

Reviewing the Court's Decision Upholding the Conflict Minerals Rule

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We [alerted](#) companies to the fact that yesterday, the U.S. District Court for the District of Columbia rejected a suit to invalidate the SEC's conflict mineral rule. The 63-page [opinion](#) rejects plaintiffs' various arguments to strike down the law.

Arbitrary and Capricious Claim Based on Economic Analysis. Plaintiffs challenged the rule under the Administrative Procedural Act, claiming that the Commission ignored its statutory obligations to conduct an adequate cost-benefit analysis of the rule and whether the action will promote efficiency, competition and capital formation. Plaintiffs argued that the SEC was required by the Exchange Act to independently determine whether the rule was necessary or appropriate to decrease the conflict and violence in the DRC.

The Court found, however, that the statutory provisions only obligate the SEC to "consider" the impact that a rule may have on economic-related factors such as efficiency, competition and capital formation, and while the Commission may find it appropriate to weigh costs and benefits, the Exchange Act does not mandate the SEC to conduct a broader, wide-ranging benefit analysis. The Court declared that "[s]imply put, there is no statutory support for Plaintiffs' argument that the Commission was required to evaluate whether the Conflict Minerals Rule would actually achieve the social benefits Congress envisioned."

The Court distinguished this rule from other Commission rules that have been struck down for lack of economic analysis, such as the proxy access rule, noting that (a) in those cases, the Commission needed to consider economic implications, but the conflict mineral rule aims to achieve a humanitarian benefit identified by Congress and (b) unlike the other situations where the Commission voluntarily adopted rules, the conflict minerals rule was promulgated pursuant to an express, statutory directive from Congress so the SEC's role was not to "second-guess" Congress's judgment as to the benefits of disclosure.

Arbitrary and Capricious Claim Based on Specific Rule Requirements. The Court determined that the SEC's decision not to include a de minimis exception was reasonable based on practical and policy-making rationales, and not, as Plaintiffs alleged, because the Commission wrongly believed that they were foreclosed from allowing such an exception or exercised that discretion arbitrarily.

Plaintiffs argued that the basis for "reasonable country of origin" was overly broad, requiring diligence and reports whenever there is reason to believe that minerals may have originated in the region. The Court disagreed and decided that this aspect was proper given that Congress was silent as to how companies should go about finding out whether their minerals did originate in the DRC. The statute also does not directly speak to when disclosure would be required, and the SEC reasonably evaluated and rejected other alternative approaches. The Court also determined that the rule's application regarding "contract to manufacture" was permissible, in light of the uncertainty surrounding Congress's intent in the statutory language and general ambiguity regarding what it means to "manufacture."

First Amendment Challenge. Plaintiffs' first amendment challenge was limited to the requirement to make the information publicly available on company websites, rather than in the SEC filing requirements, in particular, compelling companies to state on their websites that certain of their products are not conflict-free. The Court found that since the disclosure can be the same as what would be in the filed conflict minerals report, the ability for companies to add explanatory information as well as the transition period, the website disclosure requirement reasonably fit Congress's objectives.

Will this be Appealed? It is unclear whether the plaintiffs will appeal this ruling. In any case, it is important to remember that if the case is appealed, and even if the appeal succeeds, the Dodd-Frank Act requires that the SEC adopt rules mandating disclosure around conflict minerals. Companies' compliance efforts should bear in mind that disclosure of some sort will ultimately be required.

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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