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Conflict minerals update—D.C. Circuit Court upholds decision that "DRC conflict free" disclosure requirement violates First Amendment

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On August 18, 2015, a three judge panel of the U.S. Court of Appeals for the District of Columbia Circuit, in a split decision, reaffirmed that Court's April 2014 decision in *National Association of Manufacturers v. Securities and Exchange Commission*, holding again that a U.S. Securities and Exchange Commission (SEC) requirement for companies to describe their products as having "not been found to be 'DRC conflict free'" is compelled speech that violates the free speech protections afforded by the First Amendment.[1]

According to the majority opinion, not only did the SEC fail to show the effectiveness of the disclosure on "the promotion of peace and security in the Congo" but conflicting evidence showed that the cost of compliance (estimated at approximately $207 million to $609 million annually after an initial investment of $3 billion to $4 billion) may cause manufacturers to boycott mineral suppliers with possible Congo-area contacts, leaving miners with no work, and thereby potentially exacerbating the humanitarian crisis. The required disclosure also failed the test of "purely factual and uncontroversial" since "'[not] conflict free' is a metaphor that conveys moral responsibility for the Congo war." The full text of the opinion is available here.

In response to the Court's original ruling, shortly before the deadline for filing the first conflict minerals reports in 2014, the SEC issued guidance and a partial stay of the conflict minerals reporting rules mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. Under this guidance, companies have been excused from the requirement to describe their products as "DRC conflict free," having "not been found to be 'DRC conflict free'" or, for a two-year transition period, "DRC conflict undeterminable." The guidance also excused companies from obtaining and filing an independent private sector audit report unless they voluntarily chose to describe any of their products as "DRC conflict free."

[1] Additional information regarding the 2014 decision is available here: http://www.nixonpeabody.com/public_companies_must_disclose_source_of_conflict_materials

The SEC's challenge to the original 2014 ruling followed the Court's decision in *American Meat Institute v. US Department of Agriculture*, which also dealt with commercial First Amendment issues but in the context of compelled meat labeling disclosures designed to prevent the deception of consumers. There, the Court declined to invalidate the labeling requirements imposed by the federal government, finding that a looser standard of review applied in First Amendment cases involving compelled speech connected to commercial or voluntary advertising. The Court's August 18, 2015 majority opinion distinguished such types of factual statements from the statements required by the conflict minerals disclosure rules, concluding that this looser standard of review did not apply in the conflict minerals reporting context. Moreover, the majority concluded that the disclosure compelled by the conflict minerals rules violates the First Amendment, even under the looser standard of review applied in the meat labeling case.

What does this decision mean for companies that are subject to conflict minerals reporting requirements?

Following this decision, the portions of the conflict minerals rules that have been in force for the past two reporting years remain in force. Companies should therefore continue their supply chain due diligence and reporting efforts in preparation for their next Form SD and, if applicable, Conflict Minerals Report filings and website postings.

We expect that, absent further judicial proceedings or explicit guidance to the contrary, the previously issued SEC guidance on product description requirements will continue to apply. Importantly, as provided in that guidance, this likely also means that companies will not be required to obtain an independent private sector audit for the current reporting year unless they voluntarily elect to label any of their products "DRC conflict free."

Companies should continue to monitor further litigation and regulatory developments. Following this decision, the SEC may provide additional guidance and disclosure commentary to assist companies with their compliance and disclosure efforts in this area. The SEC may request a review of the latest decision by the full Court of Appeals or may appeal the decision to the Supreme Court. The SEC may also propose amendments to the current rules to address the First Amendment issues found by the Court. In any of these cases, however, it is unlikely that the constitutional issues would be resolved prior to the 2016 filing deadline.

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