

Federal Appeals Court Largely Upholds Conflict Minerals Rules

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April 23, 2014

On April 14, 2014, the United States Court of Appeals for the D.C. Circuit issued its much anticipated decision regarding the challenge to the Securities and Exchange Commission's Conflict Minerals Rules. The Court largely upheld the Rules, although it took issue with one aspect of the new regulations on free speech grounds. The case is *National Association of Manufacturers, et al. v. Securities and Exchange Commission, et al.* (D.C. Cir. No. 13-5252).

Following the decision, in the absence of SEC advice to the contrary, companies should continue to plan to comply with the Rules in the current reporting cycle, with the first filing due on June 2.

Purpose of the Rules

Effective November 2012, the SEC adopted the Conflict Minerals Rules pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act. The Conflict Minerals Rules require SEC reporting companies to disclose whether any of tin, gold, tungsten or tantalum – the four “conflict minerals” – are necessary to the functionality or production of their products and originate from war-torn Democratic Republic of the Congo or any one of nine neighboring countries. The Rules are intended to cut down on funding for armed groups in the Central African conflict by requiring companies to report on their use of conflict minerals from the region.

Public companies that determine that none of the four conflict minerals are necessary to the functionality or production of their products have no obligation under the Conflict Minerals Rules. Note, however, there is no *de minimis* exception, and the slightest impact of conflict minerals on a company's products will subject that company to the Conflict Minerals Rules.

During a two year phase-in period (four years for smaller companies), public companies may report products as “DRC conflict undeterminable,” rather than “conflict-free” or “not conflict-free.”

The Challenge

The U.S. Chamber of Commerce and two other groups challenged the Conflict Minerals Rules in federal court on a variety of grounds, including that the SEC had violated the Administrative Procedures Act in various ways (such as by not allowing for a *de minimis* exception), and had failed to conduct a more rigorous cost-benefit analysis before promulgating the Rules (which will cost industry billions of dollars in compliance costs). The Conflict Minerals Rules were also challenged on the ground that they require that companies make specific disclosures in violation of their free speech rights.

The Court's Ruling

In upholding the Conflicts Minerals Rules, the Court first decided that the SEC had acted appropriately under the Administrative Procedures Act in enacting the Rules and that it was not required to conduct a more detailed cost-benefit analysis than it did. On the free speech component, and as part of a larger legal struggle regarding the scope of corporate free speech rights, the Court divided 2-1, with the majority ruling that the portion of the rule that requires reporting companies to disclose to the SEC and post online whether any of their products have not been found to be “[Democratic Republic of the Congo]-conflict free” constitutes improper compelled speech. The majority explained that the required “conflict free” label is intended to “convey moral responsibility for the Congo war” and impermissibly forces an issuer “to tell consumers that its products are ethically tainted” and “to confess blood on its hands.” The ruling simply relieves companies of the obligation to report in those precise terms. Note, however, that the ruling does not seem to prevent companies from

making the banned statement voluntarily.

Next Steps

While the parties to the litigation, including the SEC, continue to maneuver in court, and while the SEC may issue further guidance in light of the recent ruling, public companies subject to the Conflicts Minerals Rules should continue to ready their filings on Form SD for calendar year 2013, which are due **June 2, 2014**.

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