSA and other conflict minerals assessments also provide an opportunity for companies to exchange with a subject matter expert on due diligence best practices. Many of our clients continue to reach out to us for updates on conflict minerals trends and developments.

We hope that this Industry Guidance Note demystifies the IPSA process and also highlights how it can be an extremely useful due diligence tool, regardless of regulatory obligations to pass it. For this reason, as well as others we have seen increased interest in IPSA audits in 2016.

Going forward we are happy to speak to any company who wants to implement an IPSA audit now or simply wants to discuss the implications and value of the process in more detail.

## ABOUT RCS GLOBAL

### Leading the drive to strengthen auditing and prove compliance

RCS Global is the industry-leading supplier of performance based Independent Private Sector Audits (IPSAs) and IPSA audit readiness services in the US. In 2016 we were ranked as one of the top two IPSA auditors in the world and have carried out more IPSAs than any other supplier in the market.

We also play a key role in the design and delivery of responsible supply chain audits and regulatory frameworks in the US, EU and China. Most recently we worked in partnership with the Conflict Free Sourcing Initiative (CFSI) to develop and implement the new CFSI Downstream Audit, a major development in this area – consolidating responsible sourcing reporting requirements within the downstream. This means companies can streamline audits as they may no longer need to commission and/or undergo multiple audits each year.

### Making raw material supply chains more responsible from source to store

Overall, RCS Global is now one of the world's leading responsible raw material supply chain audit and advisory groups. We empower upstream, midstream and downstream operators to demonstrate the highest standards of responsible supply chain due diligence and compliance. Together with our clients, we are making industry more ethical, accountable and transparent.

RCS Global has established an unrivalled position as the bridge between actors at each stage of the value chain, from major EU and US regulators and corporations to global manufacturers, processors, mining companies and artisanal mining communities.

Our senior staff each have over a decade of experience in supply chain auditing, advisory, technical assistance and research and our brand reputation is built on our team's performance since 2008. We currently work with the OECD, CFSI, BetterCoal, CCCMC, RJC and other industry bodies, as well as world leading companies.

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ELECTRONIC INDUSTRY CITIZENSHIP COALITION

TRAFIGURA

Microsoft  
NOKIA



AVX  
A KYOCERA GROUP COMPANY



CCCMC

OECD  
BETTER POLICIES FOR BETTER LIVES

bettercoal  
defining standards.refining practice





### *Our position means that we have:*

- 1.** The experience, expertise and confidence to guide you through your next steps in implementing the OECD Due Diligence Guidance's requirements. Whether that is obtaining more insights through research, making sure your management systems are robust, managing your supplier engagement and training, or undertaking supplier validation audits.
- 2.** A decade of boots on the ground experience. With our representation in China and Africa we have an in-depth understanding of mineral supply chains, from multinational downstream actors to micro-scale artisanal mining operations, as well as the governance realities these supply chains have to function in.
- 3.** A profound understanding of the risks in these supply chains and the standards that govern responsible supply chains worldwide - including regulatory and voluntary standards in North America, Europe and China.
- 4.** Excellent professional networks, from companies, to implementing bodies and governments, NGOs and the media.



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