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Court Upholds Finding That 'Conflict Minerals' Rule Is Unconstitutional

Government labeling measures could be more vulnerable to legal challenge in the wake of an appeals court ruling that struck down part of a Securities & Exchange Commission (SEC) rule requiring manufacturers to declare that their products are "not DRC conflict free" if they use imported metals that could be linked to armed conflict in the Democratic Republic of the Congo (DRC), according to lawyers following the case.

In a 2-1 split ruling made Aug. 18, the Court of Appeals for the D.C. Circuit effectively raised the bar that the government must meet to justify compelled commercial speech. It found the part of the SEC rule containing the declaration requirement could not meet that hurdle and thus concluded that it violates the First Amendment; it left untouched another portion of the rule — promulgated under the Dodd-Frank law — requiring listed companies to trace certain metals they use.

The most immediate implication of the ruling is to nullify a requirement that manufacturers worried would force them to sully their brands by associating their products with the bloodshed in the DRC, which upholds the court's 2014 ruling in the matter. But lawyers following the case said that the legal reasoning employed by the judges in the case, if repeated in future decisions, could end up making it harder for the government to compel companies to say whether their products contain genetically modified organisms (GMOs), for example, or have certain environmental qualities.

The court acknowledged the potentially far-reaching implications of its decision in the ruling itself by agreeing with the dissenting opinion that "United States is thick with laws forcing '[i]ssuers of securities' to 'make all sorts of disclosures about their products." But the majority rejected the notion that it should rule otherwise because it might open the door to adverse decisions against those requirements as well. In addition, the court also differentiated the conflict minerals rule from other public disclosure policies, arguing it is not meant to provide economic or investor protections.

Because of this, lawyers speculated that the SEC would appeal for a decision by all of the court's judges, or even petition the Supreme Court to take up the case. The SEC declined to comment for the story.

At the heart of the matter is the amount of judicial scrutiny that the government should be subject to when compelling speech. The SEC contends that its measure should be subject to the least amount of scrutiny, known in legal jargon as "rational review," under which the government must prove its measure is related to a legitimate government interest.

U.S. companies asserted that the SEC rule should have to face a higher level of scrutiny — applying what is called the "Central Hudson test" — that would require the agency to show that its measure not only relates to a government interest, but directly advances that interest, and is not more extensive than necessary.

In its decision, two of the appeals court's three-judge panel agreed with the companies, represented by the National Association of Manufacturers (NAM) and other national-level business organizations. The judges contended that the lower, "rational review" test was only applied to compelled speech related to advertising.

This ruling potentially disqualifies all manner of government labeling measures from review under the lesser amount of scrutiny. It also represents a further articulation by the court on what the bounds of the "rational review" test are.

The court in April 2014 ruled that rational review only applies in cases where compelled speech is used for the purpose of preventing consumer deception. That finding was later overturned when an en banc panel — in favor of the U.S. Department of Agriculture's country-of-origin labeling (COOL) regime for meat — said that rational review extended beyond those parameters, without offering further clarity.

While the rulings in the COOL and conflict minerals do not directly contradict each other, two lawyers following the case said that it could set up an issue of "exceptional importance" because the COOL decision intended to broaden the scope of rational review while the conflict minerals decision intended to narrow that scope.

The deadline for the SEC to file for an en banc review of the decision is Oct. 2. For an appeal to be accepted, the case must either cause a disagreement within the judicial circuit or represent a matter of "exceptional importance."

Ron Fein, legal director of Free Speech For People, said that he believes the exceptional importance standard has been met because the en banc panel in the COOL case seemed aimed at broadening the application of rational review, while the conflict minerals effectively limits its application.

Once it determined the correct legal yardstick by which to measure the SEC rule, the court went on to fault the measure for failing to directly advance the government interest. The SEC's assumption, according to the court, is that its rule would decrease the revenue of armed groups in the DRC — which would therefore diminish the humanitarian crisis. This is entirely unproved and based on speculation, the court said.

"All of this presents a serious problem for the SEC because, as we have said, the government may not rest on such

speculation or conjecture. Rather the SEC had the burden of demonstrating that the measure it adopted would 'in fact alleviate' the harms it recited 'to a material degree.' The SEC has made no such demonstration in this case and, as we have discussed, during the rulemaking the SEC conceded that it was unable to do so."

The SEC measure requires a manufacturer using gold, tin, tantalum and tungsten that are sourced from the DRC or any of its bordering countries to state on their website that their products are "not DRC conflict free."

The court further said that even if it were to presume that the declaration requirement were related to advertising, the rational review test would still not apply because the speech would not be "factual and uncontroversial."

The court said the COOL case made a distinction between "factual" and "controversial," explaining a statement can be controversial "for some reason other than [a] dispute about simple factual accuracy." The court also cited its initial April 2014 ruling, in which it elaborated on why it felt the statement was controversial.

"Products and minerals do not fight conflicts. The label '[not] conflict free' is a metaphor that conveys moral responsibility for the Congo war," the 2014 ruling says. "It requires an issuer to tell consumers that its products are ethically tainted, even if they only indirectly finance armed groups. An issuer, including an issuer who condemns the atrocities of the Congo war in the strongest terms, may disagree with that assessment of its moral responsibility. And it may convey that 'message' through 'silence.' By compelling an issuer to confess blood on its hands, the statute interferes with that exercise of the freedom of speech under the First Amendment."

In the dissenting opinion, Judge Sri Srinivasan argued that the SEC rule should be subject to rational review and that the compelled speech — "not DRC conflict free" — was both factual and uncontroversial. Srinivasan claimed that the conflict minerals rule was no different than USDA's COOL rule because both provide origin-related information and both use terms that are defined in law.

"It is hard to see what is altogether different about another species of 'geographical origin' law requiring identification of products whose minerals come from the DRC or adjoining countries," the dissent said. Srinivasan also argues that "controversial" only relates to a disagreement of whether information is factual. Because the language is factual, Srinivasan said, it is not controversial.

On the matter of scrutiny, Srinivasan says that "[n]o other court has ever identified" the rational review test as only applying to compelled speech that relates to advertising.

This view contrasts with the majority's opinion that the Supreme Court intentionally tailored its ruling in a case known as *Zauderer* to apply the more permissive standard only in those cases. The majority cites the high court's ruling in the *Zauderer* case because it specifically mentions "advertising" throughout its ruling, which Srinivasan claims was only due to the specifics of the case rather than the scope of the ruling.

The dissenting opinion also argued that the rule would pass even the stricter level of scrutiny because it directly advances the government's interest in informing consumers about the origin of the minerals used in products they may buy.

In a statement to *Inside U.S. Trade,* NAM, one of the appellants in the case, said it hopes this decision would lead to the repeal of extensive supply-chain reporting requirements that have been in effect since last year.

"We believe it is unreasonable to require companies to continue to spend substantial resources implementing the SEC's rule when its central feature has been invalidated on constitutional grounds," the statement said. "Therefore, we believe the SEC and Congress should reexamine this approach of the Dodd-Frank Act and rule in light of the court's decision."
