Dodd-Frank Conflict Minerals: What's "Material" in Pre-Reporting Period?

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Dodd-Frank Conflict Minerals (DFCM) (section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act) applies to publicly-traded companies, beginning with calendar year 2013. The first SEC filing (Form SD) is due May 31, 2014. We are now in a unique window where the covered year is over, but the filing has not yet been made. How do companies handle information learned during this pre-reporting period? Does the nature of the information matter?

Materiality in the Pre-reporting Period: Whatever the cut-off dates established for production, supply chain engagement, and other parameters, the pre-reporting period is a unique window. Are there circumstances when information after December 31 (or other cut-off dates) should be reported or disclosed for the prior year?

Consider an analogy in financial reporting. Suppose Acme Toy Company's books show $10 million in annual sales at December 31. In January, before the Acme has submitted calendar year financial reports, the company learns that $4 million of products will be returned.

- Should it report sales of $10 million or $6 million?
- Does it matter when the products are actually returned, or when the company learns of the planned returns?
- Does it matter if the products are returned unopened and saleable, or if they are broken, customer returns, and unusable?

If the amount of the product returns were 40 <u>dollars</u>, there would be no question. However, a 40 <u>per cent</u> product return affects income, profitability, stock value, and the way a current or prospective investor evaluates the company. What is <u>material</u>, and what is not? Certified Public Accountants (the author is not one!) apply accounting rules to decide how to report Acme's sales, and what should be disclosed as narrative.

Materiality for DFCM is yet to be determined. Materiality is generally accepted to be in the eye of the beholder. Something is material if it would influence a reasonable person's decision. The users of the Forms SD, the decisions they make, the basis of these decisions are unknown at this time.

The author suggests that companies consider materiality concepts as they document how information is received, considered, and allocated to reporting years. Policies and procedures should align with how companies apply materiality to other disclosures in financial filings, including Management Discussion & Analysis in Forms 10-K.