

Employee Relations LAW JOURNAL

Swiss Conflict Minerals and Child Labor Due Diligence Legislation Takes Effect; Requires Due Diligence and Reporting by Many U.S.-Based Multinationals Doing Business in Switzerland

By Michael R. Littenberg, Samantha Elliott and Abigail Alfaro

The authors discuss an ordinance specifying due diligence and reporting obligations relating to conflict minerals and child labor that are laid out in the Swiss Code of Obligations.

In December, the Swiss Federal Council published the final Ordinance specifying due diligence and reporting obligations relating to conflict minerals and child labor, which are laid out in a statute, the Swiss Code of Obligations. Together with the statute, the Ordinance creates new obligations for many U.S.-based multinationals doing business in Switzerland. The statute and Ordinance also will have commercial ramifications for U.S.-based and other companies that are in the supply chains of enterprises subject to these requirements.

Michael R. Littenberg, a partner in Ropes & Gray LLP and chair of the firm's Environmental, Social and Governance ("ESG"), Corporate Social Responsibility ("CSR") and business and human rights compliance practice, represents U.S. and foreign public and private companies, investment banks, private equity funds and other managers in transactional matters, including securities offerings and mergers and acquisitions, and ongoing compliance. Samantha Elliott and Abigail Alfaro are associates in the firm's ESG, CSR and business and human rights compliance practice. The authors may be contacted at michael.littenberg@ropesgray.com, samantha.elliott@ropesgray.com and abigail.alfaro@ropesgray.com, respectively. This article was prepared in conjunction with attorneys at Swiss law firm Advestra.

The Ordinance and the relevant provisions of the Swiss Code of Obligations entered into force on January 1, 2022, but are subject to a one-year transition period.

This article provides an overview of the new requirements and near-term compliance recommendations.

THE LEAD-UP TO THE ORDINANCE

The Responsible Business Initiative

In 2015, 77 Swiss civil society organizations launched the Responsible Business Initiative (“RBI”). The RBI was a popular initiative under the Swiss public referendum system of direct democracy. A popular initiative allows Swiss citizens to request, through a national vote, an amendment to the Swiss federal constitution. If a popular initiative obtains the requisite number of signatures, the initiative is then submitted to the Federal Council (executive branch) and the Parliament, which can accept or reject the initiative or draft a counterproposal. The RBI exceeded the signature threshold and was submitted to the Swiss government during October 2016.

The RBI would have amended the Swiss federal constitution to add a new Article 101a, “Responsibility of business.” The constitutional amendment would have required enterprises with their registered office, central administration or a principal place of business in Switzerland to respect abroad internationally recognized human rights and international environmental standards. This duty would have extended to subsidiaries and other controlled enterprises.

The constitutional amendment would have required subject enterprises to carry out risk-based human rights and environmental due diligence.

In particular, enterprises would have been required to:

- (1) Identify impacts;
- (2) Take appropriate measures to prevent violations and cease existing violations; and
- (3) Account for the actions taken.

A subject enterprise would have been liable for damages abroad for violations of internationally recognized human rights or international environmental standards caused by its controlled enterprises, unless the subject enterprise could prove that it took all due care to avoid the loss or damage, or that the damage would have occurred even if all due care had been taken.

The Outcome of the Referendum

For a constitutional amendment to pass, it must receive both a majority of the total votes cast and majority support in over half the Swiss cantons. The constitutional amendment was supported by 50.7 percent of voters, but less than half the cantons. Analogous to the blue state/red state divide in the United States, the amendment did not receive majority support in many of the more conservative rural cantons.

The Federal Council did not support the proposed constitutional amendment, expressing concern with the effect it would have had on the competitiveness of Swiss companies. The business community's views were mixed. For example, in the lead-up to the vote, a large global Swiss-based bank took out a full page ad in an influential newspaper criticizing the initiative. However, many Swiss companies – including some large global brands – had previously expressed their support.

The Parliament's Indirect Counterproposal Moves Forward

As noted above, before a popular initiative can head to a national vote, both houses of the Swiss Parliament have the opportunity to make counterproposals. After almost two years of back-and-forth, in June 2020, the Parliament agreed upon the indirect counterproposal advocated by the Council of States (the upper house). It is referred to as an indirect counterproposal, rather than a direct counterproposal, because it takes the form of a statute (rather than an amendment to the constitution) and, therefore, the public referendum did not expressly allow voters to choose between the RBI and the indirect counterproposal.

If a counterproposal passes both the Council of States and the National Council (the lower house), and if the counterproposal has the support of the popular initiative's sponsors, the sponsors can withdraw the initiative and the Parliament's counterproposal becomes law.

In this case, the initiative's sponsors did not support the indirect counterproposal passed by Parliament, so the initiative was put to a national vote. However, if the initiative is put to a vote and fails – as was the case here – there are two possible subsequent paths: the Parliament's indirect counterproposal can either become law or it can be submitted to a popular vote if requested. In this case, the indirect counterproposal was not submitted to a popular vote. Instead, it amended the Swiss Code of Obligations. Note that the amendment to the Code of Obligations also requires broader-based ESG reporting by public companies and larger financial institutions supervised by the Swiss Financial Market Supervisory Authority. Those requirements are not discussed in this article.

In Spring 2021, the Federal Council published a draft Ordinance to implement the indirect counterproposal set forth in the Code of Obligations. Following expiration of the consultation period, the final version of the Ordinance was published on December 3, 2021. The final provisions of the Swiss Code of Obligations and the Ordinance (generally referred to herein as the “provisions”) are discussed below.

SCOPE OF THE NEW PROVISIONS – CHILD LABOR AND CONFLICT MINERALS

The provisions apply to child labor and specified conflict minerals and metals. In this regard, the provisions are narrower than other recently adopted corporate human rights due diligence legislation in Germany and Norway, which apply to human rights risks and impacts broadly.

Child Labor

“Child labor” includes the following, whether carried out within or outside of an employment relationship:

- Work performed by persons under 18 that comes under the International Labour Organization’s Worst Forms of Child Labour Convention;
- If a jurisdiction has ratified the ILO’s Minimum Age Convention, child labor prohibited by that jurisdiction’s laws in conformity with the Convention;
- If a jurisdiction has not ratified the Minimum Age Convention, work performed by persons who are subject to compulsory schooling or who are 15 or under; and
- If a jurisdiction has not ratified the Minimum Age Convention, work performed by persons who have not yet reached the age of 18 if that work is expected to be dangerous to life, health or morals of the worker by its nature or the conditions under which the work is performed.

Conflict Minerals and Metals

The provisions apply to tin, tantalum, tungsten and gold minerals and metals specified in more detail on an annex to the Ordinance. These

minerals and metals are frequently referred to as “conflict minerals” or the more neutral term “3TG.”

The in-scope 3TG minerals and metals are limited to specified tariff numbers and consist of ores, concentrates, powders, rods, wires and other forms of 3TG at a similar stage of processing. Therefore, an enterprise is not subject to the conflict minerals provisions if it imports or sells products or components that contain 3TG or manufactures products that contain 3TG, so long as it is not the importer into Switzerland or processor of 3TG with a specified tariff number. This is consistent with the approach taken by the European Union in its Conflict Minerals Regulation.

Entire Supply Chain Covered

Under the Ordinance, the “supply chain” is defined as a process covering both the enterprise’s own business activities and those of all upstream economic operators that (1) have minerals or metals originating from conflict-affected or high-risk areas in their custody and that are involved in their movement, preparation and processing in the final product, or (2) offer products or services for which a reasonable suspicion exists that such products or services were produced using child labor.

SUBJECT ENTERPRISES

The new provisions apply to enterprises with a registered office, central administration or principal place of business in Switzerland. This includes Swiss-organized subsidiaries of foreign-based multinationals.

“Enterprise” is broadly defined in the Ordinance to include all forms of legal enterprises. It also picks up all types of business activities. For example, in contrast to some corporate human rights legislation, “enterprise” is not limited to specified industries or types of businesses, such as retailers or manufacturers. The provisions also are not limited to activities by subject enterprises that occur in Switzerland.

As discussed in this article, there are several exceptions to the due diligence and reporting requirements of the new provisions.

EXCEPTIONS TO DUE DILIGENCE AND REPORTING

Child Labor Due Diligence and Reporting Exceptions

There are three exceptions specific to the child labor due diligence and reporting requirements of the Ordinance. However, these exceptions do not apply if the products or services are conclusively made or provided with child labor.

Small or Medium-Sized Enterprise

An enterprise generally is not subject to the child labor due diligence and reporting requirements of the Ordinance if it is a small or medium-sized enterprise. An enterprise is an SME if it and its controlled entities are under two of the following thresholds for two consecutive fiscal years:

- Total assets of SFr 20 million (approximately \$21.7 million);
- Sales of SFr 40 million (approximately \$43.5 million); and
- An annual average of 250 full-time employees.

Low Risk of Child Labor

An enterprise also generally is not subject to the child labor due diligence and reporting requirements of the Ordinance if it presents a low risk of child labor. Under these circumstances, the enterprise is not required to assess whether there is a reasonable suspicion of child labor.

An enterprise is considered to be “low risk” for child labor if the products the enterprise purchases or manufactures or the services it procures or provides are from countries designated as “Basic” in UNICEF’s Children’s Rights in the Workplace Index. This assessment must be conducted annually.

Fifty countries currently are categorized as Basic. The other categories are “Enhanced” and “Heightened.” Categorization for purposes of children’s rights does not necessarily equate with companies’ risk assessments for other human rights issues. For example, many Western European countries, such as France, Germany, the Netherlands and the United Kingdom, are categorized as Basic, as are Australia, New Zealand, Canada and Japan. Among others, Russia and Romania also are considered Basic. The Enhanced category picks up a wide range of countries with vastly different labor practices, including, alphabetically, Afghanistan, Bangladesh, China, the Democratic Republic of the Congo, Myanmar, North Korea, Turkey, Uzbekistan and the United States.

An enterprise that is low risk for child labor must document its conclusion. The conclusion is not required to be published or filed with a regulator.

Lack of Reasonable Suspicion

If an enterprise concludes that it cannot utilize the above-mentioned exemptions, it may be exempted from the child labor due diligence and

reporting requirements if there is not a reasonable suspicion of child labor. There is a reasonable suspicion of child labor if there is specific information available that would lead a reasonable person to believe that a product or service involves child labor. If the enterprise concludes there is not a reasonable suspicion of child labor, it must document its finding. The finding is not required to be published or filed with a regulator.

Conflict Minerals Due Diligence and Reporting Exceptions

De Minimis 3TG Usage

An enterprise is not subject to 3TG due diligence and reporting requirements if the 3TG it imports or processes does not exceed the levels specified on an annex to the Ordinance. The 3TG usage thresholds largely match those in the EU Conflict Minerals Regulation. The Federal Council may modify the annex.

For purposes of calculating whether a threshold is exceeded, the undertakings consolidated under the enterprise are included.

3TG Not From a Conflict-Affected or High-Risk Area

As used in the Ordinance, “conflict-affected and high-risk areas” are areas in a state of armed conflict or fragile post-conflict as well as areas witnessing weak or non-existent governance and security and in which widespread and systematic violations of international law, including human rights abuses, take place. This is the same meaning as under the EU Conflict Minerals Regulation and the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas.

The Ordinance does not identify specific areas by name as conflict-affected and high-risk. Instead, the Federal Council’s guidance refers to the European Union’s 2018 recommendations for determining whether areas are conflict-affected and high-risk for purposes of the EU Conflict Minerals Regulation and the list of conflict-affected and high-risk areas periodically published by Rand International.

The Federal Council notes in its guidance that this assessment must be done on a regular basis since conflict-affected and high-risk areas are not static. This is underscored by the evolution of the Rand International list since it was first published in December 2020.

If the enterprise concludes its 3TG is not from a conflict-affected or high-risk area, it must document its finding. The finding is not required to be published or filed with a regulator.

Compliance with Equivalent Regulation or Instrument

If none of the following exemptions are available, an enterprise will be exempt from due diligence and reporting if it complies with an internationally equivalent regulation or instrument. The regulations and instruments that currently qualify are listed on an annex to the Ordinance (for brevity, these are referred to as “Specified Instruments” in this article):

Child Labor

- ILO Minimum Age Convention, Worst Forms of Child Labour Convention and ILO-IOE Child Labour Guidance Tool for Business; and
- OECD Due Diligence Guidance for Responsible Business Conduct.

Conflict Minerals

- OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas; or
- EU Conflict Minerals Regulation.

To use this exception, the enterprise must prepare a report that identifies the Specified Instrument and comply with its requirements in their entirety.

TRANSITION PERIOD

Enterprises that cannot utilize an exception from due diligence and reporting will in any case have a transition period before they are required to comply with the provisions. Compliance will not be required until the enterprise’s fiscal year beginning in 2023.

The transition period is intended to give enterprises time to assess applicability of the new provisions and to put necessary policies and procedures in place.

DUE DILIGENCE REQUIREMENTS

Enterprises that are not exempt from due diligence must conduct risk-based due diligence relating to child labor and/or conflict minerals, as applicable.

Supply Chain Policy

As part of its due diligence, an enterprise is required to establish a supply chain policy.

Under the policy, the enterprise must, as applicable:

- Ensure it complies with due diligence obligations in its supply chains (including all upstream economic operators), when:
 - Offering products or services that are reasonably suspected of having been manufactured or provided using child labor, and/or
 - Procuring 3TG originating from conflict-affected and high-risk areas;
- Communicate up-to-date information on the policy to its suppliers and the public;
- Integrate the supply chain policy into contracts and agreements with suppliers;
- Ensure that concerns about child labor and conflict minerals in its supply chain can be reported; and
- Investigate concrete indications of child labor and/or identify and assess risks of adverse impacts of 3TG originating from conflict-affected and high-risk areas in the supply chain, and in each case take appropriate measures to avoid or mitigate adverse impacts, evaluate the results of measures taken and communicate the results of the measures taken.

The policy is required to specify the tools used by the enterprise to identify, assess, eliminate and/or mitigate adverse impacts in its supply chain. Under the Ordinance, these include in particular the following:

- On-the-spot checks;
- Information from public authorities, international organizations and civil society;
- Use of experts and specialist literature;

- Assurances from supply chain economic operators and other business partners; and
- Use of recognized standards and certification schemes.

Traceability System

The Ordinance requires enterprises to establish a supply chain traceability system for child labor and/or conflict minerals, as applicable. The requirements differ for each of these subject areas.

Child Labor

The traceability system must contain and document the following information where there is a reasonable suspicion of child labor:

- The description of the product or service and, if any, trade name; and
- The name and address of the supplier and the production sites or the service provider to the enterprise.

Conflict Minerals

The traceability system must contain and document the following information for 3TG originating from a conflict-affected and high-risk area:

- The description of the mineral or metal, including its trade name;
- The name and address of the supplier;
- The country of origin of the mineral;
- For metals, the name and address of the smelters and refiners in the supply chain;
- For minerals, to the extent available, the volume or weight and the date mined;
- For minerals originating from conflict-affected and high-risk areas or for which the enterprise has identified other supply chain risks specified in the conflict minerals-related Specified Instruments listed earlier in this article, additional information

in accordance with the supply chain recommendations in those instruments, such as mine of origin, where the mineral is combined with other minerals, traded or processed and the taxes, duties and fees paid; and

- For metals, (1) where available, assessments of smelters and refiners carried out by third parties; (2) where these assessments are not available, the country of origin of the mineral and the location of the smelter or refiner; and (3) for metals originating from conflict-affected and high-risk areas or if other supply chain risks specified in the previously listed conflict minerals-related Specified Instruments have been identified, additional information relating to downstream undertakings in accordance with the recommendations in those Specified Instruments.

By-products are required to be traced back only to the point at which they were first separated from their primary mineral or metal.

Grievance Mechanism

In addition to referring to grievance reporting in the policy requirements, the Ordinance contains a separate section addressing grievance mechanism requirements in slightly more detail.

As an early warning mechanism for risk identification, the enterprise must provide a reporting mechanism that allows all interested persons to express reasonable concerns regarding actual or potential adverse impacts relating to child labor or 3TG. The enterprise must document any complaints received.

Risk Mitigation

Under the Ordinance, the probability and severity of adverse impacts is to be taken into account in connection with the identification and assessment of supply chain risks. Risks are to be identified and assessed based on the Specified Instruments.

The probability and severity of adverse impacts also is to be taken into account in the elimination, prevention or mitigation of identified supply chain risks. The effectiveness of the measures taken is required to be assessed on a regular basis.

Audit Requirements Relating to 3TG

If conflict minerals due diligence is conducted, an annual third-party audit is required. The scope of the audit is to provide negative assurance

concerning the enterprise's compliance with its 3TG-related diligence obligations under the Ordinance. The auditor must be admitted as an audit expert pursuant to the Swiss Audit Oversight Act. The audit requirement does not extend to child labor due diligence.

Partial 3TG Due Diligence Exception

An enterprise is exempt from the requirements to establish a grievance mechanism and risk management plan and obtain an audit report if it imports and processes only recycled metals.

REPORTING

Subject enterprises that are required to conduct due diligence generally are required to prepare an annual report discussing their compliance with the due diligence obligations. Swiss law is silent on the detailed content of the report.

The first report will be due in 2024 in respect of the fiscal year that began in 2023. The report is required to be posted on the enterprise's website within six months after the end of the fiscal year and must be accessible for at least ten years.

Reporting Exceptions

Enterprises based in Switzerland are exempt from the reporting requirement if they are controlled by a company established abroad that publishes a similar report. However, the Swiss enterprise must include a note in its financial statements indicating the controlling company that includes the Swiss enterprise in its report. The enterprise also is required to publish the controlling company's report.

Enterprises that offer products or services from enterprises that already have published a report also are exempted from the duty to publish a report.

CRIMINAL LIABILITY FOR NON-COMPLIANCE

The Swiss Criminal Code provides for a fine of up to SFr 100,000 for intentionally providing a false statement in a report pursuant to the provisions, intentionally failing to comply with the reporting obligation or failing to comply with the traceability documentation obligations. In case of negligence, the maximum fine is reduced to SFr 50,000.

COMPLIANCE RECOMMENDATIONS

U.S.-based multinationals doing business in Switzerland should take the following near-term compliance steps, as applicable:

- As an initial matter, determine whether any group company comes within the new provisions of the Swiss Code of Obligations and the Ordinance. If so, determine whether any of the exceptions to due diligence apply. U.S.-based multinationals are unlikely to come under the conflict minerals prong of the Ordinance since it applies narrowly to 3TG importers and processors. The child labor prong will be more relevant.
- If one or more exceptions apply, document those exceptions to the extent required by the Ordinance, as discussed in this article.
- If subject to the provisions and no exceptions to due diligence apply, assess existing policies and procedures against the requirements of the Ordinance. To the extent there are gaps, establish an action plan to address the deficiencies. Most U.S.-based multinationals have moved to a common enterprise-wide approach to managing human rights matters, or are in the process of doing so. To the extent aspects of the current child labor or conflict minerals compliance program require enhancement to meet the requirements of the Ordinance, consideration will need to be given whether to roll the enhancements out across the enterprise, or only at the operations subject to the provisions. In addition, the enterprise will need to determine whether it can take advantage of a reporting exception, although that can be assessed closer to the time of the first annual report.
- If relying on the SME and/or “low risk” exceptions to child labor due diligence and reporting, set up an annual process to assess the continuing applicability of the exceptions.
- Even if not subject to the provisions or an exception is available, be mindful of commercial expectations arising out of the due diligence and reporting requirements of commercial customers, and their direct and indirect commercial customers. U.S.-based businesses will need to manage to these expectations, which may require enhancements to policies and procedures.

Copyright © 2022 CCH Incorporated. All Rights Reserved. Reprinted from *Employee Relations Law Journal*, Summer 2022, Volume 48, Number 1, pages 51–63, with permission from Wolters Kluwer, New York, NY, 1-800-638-8437, www.WoltersKluwerLR.com

