

Court Vacates SEC Resource Extraction Rules

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The U.S. District Court for the District of Columbia has granted plaintiff American Petroleum Institute and others a motion for summary judgment and thrown out the SEC rules requiring oil and gas companies to disclose payments made to foreign governments in connection with the commercial development of oil, natural gas and minerals.

The SEC promulgated final rules in September 2012 that required disclosure of information on Form SD filed via EDGAR and made public. The Court declined to reach a decision on all of the challenges, including plaintiff's argument that the rules compel speech in violation of the First Amendment, and instead based its ruling on findings that the Commission misread the statute to require public disclosure, and the decision to deny any exemptions was arbitrary and capricious.

Judge Bates determined that the statute's plain language is silent as to the need to make a public filing of these reports, rejecting the SEC's argument that the statute is unambiguous in this respect. In particular, the Court was persuaded that a separate section of the statute was clear as to making publicly available a compilation of the information, but only to "the extent practicable." Reading the statute to require public disclosure of the entire annual report would then completely obviate the need that a compilation of information be practicable.

The Court also found other instances where a "report" under the Exchange Act can refer to disclosures made only to the Commission, such as under Section 13(f), and the SEC also allows for confidential treatment of certain information. In addition, Judge Bates disputed the Commission's reading of "compilation" as requiring a comprehensive collection of all of the information, noting that a compilation can include selection and editing of materials.

With respect to considering the countries that specifically prohibit disclosure (Angola, Cameroon, China and Qatar), the Commission had acknowledged the potential for issuers to suffer significant losses, but declined to adopt an exemption, finding that an exemption could undermine the statute's purpose by encouraging countries to adopt laws specifically prohibiting disclosure. The Court found that the statute expressly evidenced openness to appropriate exemptions by the SEC, and held that while it may be reasonable for the Commission to conclude that an exemption is not warranted, it should have considered the specific instance related to a specific country or certain issuer as to the burden on competition. Overall, a fuller analysis was necessary rather than reliance on a statement as to potential problems with exemptions generally.

Ultimately, the Court decided to vacate the rule and remand to the SEC since issuers are not yet required to make disclosures under the rule. In its opinion, the Court expressed concern that the rule's shortcomings are "grave indeed," noting that the Commission "fundamentally miscalculated the scope of its discretion at critical junctures." The Court indicated that the SEC may promulgate an entirely different rule "when informed that it does have the power," rather than believing that it had very limited flexibility.

It remains to be seen how this will affect the conflict minerals rule, which is before Judge Robert Wilkins of the same U.S. District Court. According to news reports, during three hours of oral arguments on Monday, the judge wondered whether federal courts should consider deferring to Congress, but also questioned whether the SEC appropriately minimized negative impacts.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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