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Conflict Minerals Update – SEC Releases Guidance Following District Court Decision

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On April 3, 2017, the US District Court for the District of Columbia (the "Court") entered a final judgment in *National Association of Manufacturers, et al. v. Securities and Exchange Commission*,[1] ruling that Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Rule 13p-1 under the Securities Exchange Act of 1934 (the "Exchange Act") and Form SD violate the First Amendment of the US Constitution to the extent that the statute and the rule require companies to report to the Securities and Exchange Commission (the "SEC") and state on their websites if any of their products "have not been found to be 'DRC conflict free.'" The Court invalidated this portion of the rule and remanded to the SEC to take appropriate action in furtherance of the Court's decision.

In response to this ruling, on April 7, 2017, the staff (the "Staff") of the SEC's Division of Corporation Finance ("Corp Fin") issued a statement[2] containing guidance for companies preparing their Form SD filings for calendar year 2016, which are due May 31, 2017. In this statement, which updates Corp Fin's 2014 guidance, the Staff announced that it will **not** recommend enforcement action if a company only includes disclosure in Form SD concerning the "reasonable country of origin inquiry" ("RCOI") (under Items 1.01(a) and (b)) and does not include disclosure relating to due diligence on the source and chain of custody of conflict minerals or a Conflict Minerals Report and associated Independent Private Sector Audit ("IPSA") (under Item 1.01(c)). Item 1.01(c) requires that if the company knows, or reasonably believes, based on its RCOI, that any of its necessary conflict minerals originated in the Democratic Republic of Congo or an adjoining country and are not from recycled or scrap sources, the company must (i) exercise due diligence, including obtaining an IPSA, on the source and chain of custody of its conflict minerals, and describe the due diligence conducted in the Conflict Minerals Report attached as an exhibit to its Form SD and (ii) describe its products that contain necessary conflict minerals, the facilities used to process the necessary conflict minerals, the country of origin of the necessary conflict minerals, and the efforts to determine the mine or location of origin with the greatest possible specificity. While Corp Fin's 2017 guidance appears to provide significant relief for companies subject to these reporting requirements, the Staff noted that its statement remains subject to further action by the SEC, is related to enforcement action only, and is not a statement of a legal conclusion. This differs from Corp Fin's 2014 guidance, which outlined specific instructions for what the SEC expected to see in company filings submitted under the relevant rules.

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1 *Nat'l Ass'n of Mfrs., et al. v. SEC*, No. 13-CF-000635 (D.D.C. Apr. 3, 2017).

2 Available at https://www.sec.gov/news/public-statement/corpfin-updated-statement-court-decision-conflict-minerals-rule

Also on April 7, 2017, Acting SEC Chairman Michael Piwowar issued a public statement[3] in which he noted that, because the primary function of the extensive requirements for due diligence on the source and chain of custody of conflict minerals set forth in Item 1.01(c) of Form SD (including the IPSA requirement) is to enable companies to make the "DRC conflict free" disclosure found to be unconstitutional,"it is difficult to conceive of a circumstance that would counsel in favor of enforcing Item 1.01(c) of Form SD."

Effect of the Corp Fin Guidance on May 31, 2017 Conflicts Minerals Filings

Unfortunately, Corp Fin's recent guidance does not provide clear relief from reporting obligations, but merely indicates that the Staff would not recommend enforcement action against companies that do not include the information required by paragraph (c) of Item 1.01 of Form SD. It also does not conclusively resolve the ultimate scope or application of the conflict minerals rule. Nevertheless, the guidance reaffirms that companies that do not voluntarily choose to label their products as "DRC conflict free" would not be expected to conduct an IPSA.

While choosing not to provide a Conflict Minerals Report would eliminate a substantial reporting burden, as a practical matter, most companies are likely far along (or have completed) their RCOI and due diligence related to calendar year 2016. Furthermore, affected companies should take into consideration investor perception of a scaled-down disclosure. In this context, it is worth noting that NGOs, activists and certain investors may continue to expect conflict minerals disclosure regardless of any SEC enforcement decision. Additionally, companies may need to take into account the views of key customers with respect to product sourcing when contemplating revisions to their conflict minerals disclosure approach and policies. Finally, as a technical matter, the conflict minerals rule itself has not been amended and Corp Fin's current enforcement position is not controlling on the courts, and thus companies remain subject to private causes of action under Section 18 of the Exchange Act for misleading statements in a Form SD, which is "filed" rather than "furnished" with the SEC.

On balance, in light of the foregoing considerations and in the absence of definitive clear relief from the SEC, and given the timing of Corp Fin's statement, most reporting companies are likely to keep their reporting approach unchanged pending additional guidance or rulemaking initiatives.

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[3] Available at https://www.sec.gov/news/public-statement/piwowar-statement-court-decision-conflict-minerals-rule