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DODD-FRANK’S CONFLICT MINERALS RULE: THE TIN EAR OF GOVERNMENT-BUSINESS REGULATION

HENRY LOWENSTEIN*

From 2007-2012 the United States encountered its longest and deepest economic recession since the 1930’s. Most analysts attribute the economic contraction’s proximate cause to a systemic meltdown in the national and world financial markets. This occurred due to the convergence of government policy stimulating irrational lending practices in real estate (sub-prime mortgages), weak financial instruments based upon them along with hedge fund manipulations and questionable if not fraudulent practices of major financial institutions.1 Major financial institutions risked insolvency, required government intervention2 and some such as the venerable financial house, Lehman Brothers, went out of business altogether.

Out of investigations and resultant public political pressure, Congress enacted the most sweeping banking and financial service market structural reforms since the Glass-Steagall Act of 1933.3 Thus, came about the lengthy and controversial Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.4 Not unlike other legislation by Congress, deep within it’s over 2,300 page of statutory text were provisions having nothing to do with the financial services market or any cognizable theme of the legislation itself.

This paper examines one of those unrelated provisions, which have recently come to light with recent realization of its potential massive adverse impacts on business, manufacturing, and ultimately consumer costs of products. Buried within Dodd-Frank’s statutory text is Section 1502, known as the “Conflict Minerals Provision”5 (later developed into a “rule” and hereafter “CMR”). The provision establishes a requirement that

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2 Primarily the U.S. Treasury TARP Program (Troubled Asset Relief Program). See Emergency Stabilization Act, P.L. 110-34 (2008). TARP was an over $1 billion purchase by the U.S. government of financial institution assets to retain their institutional liquidity.


5 Id. § 1502.
manufacturers who are publicly listed corporations trace, certify and report the origins and use of four specific minerals, gold and the “Three T’s” (tin, tungsten and tantalum) used in modern day manufacturing to verify they did not originate from mines in the “Democratic Republic of Congo (formerly Zaire) or adjoining countries.”\textsuperscript{6} These minerals are collectively known as so called, “Conflict Minerals.”\textsuperscript{7} The law neither bans the purchase, import or use of these minerals from the identified nations. Rather, it is (at this point) limited to reporting, but as this article will outline, that reporting is neither benign in its effect nor limited in its cost burden to industry.

The law further delegated regulations and enforcement of CMR not to an existing federal regulatory agency most qualified in expertise and oversight of minerals or natural resource or import-exports, but to the U.S. Securities and Exchange Commission (SEC); a financial regulatory agency with no prior mission or expertise in any aspect remotely related to the subject matter jurisdiction imposed by Congressional mandate.\textsuperscript{8} This was done at a time when the SEC is overwhelmed with financial market cases from its existing mission, \textit{Dodd-Frank} financial market mandates, and the effect of 2013 federal budgetary sequestration reducing all agency budget resources.

Congress’s choice of mechanism for §1502 raises serious questions about the legality of the law, the method chosen to address the issue, matters of equal protection of American firms and industries, the financial burden placed on both the SEC and businesses at a time of recession and public outcry (both among those against regulatory interference in Commerce and by those who approve of it), better effectiveness and efficiency in regulatory oversight. Indeed, at a time when both parties in Congress and the Executive branch agree in principle of the need to improve effectiveness and efficiency of government, the Conflict Minerals Rule presents one example of a “tin ear” in public policy and business law.

\textsuperscript{6}\textit{Id.}

\textsuperscript{7} The term “conflict mineral” is defined in Section 1502(c)(4) of the Act as (A) columbite-tantalite, also known as coltan (the metal ore from which tantalum is extracted); cassiterite (the metal ore from which tin is extracted); gold; wolframite (the metal ore from which tungsten is extracted); or their derivatives; or (B) any other mineral or its derivatives determined by the Secretary of State to be financing conflict in the Democratic Republic of the Congo or an adjoining country. U.S. Securities and Exchange Commission, “Final Rule: Conflict Minerals,” 17 C.F.R. Parts 240 and 249b [Release No. 34-67716, File No. S7-40-10], August 22, 2012. [Hereafter, referenced as “CMR”]. at footnote 6. We reference in this paper from the original release. The Conflicts Mineral Rule was subsequently published in the Federal Register on September 12, 2012, see F.R. 77 (177) 56274 et. seq.

\textsuperscript{8} For example, the U.S. Government has agencies with better regulatory fit such as Commodity Futures Trading Commission, U.S. Department of Commerce, U.S. Customs Service, U.S. Department of Energy, U.S. Department of Interior or perhaps even the U.S. Geological Survey among others.
Public policy debates often assert the inefficiency, cost burden and even illogical processes that occur in government regulation of business have the effect of delaying innovation, diverting management energy and adding deadweight costs to both the cost of production and the operation of government itself. The Conflict Minerals Rule presents us with the perfect storm object lesson on the perils of poorly defined government regulation, well meaning in its intent, but functionally expensive, irrational and inoperative in its implementation.

In this article we will discuss how the convergence of the CMR’s deficiencies add to costs of business, inefficiencies in the regulatory structure, conflict with constitutional rights, legislative intent-statutory provisions; all producing a chaotic mix which serves to not only fail to achieve the purported public policy goal Congress established, but actually exacerbate the very human rights situation at issue. The CMR presents a case study in point of the long-standing historical observation that government makes for poor businessmen and businesses poor foreign policy diplomats.

This article will first provide an overview of the Conflicts Minerals Rule, the recent SEC implementation rules and its impact on business. In the second part, we examine the legal challenges to the law, many of which are already before the U.S. Court of Appeals for the District of Columbia Circuit in the National Association of Manufacturers (NAM) v. SEC, its initial hearings being scheduled for May 2013.

Finally, we discuss conclusions and unintended consequences even now observed as the rule nears implementation.

I. THE CONFLICTS MINERALS RULE: A CONFLICT OF POLICIES

The famous American journalist and social critic, H. L. Mencken (“Sage of Baltimore”), ever skeptic of government once remarked, “The urge to save humanity is almost always a false front for the urge to rule.”

Whether out of humanitarian motives, or, a Mencken-alluded desire for economic control, Congress added §1502 into the Dodd-Frank Act to address its concerns with adverse humanitarian conditions in one African nation e.g. the Democratic Republic of Congo (“hereafter DRC”). In so doing, Congress posed a new and perhaps unprecedented sea change direction in traditional Federal business regulatory policy by implementing selective foreign policy

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9 National Association of Manufacturers, Chamber of Commerce of the United States of America and Business Roundtable v. Securities and Exchange Commission, Amnesty International USA, Amnesty International, LTD, Case No. 12-1422, D.C. Cir., January 13, 2013. (Hereafter, referenced as “NAM”) [Author’s note: Final arguments were heard by the D.C. Cir. on January 7, 2014; decision pending at the time of writing of this article.]

and its attendant costs exclusively and directly upon publicly traded companies.

It further delegated oversight to non-traditional regulatory agencies. Historically, U.S. regulatory structure placed oversight over federal mandates in the hands of agencies with specific subject matter, technical or legal expertise over the issue regulated. Thus, for example, the former Interstate Commerce Commission regulated railroads (later adding pipelines); The Federal Aviation Administration regulates aviation. All expertise in nuclear minerals, materials and related atomic energy matters is given to the Nuclear Regulatory Commission (NRC).

The Conflict Minerals Rule, however, presents a regulatory anomaly. Here the rule governs manufacturers (and only those in publicly-listed firms), over very narrow selected (one might opine arbitrarily-selected) list of raw materials, solely at this point for information purposes. The rule is delegated to a regulatory agency lacking subject matter mission, expertise or resources to implement; the U.S. Securities and Exchange Commission (SEC); its mission explicitly regulatory over financial markets and their operation.

The mission of the U.S. Securities and Exchange Commission is to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.

11 Note: Dodd-Frank does include two other specialized corporate disclosures of a non-traditional, non-financial market nature to the SEC under Title XV. Section 1503 requires public disclosure of mine safety issues, violations and orders issued to domestic mines under the U.S. Mine Safety and Health Administration (MSHA), and, Section 1504 requires corporations engaged in oil and natural gas development to annually report on (legal) payments made to the U.S. or any foreign government entity. However, both these provisions have a direct material impact on investors and thus are consistent with the Commission’s stated mission. See: “Dodd-Frank Act Rulemaking: Specialized Corporate Disclosure,” U.S. Securities and Exchange Commission, (http://www.sec.gov/spotlight/dodd-frank/speccorpdisclosure.shtml) (last visited October 12, 2012).


13 Federal Aviation Act, 72 Stat. 731 (1958) (Successor legislation to Air Commerce Act, 44 Stat. 568 (1926) and Civil Aeronautics Act, 52 Stat. 973 (1938)).


A. What is the Conflicts Minerals Rule (Section 1502)?

The purported public purpose for the Conflict Minerals Rule (CMR) will be discussed shortly. At the outset, however, let us describe in summary the compliance mandate of the rule, itself. In August, 2012 after extraordinary public comment, the SEC issued an over 300 page final rule and explanatory notes, promulgating a three phase process for reporting the origins of the four designated minerals (aka “Conflict Minerals”) to disclose whether their origins are from the DRC or adjoining countries (aka “conflict countries”).

Step One requires companies to determine if the conflict minerals used are “necessary to the functionality or production of the product.” If not, no disclosure is required and the company need not go further with its analysis or reporting diligence.

Step Two requires that a company using the designated minerals make a “reasonable inquiry” into its country of origin. The firm then reports whether: (a) they know the materials were not from a conflict country; (b) have reason to believe they are (or are not) from a conflict country, or, (c) the materials came from scrap or recycled materials were the origin of the mineral is unknown.

Step Three requires the company to conduct a substantial due diligence on the source and chain of custody of the conflict minerals, based on an internationally established framework. The resulting report must be audited independently and the entire report and process reported separately from the annual 10-K report to the SEC by a new form, Form SD, on a calendar year basis. The SEC has exempted all stockpiles of materials purchased prior to 2014.

Both the statute and rule provide no prohibition on purchases of conflict minerals from the DRC or elsewhere, no penalties, criminal or civil, and no other legal sanctions direct or implied. Thus, while Congress saw fit to raise the DRC’s human rights problems to this statutory level, it nevertheless left it perfectly legal to continue trade and commerce in the metals in question.

The law and the rule’s purpose in theory is to attempt by public disclosure to embarrass companies from using materials of DRC origin, thus putting a chilling effect on future purchases and consequently restraining revenue to bad actors in the DRC who are causing human rights violations.

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17 Exchange Act, supra note 15, § 13(p) and SEC implementation regulations, 17 C.F.R. Parts 240 and 249b et. seq.
18 Id.
19 Id.
20 Id.
The only penalty is that which the law current grants the SEC for failure to file reports under the Exchange Act.\textsuperscript{21}

Each of CFR steps contains subcategories and an actual serpentine flow chart (displayed in Exhibit A) within the SEC rule and reproduced herein.\textsuperscript{22} As will be discussed, the terminology is often vague, ill defined or undefined, to the point of effectively precluding any rational implementation to industry or the SEC despite the SEC’s own best efforts to do so.

B. Scope—Public Objectives: General Overview

As an initial point of analysis, there is no question that the rule clearly falls within Congress’s enumerated power under the \textit{Commerce Clause} to regulate interstate and foreign commerce.\textsuperscript{23} Moreover, that the Conflict Minerals Rule is well meaning as an expression of national human rights policy there can be no doubt. Congress was concerned about the horrible violence and outrageous violation of human rights by armed groups in the Eastern Congo, uncontrolled by DRC’s central government and the resultant corrupt funding of their atrocities in the mining and trade of minerals. The U.S. General Accountability Office (GAO) found over 9\% of DRC’s population negatively impacted from these conditions over 2009-2010.\textsuperscript{24} All parties in the debate certainly stipulate that the human rights conditions in the DRC are dreadful and the opponents of CMR have no issue with public policy to address it; on its face.\textsuperscript{25}

Congress was heavily lobbied by non-government organizations such as Amnesty International, Global Witness among others. With forthcoming elections and desires of a number of Congressmen, the Dodd-Frank law in legislative process at the time became merely a convenient vehicle to attach this rule. Buried in the law’s massive text, CMR escaped public and industry scrutiny finding itself fairly insulated from isolation and removal.

That said, a threshold problem of the law is apparent from the outset. That is the human rights conditions enumerated in the DRC are not exclusive to the DRC. In fact, on the U.S. State Department’s list of nations with human rights abuses the DRC is not at the top. In fact, the DRC does not

\textsuperscript{21} \textit{Id.} § 13 (a) et. seq. (penalty is limited to civil fines for failure to file).
\textsuperscript{22} CMR, \textit{supra} note 7, et. seq.
\textsuperscript{23} U.S. Const. art. I., sec. 8, cl. 3.
\textsuperscript{25} Brief for National Association of Manufacturers, et.al, as Amici Curiae (\textit{Experts on the Democratic Republic of The Congo}) Supporting Petitioners, NAM, \textit{supra}, note 9, Document No. 1416913 at 1-7 (hereafter, “Experts Amicus Brief”), provides a short history of the violence and origin of violence in the DRC.
even make the list of Freedom House’s annual “Worst of the Worst” Repressive Societies List.\textsuperscript{26} Moreover, as we will discuss in the article, nations of worst human rights abuses that are major producers of the Conflict Minerals are not subject to the law.

C. Conflict Minerals in Industry and Society

It is well recognized in our Twenty-First Century that advances in technology have caused industry to depend on trade to obtain a host of key minerals and “rare earth materials” necessary for modern products. The minerals chosen in §1502 fall squarely in this category. Unfortunately, when the universe and planet earth was formed the location of these mineral deposits recognized no national boundaries, and, as often has been the case, ended up within the borders of nation states of questionable ethical and moral repute.\textsuperscript{27}

Tantalum is a necessary element used in mobile telephones, computers, digital phones, televisions, automotive electronics and related electronic devices as well as carbide tools and jet engine components. It is a significant component used in high precision medical implants and prosthetic devices.\textsuperscript{28}

Tin also is essential to electronic circuits, alloys, metal plating and solders as well as traditional uses in cans and containers.\textsuperscript{29} Tin, once considered a low value metal used in among other things canning, has become an essential element in solder used to connect circuits in the most widely used consumer electronics and specialty electronics. For example, an Apple Ipad (tablet) uses 7,000 solder points of tin solder. A flat screen TV contains 4.8 grams of tin solder, the typical smart phone over 3 grams.\textsuperscript{30}

Tungsten is used in metal wires, electrodes, lighting contacts, electronics, aerospace components, heating, ball point pens, automotive and


\textsuperscript{27} The situation is reminiscent of the often quoted remark of the late Golda Meir, Prime Minister of Israel (1898-1973) commenting on the presence of oil in many unstable countries, “Let me tell you one thing I have against Moses. He took us 40 years in the desert in order to bring us to the one place in the Middle East that has no oil.” \textit{Prime Minister Speech} 1973.


\textsuperscript{29} \textit{Id}.

\textsuperscript{30} Cam Simpson, \textit{Tech’s Tragic Secret}, \textit{BLOOMBERG BUSINESSWEEK}, Aug. 27-Sept. 2, 2012, at 52. (Five Apple I-pad electronic tablets consume as much tin solder as is found in the average 4,000 pound automobile).
welding applications. It is found in golf clubs, medical devices and window heating systems.31

Gold needs no introduction. Beyond its jewelry, ornamental and monetary uses, gold is used in electronic components in communication, aerospace and medical devices; among uses in other high technology devices and components.32 Hence these minerals find themselves in a host of products from ubiquitous household items to the most sophisticated high technology products and applications.

The key conundrum posed by the CMR of course is that the Democratic Republic of Congo (DRC) (or its “adjoining nations”) is not the only nation that is adversely affected by human rights “bad actors” for whom, at least at this time, the DRC government lacks capacity to control. Other world nations presenting like extraordinary social problems by government sanctioned actions or independent actors are not covered under this legislation nor are the four minerals enumerated confined exclusively to socially responsible nations. In fact the record shows quite the contrary. If there exist other, yea, even worse human rights abusive nations supplying these materials, then why confine this commercial law to this single bad actor state and not others? Thus, a key legal question is why a “compelling state interest” to the DNR and no others?

The disparity in public policy present is so extensive as to lack clear and convincing reasoning from Congress. The answer to this question leads us to the issue of arbitrary selection as one basis of legal challenge to the rule under the federal administrative law’s arbitrary and capricious doctrine.33 As we will see in the next section, §1502’s statutory deficiencies as well of those of SEC’s implementation rule, leave the law subject to a host of legal challenges.

II. REGULATORY MIASMA: LEGAL AND PRACTICAL CHALLENGES TO THE CONFLICT MINERALS RULE

The Conflict Minerals Rule poses a host of legal complications that are pending judicial review. In this section we outline key areas problematic to the statutory language and regulatory implementation of CMR. Some, but not all of these issues have been raised in the pending NAM case.

31 Id. (Most consumers know tungsten as the filament element within conventional incandescent light bulbs.)
32 Id.
33 There should be a clear error of judgment; an action not based upon consideration of relevant factors and so is arbitrary, capricious, an abuse of discretion or otherwise not in accordance with law or if it was taken without observance of procedure required by law (Natural Res. Def. Council, Inc. v. United States EPA, 966 F.2d 1292, 1297 (9th Cir. 1992)).
A. The SEC as Administrator, Rulemaker and Enforcer of the Conflict Mineral Rule

On first impression courts would certainly recognize the questionable aspect of delegating the U.S. Securities and Exchange Commission (SEC) for the objectives and task of making operational the CMR. Given the Commission’s established mission, expertise and resources, the SEC appears to be a demonstrably improper forum for the regulation. This is because the SEC’s scope of jurisdiction is limited to publicly listed corporations on U.S. stock exchanges. Its expertise is primarily financial.

Privately held corporations are outside the jurisdiction of the SEC and the CMR. Thus, the rule has no application to non-exchange listed firms. In the global marketplace, multi-nationals have the ability to shift the nationality of subsidiaries and manufacturing to entities outside U.S. long arm statutes or jurisdiction of U.S. public exchanges escaping the law, leaving the reporting burden primarily upon small domestic manufacturers. The rule and its cost and productivity implications create a substantial unleveled playing field for manufacturers. The exclusion of private firms is irrational.

The SEC, itself, is ill equipped to monitor compliance, its staff primarily skilled in securities markets and financial regulation. The agency’s focus over the years has been expertise in legal, accounting, and cyber systems, specifically focused to keeping capital markets open and honest. Since the collapse of Enron in the 2000’s and the enactment of the first major modern financial industry reform, the Sarbanes-Oxley Act (2002), the SEC has been challenged with major demands incongruent with its staffing and budget.

In the light of the fallout from the 2008 financial collapse and recession, the agency is further overwhelmed with rule marking, enforcement and compliance matters to its core mission on top of those financial duties imposed by Dodd-Frank’s other provisions. Delegating the CMR rule to the SEC is analogous to government mandating that a cardiac patient be seen by an ophthalmologist on the basis that they are both medical doctors!

One aspect of CMR provides an object case in point. Under the CMR, reports are required where the conflict minerals uses are “necessary to the functionality” of the product. Defining functional necessity is an engineering question in most cases. Who decides whether a metallic cover inclusive of tungsten is “necessary to the functionality” or merely packaging and appearance design in which case it is not a “functional’ part. This

36 Id.
would require the SEC to hire expensive engineers or contract with engineering consultants where firms challenge their reporting requirement. Likewise is the term “necessary to the production” where a conflict mineral may not be a part of the product but part of the production process. The SEC lacks such technical expertise and to date any reasonable resources to do so. Hence, the delegation in itself appears arbitrary to the point where it ensures the rule constructively cannot be enforced.

In FY 2010 the entire budget for the SEC was slightly over $1.3 billion of which nearly 60% was dedicated to securities market enforcement and examination. In 2013, the SEC is taking the same 2.3% across the board cut under 2013 budget sequestration as all Federal agencies as well as Congressional efforts to further reduce its budget.

The Dodd-Frank Act’s financial provisions alone add to the agency’s regulatory tasks. The Wall St. Journal reported in May 2011 that both the statutory language and implementation regulations for the Dodd-Frank Act governing the financial industry (among other visual analogies) were equivalent to 21.2 times the height of the Statue of Liberty or 2.6 times the height of the Empire State Building.

The United State confronted with a Federal budget deficit in FY 2012 of over $1 trillion and a Federal debt of over $16 trillion, regardless of political party in power, reductions in government spending will occur. To date Congress has shown no willingness to substantially increase the Commission’s resources.

Hence, the SEC will be forced to make priorities. In the conflict between its primary statutory duty to securities markets and the CMR, it is more likely than not the CMR will be relegated to the back burner of enforcement if not lose out altogether. Consequently, businesses will have incurred large costs of reporting and its attendant diversion of staff resources to no public benefit, placing U.S. industries at a greater competitive disadvantage in the marketplace. The SEC faces the challenge of being a depository of millions of reports unprocessed or read

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37 Michael J. Ryan, *U.S. Capital Markets Competitiveness: The Unfinished Agenda*, U.S. CHAMBER OF COM., Washington, DC, Summer 2011, Figure 4 at 18.
40 In fact at the time of this writing the SEC faces the mandated 2.3% across the board budget cut required by Congress’s Budget Sequestration schedule to go into effect February 28, 2013. Such a budget cut would further debilitate the SEC from carrying out its statutory mission.
B. Arbitrary and Capricious Standard to Public Policy

A threshold issue in CMR is its isolation of the DNR for reporting purposes while ignoring substantially larger producers of conflict minerals who have demonstrably worse human rights records. This raises a key issue of CMR failing to meet the *arbitrary and capricious standard* the court’s hold to regulatory actions.

Current conceptions of “arbitrary and capricious” review focus on whether agencies have adequately explained their decisions in statutory, factual, scientific, or otherwise technocratic terms. Courts, agencies, and scholars alike, accordingly, generally have accepted the notion that influences from political actors, including the President and Congress, cannot properly help to explain administrative action for purposes of arbitrary and capricious review.41

This standard has been long held under the *Administrative Procedures Act*42 and its subsequent judicial rulings which established the “Hard Look” rule in agency regulatory review.43 The *Hard Look Doctrine* arises out of the case *State Farm v. National Highway Traffic Safety Administration (NHTSA)* (1983).44 This doctrine for the most part continues in judicial review. For example in *Massachusetts v. EPA* (2007), the Supreme Court reversed the Environmental Protection Agency (EPA) on the grounds that the rule in question was made with and based upon no scientific or expert basis.

Regulatory agencies have often depended on the defense afforded by *Chevron v. Natural Resources Council*45, to uphold their rulemaking against the Arbitrary and Capricious Doctrine. Here court deference is given if: (1) Congress spoke to the precise question at issue, and (2) if the statute is silent or ambiguous on the specific issue, is the regulatory construction permissible under the statute?46

42 5 U.S.C. §706(2)(A)-(C), “shall hold unlawful and set aside agency action when found to be arbitrary.”
46 *Id.* at 842, *see also* Wright v. Everson, 543 F.3d 649 (11th Cir. 2008).
Nevertheless, *Chevron* does not give infinite leave to Congress or agencies to promulgate laws and rules that lack objective standards or expertise. It is here that the CMR fails even the most liberal test. For example, let us examine the situation in the designated conflict mineral, Gold.

The DRC is not the largest producer of gold with unconscionable human rights conditions. According to the U.S. Geological Survey, the DRC in fact is #77 in gold production. Of much higher production are nations of highly questionable human rights issues and listed on the U.S. State Department’s list of human rights violators. These nations include: Peoples Republic of China (#1), Russia (#4), Uzbekistan (#10), Zimbabwe (#23), Iran (#66), Cuba (#69), and Myanmar [Burma] (#76). Likewise, both in Tin and Tungsten, the largest producers, particularly the Peoples Republic of China and Russia are market leaders in production list with other non-African problematic human rights-issue nations also producers. Clearly, turning a blind eye to the two largest producers (Russia and China) are purely political factors, not objective economic ones which would appear impermissible, not withstanding scrutiny under the *Hard Look* rule.

Tin poses a clear question in this regard. A major 2012 investigative expose by *Bloomberg Businessweek*, detailed the tragic and horrifying conditions in the tin mines of Bangka-Belitung Province of Indonesia that produce in excess of 30% of the world’s tin ore. Indonesia, however, is not on the human rights abuse list and is an ally of the United States. 40% of world tin ore comes from the Peoples Republic of China, not an ally of the United States and high on the list of human rights abuses, but not subject to the CMR rule.

While the CMR rule applies strictly to reporting on gold and “The Three T’s,” there is genuine risk that unchecked, the rule could be expanded out to other minerals, especially those in high demand by high technology companies. For example, the electronics industry is dependent on a host of minerals generally classified as “Rare Earths” such as yttrium, (necessary for important electronics such as cell phones and medical uses).

Here one finds the Peoples Republic of China to be the single dominant world producer. In short, if the public policy goal is human rights the singling out of just one small African nation and a number of “adjoining” countries which may or may not remain on the U.S. State Department

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49 Simpson, *supra* note 30, at 52.
50 Id.
Human Rights watch list in any given year, while excluding nations demonstrably higher on the State Dept. list raises the question of impermissible arbitrary state selection, certainly suspect classification. This then adds to the fact that a substantial business cost is imposed on an arbitrary selection of industry to report mineral origin.

What is the “compelling state interest” for DRC versus other alleged abusive human rights states? These questions are ultimately to be solved by the federal courts or a subsequent re-consideration of the rule by Congress, itself.

C. Rational Basis Test—Vagueness and Equal Protection

Close on the heels of both the questionable regulatory delegation and the arbitrary & capricious doctrine issues is the very serious matter of CMR failing the judicial rational basis test. Coupled with this factor is the extraordinary vague and ill-defined language of the statute and rule along with its failure to provide equal protection under the law to industry, both raising Constitutional Fourteenth Amendment issues.51 We take these together as they are interrelated. Technology corporations such as Microsoft, General Electric and Motorola Solutions, adversely affected by the CMR are already signaling intent to challenge the legality of the SEC rules52 and the pending NAM case may not be the only legal challenge facing the law.

1. Rational Basis Test.

The Rational Basis Test has long been a judicial review staple but one with a very high bar for challengers to overcome. Simply defined, when the government engages in commercial regulation (or that of individuals), it is subject to a Rational Basis Test for its decisions. The judicial test requires the government regulation to bear some rational relation to the state interest and not merely be an arbitrary selection or selective enforcement that compromises equal protection rights of similarly situated entities.53

Under rational basis test for constitutionality, primary issues are whether government has power or authority to regulate particular area in question and whether method that government has chosen

51 U.S. Const. amend. XIV, et. seq.
to accomplish that goal bears rational relation to ultimate objective.  

Over time, this test has been interpreted by the Court as a high bar with deference paid to the government and burden of proof to challengers. However, the court in its application demands very clear objectively based rationality for such classifications. For example from rational basis analysis in Romer:

In order to reconcile the Fourteenth Amendment's promise that no person shall be denied equal protection with the practical reality that most legislation classifies for one purpose or another, the Court has stated that it will uphold a law that neither burdens a fundamental right nor targets a suspect class so long as the legislative classification bears a rational relation to some independent and legitimate legislative end.

In enacting §1502 at best the most logical and rational of approaches by Congress would have been to simply require reporting of the use of Conflict Minerals ONLY by those firms who actually purchase the targeted materials from DNR (or other subject nations) and to apply the rule to all similarly situated entities regardless of form of ownership. As the law now stands every public corporation must prove a negative, an anathema to the American legal system concept.

Under §1502 and its recently promulgated SEC implementation rules, only those companies subject to the Exchange Acts, i.e. publicly traded companies, are subject to the Conflict Mineral Rule. Consequently, firms that are privately owned, or publicly owned foreign transplant manufacturers not listed on United States stock exchanges or government-owned corporations are exempt from the rule.

Given the stated purpose of CMR, those American companies covered under the rule are segregated into an arbitrary class and placed in material competitive-cost disadvantage in the marketplace with private (or otherwise non-listed) competitors. The SEC estimates those subject to the rule to be 266,175 companies of which 262,524 (98.6%) are defined as small businesses (those employing 500 or less workers). The rule raises legal

54 Cash Inn of Dade, Inc. v. Metropolitan Dade County, 938 F.2d 1239 (11th Cir. 1991) (emphasis added).
57 CMR, supra note 7, at 7.
58 Id.
questions of Equal Protection, given the large number of manufacturers not covered by the reporting mandate in the same industries competing under the same circumstances.

A demonstration of this situation can be viewed by examining Forbes’ annual list “America’s Largest Private Companies.” Of the top 100 corporations on the list, fully twenty-five are major manufacturers or suppliers who would be potential users of conflict minerals. Below is a sample including rank and revenue:

<table>
<thead>
<tr>
<th>Rank</th>
<th>Company</th>
<th>Revenue</th>
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<tbody>
<tr>
<td>#2</td>
<td>Koch Industries</td>
<td>$109 billion</td>
</tr>
<tr>
<td>#5</td>
<td>Bechtel</td>
<td>27.9 billion</td>
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<tr>
<td>#25</td>
<td>Tenaska Energy</td>
<td>9.95 billion</td>
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<tr>
<td>#26</td>
<td>Kiewit Construction</td>
<td>9.94 billion</td>
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<tr>
<td>#29</td>
<td>SC Johnson &amp; Son</td>
<td>9.00 billion</td>
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</tbody>
</table>

Both the isolation of one nation producing the conflict minerals and the application of the CMR to only publicly listed companies, clearly raises the specter of suspect classifications. In *Moreno*, Justice Brennan made clear: “A bare congressional desire to harm a politically unpopular group cannot constitute a legitimate governmental interest such as will sustain a legislative classification against an equal protection challenge.”

In *Nordlinger*, the Supreme Court made clear that equal protection under the 14th Amendment does not preclude classifications. However, it merely prohibits governmental decision makers from “treating differently persons who are in all relevant respects alike.”

Likewise, the Supreme Court has stated in the past that social and economic suspect classifications that impinge on fundamental rights cannot survive a rational basis test where there is clear showing of arbitrariness and irrationality in the classification selection. The *Hard Look* test suggests that Congress cannot articulate an objective, factual, and non-political reason for CMR’s suspect geographical classification.

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59 *Americas Largest Private Companies 2011*, FORBES (November 16, 2011). (In prior years #3 domestic automaker, Chrysler Corporation also was on the private company list. Its estimated revenues were approximately $55 billion).
60 U.S. Dep’t of Agric. v. Moreno, 413 U.S. 528 (1973).
D. Equal Protection and Vagueness

The *Rational Basis* test further brings us to the issue of the equal protection issue as can be seen in the electronics market directly impacted. Dell Computer, one of the world’s largest producers recently announced a stock buyback to go private.\(^{63}\) Hence, Dell would now be exempt from the rule creating an equal protection and anti-competitive issue for Dell’s primary publicly listed competitors such as Hewett-Packard (HP) and IBM. Likewise, in the automobile industry, both General Motors and Ford are publicly listed companies, Chrysler is not. Thus, two of the “Big Three” American motor vehicle manufacturers, Ford and General Motors, are placed on an inequitable footing with the third, Chrysler. Neither of these cases can pass muster under a rational basis examination relative to the stated objective of Congress in stemming commerce with the DNR in conflict minerals.

Another related major issue is the continuing vague language of the provision and its implementation regulations to date. It is often the case that laws and regulations have verbal ambiguities that can be corrected through contextual interpretation. It is quite another situation when the text of a regulation is legally vague, i.e. where the actual meaning is so uncertain as to defy definition; more precisely the uncertainty causes such complexity as to make for impracticality in operation.\(^{64}\)

Even in its revised rules, the SEC after voluminous public comment cannot operationally define to any reasonable certainty what constitutes material terms in CMR such as “necessary to the functionality,” who is really a “manufacturer,” or “contract to manufacturer,” all of which are essential to carrying out the statutory language of §1502. Defining for example, “adjoining nations” is left to a State Department list that is in an annual state of flux, even changing during the calendar year period for this regulatory reporting. Firms could face an annual moving target.

As but one demonstration of the point, let us look at the SEC definition of the key term “necessary to the functionality.”

In determining whether a conflict mineral is “necessary to the functionality” of a product, an issuer should consider: (1) whether

\(^{63}\) Michael J. De La Merced & Quentin Hardy, *Dell is $24 Billion Deal to go Private*, N.Y. TIMES, (Feb. 5, 2013) http://dealbook.nytimes.com/2013/02/05/dell-sets-23-8-billion-deal-to-go-private/.

\(^{64}\) Antonin Scalia & Bryan A. Garner, *Reading Law: The Interpretation of Legal Texts*, (Thompson/West, 2012) at 31, 33. Vague terminology is even more problematic where its reasonable meaning cannot be sustained by the “Fair Reading” Method, i.e. “determining the application of governing text to given facts on the basis of how a reasonable reader, fully competent in the language, would have understood the text at the time it was issued.” Id. at 34 (emphasis added).
the conflict mineral is intentionally added to the product or any component of the product and is not a naturally-occurring by-product; (2) whether the conflict mineral is necessary to the product’s generally expected function, use, or purpose; and (3) if conflict mineral is incorporated for purposes of ornamentation, decoration or embellishment, whether the primary purpose of the product is ornamentation or decoration.  

Nevertheless, even with a high burden placed upon plaintiffs who allege rational basis defects, Congress has an affirmative duty to enact legislation and regulatory implementation on a rational basis.

Court may invalidate legislation enacted under the commerce clause only if it is clear that there is no rational basis for congressional finding that regulated activity affects interstate commerce or that there is no reasonable connection between regulatory means selected and asserted ends.

Notwithstanding, these hurtles, the CMR and its analysis by the SEC is replete with admissions as to the inability of the government to explain its selectivity versus other similarly situated commercial international trade situations. Here the SEC openly admits the inability to conduct an analysis of benefits other than in the thinnest subjective terms.

We are unable to quantify the impact of each of the decisions we discuss below with any precision because reliable, empirical evidence regarding the effects is not readily available to the Commission, and commentators did not provide sufficient information to allow us to do so. Thus, in this section, our discussion on the costs and benefits of our individual discretionary choices is qualitative...

The terminology is facially indistinct to raise the question of who determines these factors; the company’s production engineers, designers, users or imposition of judgment by Commission bureaucrats and staff uneducated in product design? CMR’s murky language presents a quagmire of regulatory conflict, administrative law litigation (ALJ decision making) and general confusion to industry and regulators for years to come.

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65 CMR, supra note 7, at 22.
66 Hodel, supra note 63, at 321 (emphasis added).
67 CMR, supra note 7, at 268, 269.
Ultimately, the deficiencies posed by CMR in the totality of circumstance would force either the SEC or some judicial process to go essentially beyond the statutory text to give operational meaning to the rule. That is a line of “overreach” historically eschewed by the Supreme Court. As Justice Cardozo articulated in *Great Northern Railway*, “We have not traveled in our search for the meaning of the lawmakers, beyond the borders of the statute.”

Because material terms within CMR are so vague, the rule is exposed to great risk of failing the test of constitutionality. To be sure, federal courts have set a high bar asserting a due process violation under the legal *doctrine of vagueness*. "Uncertainty ... is not enough for [the commercial regulatory statute] to be unconstitutionally vague; rather, it must be substantially incomprehensible."

The legal threshold, however, for “void of vagueness” would certainly suggest that a rule which is vastly incomprehensible to the regulatory agency itself and thus to the industry regulated runs substantial risk of a successful constitutional challenge.

To be fair, the SEC in its announcement and review of the rule certainly implies throughout that CMR had been imposed on the agency and admits to its challenges and lack of preparedness in carrying out this Congressional mandate. As such, the SEC itself unilaterally held up implementation of the rule and reporting until 2014 and established a phase-in period, perhaps in hopes Congress, itself would revisit the propriety of the issue or repeal the rule altogether prior to that date and spare the agency its negative operational and legal impacts. The SEC’s delaying action, itself, is questionable as the statute gave it no authority to do so.

**E. Costs and Undue Burden to Business**

What could be the costs of such a rule that is merely “reporting” in nature and what are the true benefits? Is CMR merely a benign disclosure or an undue burden on business? It is here the true potential damage to the competitiveness of industry, ultimately hitting the consumer pocketbook is

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demonstrated. As with all federal rules, the SEC is required by law to assess the total cost-benefit impact of new regulations.\textsuperscript{71}

Specifically, the SEC is required by the \textit{National Securities Market Improvement Act}\textsuperscript{72} to among other things, consider whether an action “will promote efficiency, competition, and capital formation” whenever it is “engaged in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest.”\textsuperscript{73}

Furthermore, the SEC has an explicit statutory requirement under the Exchange Act of 1934\textsuperscript{74} to avoid rulemaking that has the effect of obstructing or lessening competition.

The Commission and the Secretary of the Treasury, in making rules and regulations pursuant to any provisions of this chapter, shall consider among other matters the impact any such rule or regulation would have on competition. The Commission and the Secretary of the Treasury shall not adopt any such rule or regulation which would impose a burden on competition not necessary or appropriate in furtherance of the purposes of this chapter. The Commission and the Secretary of the Treasury shall include in the statement of basis and purpose incorporated in any rule or regulation adopted under this chapter, the reasons for the Commission’s or the Secretary’s determination that any burden on competition imposed by such rule or regulation is necessary or appropriate in furtherance of the purposes of this chapter.\textsuperscript{75}

In its final rule, the SEC staff, itself, admitted to an initial deadweight cost to industry of $3 to $4 billion with annual compliance cost of $207 million to $609 million each year thereafter.\textsuperscript{76} However, an analysis by what the SEC refers to as the “University Group,” a large study conducted by lead econometric researcher; Tulane University, estimated the initial deadweight costs to be $7.93 billion and compliance costs of $207 million a year, thereafter.\textsuperscript{77} The NAM estimates costs to be $9 to $16 billion.\textsuperscript{78}

\begin{footnotes}

\textsuperscript{72} 15 U.S.C. §77b(b) (2012).

\textsuperscript{73} \textit{Id.}

\textsuperscript{74} 15 U.S.C. §78w(a)(2)) (2012).

\textsuperscript{75} \textit{Id. at} § 23(a)(2).

\textsuperscript{76} CMR, \textit{supra} note 7, at 302. (In the original rule before comment, the SEC stated the cost to be no more than $71 million, a far cry from its later admitted calculation).

\textsuperscript{77} \textit{Id.} at 254.

\textsuperscript{78} Business Roundtable, \textit{supra} note 70, at 1148-49.
\end{footnotes}
Notwithstanding, the statutory requirements of the Exchange Acts to SEC rule making, the Commission, challenged to calculate a cost-benefit of its CMR rule, the SEC admits its inability to qualify benefits for analysis and its lacking the analytic tools of its ordinary mission to do so.

The statute therefore aims to achieve compelling social benefits, which we are unable to readily quantify with any precision, both because we do not have the data to quantify the benefits and because we are not able to assess how effective Section 1502 will be in achieving those benefits. Additionally, the social benefits are quite different from the economic or investor protection benefits that our rules ordinarily strive to achieve.\(^79\)

While the Commission is required by law to assess benefits to costs, it declined to even attempt a quantified benefit calculation.\(^80\) The SEC did, however, conduct an extensive analysis of costs to industry that remain controversial, disputed by industry and academic analysts. In addition to the costs previously mentioned, the SEC rule identified a paperwork burden of approximately 1,400 hours per firm to implement and 700 hours each in subsequent years.\(^81\)

There are many ways to hypothetically demonstrate CMR’s impact on firms. We demonstrate here by a simple calculation. Given the Commission’s estimated hours and the number of companies subject to CMR, implementation per business represents approximately the equivalent of thirty-five work weeks plus 17.5 work weeks per year thereafter, per capita business. That implies at minimum each affected firm having to hire at last one full time employee each to comply with the rule.\(^82\) Based upon the number of affected firms, the calculation suggests industry would have to divert hiring from productive value-added employment to hiring in excess of 262,000 employees to merely research, file, monitor and produce compliance reports to the SEC on CMR. This does not include the hours and expense of independent commercial audit mandated by the rule.

These costs go somewhere and ultimately they turn up in increased cost of product, reduced quantity (or quality) of product to consumers, or diminished earnings to shareholders. These costs also add to a growing list of incentives for businesses to go private, a trend that could adversely impact capital market efficiency. To the extent they lessen or impede competition,

\(^79\) Id. at 243-44 (Part III-Economic Analysis, B. Cost-Benefit).
\(^80\) NAM, supra note 9, at 33-34.
\(^81\) Paperwork calculations in agency rulemaking are required by the Paperwork Reduction Act of 1995, 44 U.S.C. § 3501 et. seq.
\(^82\) Calculating based on a forty-hour work week.
consumers also could suffer. One interesting exercise, beyond this paper, is to figure out, for example, that cost impact on a common product such as Campbell’s soup. The venerable Campbell’s produces two billion cans a year.83

The “chilling effect” of the CMR is intended to have on users of Conflict Minerals, itself, implicates potential economic unintended consequences. As commentators to the rule noted to the SEC, firms have choices in materials and often time substitutes (all be them more expensive). The rule may trigger a de facto boycott of legitimate mineral producers in nations or adjoining countries adversely impacting their economic development, creating unemployment/poverty that feeds new violence and human rights abuses the rule is aimed to stop. Moreover, the substitution of suppliers may shift to mineral sources from nations with demonstrably more adverse human rights records than the DRC.84

Finally, as has been seen in advances in technology, the rules artificial inflation of costs provides an incentive for industry to find substitute materials or designs that do not use the conflict minerals at all, at which point, the rule may well become moot, except for the poverty created in once producer nations.

In short the Conflict Minerals Rule and its mandate arises at a time the United States has experienced forty-four months of unemployment in excess of eight percent, slow growth in Gross Domestic Product (GDP), declining personal income, record government deficit spending and growing competitiveness overseas. It comes at a time when the U.S. is attempting to retain manufacturing to stem the decade’s long movement of jobs overseas and maintain technological leadership. Consequently, the good intentions of informing the public of trade with DRC portend to be more than offset by loss of jobs and/or reduced competitiveness against non U.S. commercial enterprises.

The nation faces challenges and priorities with limited resources in the regulation of commerce? The public policy question is whether such priority inures to CMR at this time, place and cost. The legality of the rule itself remains problematic, the negative cost implications are huge.

F. Fundamental Rights: First Amendment

To this point we have highlighted potential areas of legal challenge to the Conflict Minerals Rule that arise under various judicial rulings,

84 CMR, supra note 7, at 18.
requirements of the Administrative Procedures Act, and the Exchange Acts. The final key area represents a most important one and that is where a regulatory rule impinges on fundamental rights guaranteed by the Constitution to its citizens, including businesses.

The First Amendment sets a high bar to government interference and the regulatory rule in question is subjected to the test of strict scrutiny established by the Supreme Court initially under Carolene Products. The current Supreme Court despite its differences has been quite firm on the free speech rights of businesses against unreasonable, arbitrary or capricious government interference in commercial free speech rights.

Plaintiffs in the NAM case raised for the first time the argument that §1502 in fact compels speech in violation of the Constitution’s First Amendment. Here NAM points out citing Wooley that the first amendment protects the right to speak and “to refrain from speaking.”

NAM further points out that because the regulation requires firms to state whether their products are “DNR Conflict Free or Not,” even where the information is unknown, forces a disclosure that has the effect of imposing a “Scarlet Letter,” compelling the company to associate or appear to associate with a political group (sic. DNR) engaged in human rights violations. Consequently, the innocent inability of a firm to confirm its metal content was not of DNR origin, ceteris paribus, leaves an inaccurate and negative inference in the public and customer’s mind that the firm does have DNR content.

NAM further states that the compelled disclosures required under CMR are neither factual, uncontroversial or politically neutral. Rather, “they require commercial firms to make statements pregnant with political judgments and connections regarding events in foreign countries.”

Citing the recent R.J. Reynolds ruling, NAM points out that the CMR is not a regulation preventing misleading advertising nor does it represent a narrowly tailored safety issue that falls within the least burdensome standards of strict scrutiny. Finally, even under an intermediate scrutiny standard, NAM asserts the statute and rule fails to “directly and materially advance” a clearly defined, substantial government interest. Rather, the regulatory scheme at

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85 304 U.S. 144 (1938).
86 For example among others, see Citizens United v. SEC, 558 U.S. 310 (2010); Sorrell v. IMS Health, Inc., 131 S. Ct. 2653 (2011); Liquormart, Inc. v. Rhode Island, 517 U.S. 484 (1996), Bad Frog Brewery, Inc. v. New York State Liquor Authority, 134 F.3d. 87 (2d Cir. 1998).
87 NAM, supra note 9 “Opening Brief of Petitioners” Document #1415549, January 16, 2013, at 52. (Hereafter referred to as “NAM Brief”).
89 Id.
90 Id. at 53.
91 R. J. Reynolds Tobacco Co. v. FDA, 696 F.3d 1205 (D.C. Cir. 2012)
best provides an ineffective, remote support for a generalized governmental purposes.92

It is important to note again that while §1502 presents complex, expensive reporting, it does not bar trade with DRC nor the use of conflict minerals that originate there. This key factor belies a government argument of “compelling state interest” under strict or intermediate scrutiny. That is, if the situation were so compelling, trade would be outright banned as Congress does with North Korea, Cuba, Iran and other non-human rights compliant nations.

[T]here are many far less speech-restrictive (and more direct) ways the government could pursue its goal of benefitting the DRC. Most obviously, the government could pursue political and diplomatic means. As dissenting Commissioner Gallagher remarked, “I am not a foreign or humanitarian policy expert, but it seems to me that taking the fight directly to the warlords would be a much more effective process than waiting and hoping for some positive trickledown effect attributable to new SEC reporting requirements under section 1502.93

The Conflict Minerals Rule under these circumstances appears to breach the important line of First Amendment jurisprudence, compelling political speech that is both burdensome, inaccurate and stigmatizing, in this case to impacted businesses.

III. UNINTENDED CONSEQUENCES TO HUMAN RIGHTS

At the end of the day, what has been accomplished? After all Congress’ entire exercise in enacting §1502 and delegating to the SEC alleges a singular purpose; to help eradicate the income to only those mines supporting the armed gangs responsible for corruption and wrecking havoc in human rights in the DRC. On this point, there is scant evidence that the law as constituted will have any positive effect and more likely than not, the contrary.

As analysts have pointed out, were the rule fully implemented human rights would not only not be improved in DRC but perhaps even worsened. As pointed out in the NAM Brief, the World Bank estimates 16% of the DNC’s population (approximately 10 million people) depend on its mining industry. In gold production, for example, nearly all DRC gold is produced

92 NAM Brief, supra note 9, at 53-54.
93 Id. at 54 (citations omitted).
by artisanal miners. These small scale mines are legitimate businesses at risk of losing business and employment. Accounting and trade in Central Africa is not precise enough to differentiate the legitimate DRC mines from those supporting the illegitimate armed gangs afflicting human rights abuses. Consequently, the chilling effect placed by the CMR rule on trade in the region creates a *de facto* embargo that irreparably creates hardships on innocent Congolese citizenry. To the extent this creates more poverty, greater human suffering will occur. This also extends to innocent adjacent nations such as Tanzania that are not part of the human rights issue (while not including nations such as Zimbabwe which is a major human rights abuser).

The GAO is currently studying these on-the-ground impacts.

Secondly, borders of the DRC and adjacent nations are extremely porous. It is relatively easy for the operators of suspect mines in the DRC to disguise mine origin or otherwise smuggle these metals across border in ways that are indistinguishable. Metals are raw commodities undifferentiated normally by place of origin. In fact it is stated that nearly 100% of Congo’s gold is already smuggled.

A significant factor present may be the rule’s future impact in causing businesses to find substitute materials. For example, a substitution of tin by another equally viable metal or alloy would drop the world demand for that metal and its price. The effect would not be felt exclusively in the DRC. Rather, it would negatively impact many other third world nations in which U.S. policy is involved in advancing economic development. Emerging nations in Asia, South America and Africa could see their economies plunged into more economic distress resulting in political instability, violence, and violations of human rights; precisely opposite the intentions of Congress.

Crushing the open market for minerals achieves the opposite of Section 1502’s stated aims. Creating a permanent *de facto* embargo would permanently deprive many miners of their livelihoods, make them more likely to join armed groups, and harm communities that have thus far resisted being taken over by armed groups. Creating a permanent *de facto* embargo would also entrench the smuggling of minerals out of the DRC, where they will either be falsely labeled as originating elsewhere, or will be sold to buyers indifferent to provenance.

94 *Id.* at 17.
95 *Id.*
96 *Id* at 18.
Economic sanctions have historically proven to be problematic in their enactment and implementation. This is because the effectiveness of trade restrictions can be offset by extreme deleterious effects to the trading nation imposing the restriction. The restriction or ban on imports is generally referred to in law as an “embargo.” This is differentiated by the affirmative use of force to cut off all trade of necessities and commerce of any kind, known as a “blockade,” which in international law is an act of war.98

Where the restricted target nation is small, of little to no threat to the U.S. or does not possess rare commodities in high demand, the restriction can have minimal domestic U.S. impact. On the other hand, if the U.S. and its industry depend on the target nation’s commodity the opposite effect can occur. Hence, bans on trade with North Korea and Cuba have little to no major impact on the U.S. The ban on trade with Iran, a major oil producer, is totally mitigated by major U.S., North American and other international sources.

Two examples from U.S. history make this point. In response to British acts of seizing U.S. merchant ships on the high seas and impressing U.S. seaman in the early 1800’s, President Thomas Jefferson and Congress passed the Embargo Act of 1807.99 The law effectively banned all imports of goods from Great Britain. While in theory this would compel a change in the bad acts of the English and perhaps stimulate domestic economic development in our still fledgling republic, the effect was precisely the opposite. The law caused extreme economic damage to the U.S. economy including shortage of goods, dislocation of employment, wages and inflation.100 Without the modern tools of enforcement technology, smuggling of English goods at inflated prices was rampant across the border with Canada and through transit from Central and South America. The U.S. Treasury at the time its revenue primarily dependent on customs duties, suffered major revenue loss. To stem further economic damage Congress repealed the law two years later (1809).101

A more modern example was the precursor to World War II, the United States embargo against the Imperial Empire of Japan. President Franklin

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98 U.N. Charter, art. 42. Also see, famous blockades in history include the British blockade of French ports 1810-1814 during the Napoleonic Wars, and, the U.S. Naval blockade of the ports of Southern States (e.g. Charleston, S.C., Wilmington, N.C., Hampton Roads, V.A., etc.) during the Civil War 1961-1865.


Roosevelt and Congress’s response to Japan’s invasion of Manchuria, China and its human rights atrocities was the Export Control Act of 1940. Originally halting the trade in airplanes, parts, machine tools, oil, metals, rubber and petroleum products, the law was later expanded to exclude all trade. Japan at that time derived 90% of its trade from imports and faced devastating economic effects. Most historians today view the embargo as the key trigger to Japan’s decision to attack the U.S. at Pearl Harbor, December 7, 1941, and the U.S. entry into World War II.

Because the use of an embargo poses such extreme risks both economically and potentially to national security, it is not to be engaged lightly and certainly not within the bowels of an unrelated massive financial industry regulatory bill. Nevertheless, the Conflict Minerals Rule poses just such economic risks to the general welfare of U.S. industry and manufacturing. Rather than directly addressing the issue of a trade estoppel in conflict minerals, Congress by its stated intent seeks to establish what amounts to a de facto embargo on the D.R. Congo and its adjoining nations. Experts in their amicus brief in the NAM case have raised this issue:

Even the highly sophisticated companies that have participated in the OECD’s due diligence pilot program have reported “an increasing number of their customers requesting the exclusion of minerals coming from the [eastern DRC] due to the SEC Final Rule, which in their view creates increased cost and public disclosure,” and that the SEC’s rule is the primary incentive for companies to stop sourcing from the region.

Though they pose no direct military threat, these countries control vast deposits of not only the targeted conflict minerals but other strategic natural resources on which the U.S. and its allied nations depend. These resources are also of value to nations which the U.S. and its allies oppose. The affected nations and more broadly the Organization of African States are presented with a demonstrably discriminatory law that isolates the continent of Africa while ignoring like practices by nations elsewhere in the world. That such suspect classification in the context of history would be interpreted as racial is a foregone conclusion.

CMR has consequently set the stage for potential damage to U.S. foreign policy and diplomacy in an important emerging world sector. To the

102 54 Stat. 714 (1940).
103 56 Stat. 463 (1942) and 58 Stat. 671 (1945).
105 Experts Amicus Brief, supra note 25, at 23-24 (citation omitted).
extent the policy causes nations adverse to Western interests to exploit these resources, including fostering para-military activities serving to de-stable democratic African governments, this then posits, perhaps one of the most serious of unintended consequences of CMR. That is, Congress unwittingly opening a Pandora’s Box, exposing significant national foreign policy and national security risks to a regulatory agency completely devoid of mission, experience, knowledge, professional competence and demonstrably unprepared to engage in foreign policy and national security matters. Could there be any greater example of irrationality per se using the rational basis test to federal courts?

Finally, both Congress and the SEC ignore the deleterious impact downstream on the American consumer. Whether one accepts the SEC’s estimated cost of the CMR or those of academic and industry analysts, the billions of dollars of compliance cost come from somewhere and that is the price of goods to U.S. consumers. Moreover, the rule establishes in effect a government-sanctioned unfair trade practice, in that it structurally imposes high costs on public corporations, not equally imposed on similarly situated private and government corporations. To the extent these differences impact prices; public firms face deleterious effects which at the extreme can lead to layoffs, offshore relocation or business failure.

Already coming out of the deepest recession since the 1930’s and facing anemic growth in GDP, the deadweight costs of CMR pass through the supply chain and into every product affected. Hence, it works precisely against both Congress and the President’s goal to advance the American economy, provide price stability and advance employment, particularly in domestic manufacturing.


108 The CMR raises another issue in longstanding debate over constitutional separation of powers and U.S. Presidential authority over foreign policy and national security. The U.S. Securities and Exchange Commission is an independent regulatory agency, not under the direct control of the Executive Branch. The Secretary of State, Secretary of Defense, and National Security Advisor serve at the pleasure of the President and carry out the President’s foreign policies. Hence, §1502’s delegation of “rulemaking,” impacting U.S. foreign policy may well be viewed by those subscribing to the “executive primacy” interpretation of constitutional power over foreign and national security as an improper, if not illegal, delegation by Congress. This is another problematic issue for further research beyond the scope of this paper. For a more full discussion of the constitutional issue see H. Jefferson Powell, The President’s Authority over Foreign Affairs: an Executive Branch Perspective, 67 GEO. WASH. L. REV. 527-76 (1999).
Closely related to the cost imposition on industry is the increased cost to the SEC which in a government era of austerity will be forced to make choices on enforcing and administering CMR with its numerous complications versus carrying out its primary mission of regulating the public securities markets. Given that conflict of resource allocation, agency attention to CMR in all likelihood will be relegated to the back burner, but having in the process forced industry to expend billions of dollars to no good outcome.

IV. SUMMARY AND CONCLUSIONS

The Dodd Frank-Conflict Minerals Rule (§1502) was enacted with good intentions and laudable purposes. Nevertheless, it is already proving to be a classic example of the Law of Unintended Consequences in government commercial regulation at work. Fostered inappropriately on a regulatory agency ill prepared to implement it, placing extraordinary dead weight costs on industry, compromising free speech rights, poorly articulated for compliance, and operationally unintelligible in many respects, the rule ultimately imposes more damage on regulators and industry than any demonstrable (or even cognizable) benefit to the public. Indeed, the rule itself may well unintentionally produce precisely the opposite of the desired effects.

The NAM case will provide the first major appellate review of the both the statute and SEC rulemaking on the subject. But NAM will only be but one of a host of new cases that will proceed through the trial courts and into the appellate courts. We may well see CMR become the poster child for the “Rational Basis Test” invalidation of irrational government regulatory rulemaking.

The great danger of the promulgation of the type of regulation represented by CMR, of course, is that unchecked, Congress may structurally expand this technique of commercial law and regulation to include the panoply of the other 118 elements of the Periodic Table\(^\text{109}\) and designate the bad actor nation du jour for business reporting and regulatory scrutiny.

Today it is the conflict minerals from DRC. What element and nation will be next, to what end and what political purpose? In a global marketplace this risks a legal and regulatory morass of grand proportions which takes the eye of industry and government off of growth and full employment of its

\(^{109}\) The PERIODIC TABLE is a tabular display by science of all identified chemicals and elements by their atomic weight in the universe discovered to date. The current table contains 188 elements although some scientists indicate the actual number may be as high as 122. See “Periodic Table” http://www.chemicool.com/.
citizenry. There is a limit to cost impositions by Congress on industry recognized by the courts. “[N]o legislation pursues its purpose at all costs.”\textsuperscript{110}

Congress, itself, has demonstrated that it cannot and does not act in a timely capacity to remove a “reformed” nation from such scrutiny, leaving the country of origin and its commercial users in cost, trade and regulatory limbo. In fact §1502 contains no mechanism for the SEC, Secretary of State or President of the United States to extinguish the rule in a timely manner on the day when DRC miraculous rides itself of armed gangs, reforms itself and joins the “legitimate” Commonwealth of Nations.

As but one case in point, Congress’ famous \textit{Jackson-Vanik Amendment} of 1974 was enacted to deny “most favored nation status” to the Soviet Union and its communist eastern block nations (“Warsaw Pact”), then blocking immigration of its citizens who desired to leave for religious or political purposes.\textsuperscript{111} The Soviet Union, Berlin Wall and communist east bloc nations all disappeared into the pages of history over twenty-five years ago, yet in the year 2013, Jackson-Vanick remains on the books; a continuing impediment to relations and trade with the current Russian Republic.

Regardless of political inclinations, there is a clear public policy expectation that commercial regulations promulgated have public value, are implemented effectively, and represent the least intrusive necessary to accomplish the public purpose. Such tests of scrutiny have well established precedent in U.S. law. Both the statutory language of §1502 and the promulgation of CMR implementation raise material questions of whether the government meets the test of providing a “narrowly tailored” approach to a compelling government interest. More importantly, the rule appears to severely fail the test of establishing the “least restrictive means” of implementing that interest.\textsuperscript{112} The public and public policy imperative was not heard.

The Conflict Minerals Rule reveals yet again a common observation that corporations make for poor foreign diplomats as government makes poor business managers. No one countenances the behavior of human rights abusers in the DNC or any other world nation. It is a constant struggle of compassion and American leadership to address them. On the other hand, we do no favors to the people of those nations, nor our own citizenry by jeopardizing our own economic welfare on speculative mechanisms of dubious impact to address these issues.

The proponents of Dodd-Frank’s Conflict Minerals Rule may have heard a \textit{stanza} of special interest groups or the \textit{tune} of their own

\textsuperscript{111} Trade Act of 1974, P. L. 93-618, §401, Title IV.
humanitarianism, but not the entire public policy *symphony* by American voters. Regardless of political inclinations we live in an era of limited resources to support government regulation. There is broad consensus that where government regulation exists it should be for a compelling purpose, rationally crafted in its implementation to be both effective and economical.

What Congress failed to hear and failed to heed was the, march of American citizenry of all stripes; bipartisan that overall melody might be. In so doing Congress Conflict Mineral Rule stands as yet a prominent representative symbol of a *tin ear of government regulation*. 
EXHIBIT A: CONFLICT MINERALS RULE FLOW CHART
(Source: U.S. Securities and Exchange Commission)\textsuperscript{113}

\textbf{START}

Does the issuer file reports with the SEC under Sections 13(a) or 15(d) of the Exchange Act?

\textbf{YES}

Does the issuer manufacture or contract to manufacture products?

\textbf{YES}

Are conflict minerals necessary to the functionality or production of the product manufactured or contracted to be manufactured?

\textbf{NO}

\textbf{NO}

Rule does not apply. END

\textbf{NO}

\textbf{NO}

\textbf{YES}

Were the conflict minerals outside the supply chain prior to January 1, 2013?

\textbf{YES}

\textbf{NO}, if newly-mined

Based on a reasonable country of origin inquiry (RCOI), does the issuer know or have reason to believe that the conflict minerals may have originated in the DRC or an adjoining country (the covered countries)?

\textbf{YES}

\textbf{NO}

\textbf{NO}, if potentially scrapped or recycled

Based on the RCOI, does the issuer know or reasonably believe that the conflict minerals come from scrap or recycled?

\textbf{YES}

File a Form SD that discloses the issuer’s determination and briefly describes the RCOI and the results of the inquiry. END

\textbf{NO}

File a Form SD with a Conflict Minerals Report as an exhibit, which includes a description of the measures the issuer has taken to exercise due diligence.

In exercising the due diligence, was the issuer able to determine whether the conflict minerals financed or benefited armed groups?

\textbf{YES}

\textbf{NO}

\textbf{YES}

Is less than two years after effectiveness of the rule (four years for Smaller Reporting Companies)?

\textbf{YES}

The Conflict Minerals Report must also include a description of products that are “DRC Conflict Undeterminable” and the steps taken or that will be taken, if any, since the end of the period covered in the last Conflict Minerals Report to mitigate the risk that the necessary conflict minerals benefit armed groups, including any steps to improve due diligence. No audit is required. END

\textbf{NO}

The Conflict Minerals Report must also include an independent private sector audit report, which expresses an opinion or conclusion as to whether the design of the issuer’s due diligence measures is in conformity with the criteria set forth in the due diligence framework and whether the description of the issuer’s due diligence measures is consistent with the process undertaken by the issuer. Also, include a description of the products that have not been found to be DRC Conflict Free, the facilities used to process the necessary conflict minerals in those products, the country of origin of the minerals and the efforts to determine the mine or location of origin of those minerals with the greatest possible specificity. END

\textsuperscript{113} CMR, \textit{supra} note 7, at 33.