ORAL ARGUMENT SCHEDULED FOR MAY 15, 2013 AM

No. 12-1422

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

NATIONAL ASSOCIATION OF MANUFACTURERS;
CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA;
BUSINESS ROUNDTABLE,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent,

AMNESTY INTERNATIONAL USA; AMNESTY INTERNATIONAL LTD.,

Intervenors for Respondent.

On Petition for Review of a Final Order of the
U.S. Securities and Exchange Commission

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TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

GLOSSARY vi

SUMMARY OF ARGUMENT 1

ARGUMENT 2

I. THE COMMISSION VIOLATED ITS STATUTORY OBLIGATIONS TO CONSIDER THE EFFECTS OF ITS RULE AND AVOID UNNECESSARY BURDENS 2

A. Without Determining Whether the Rule Or Its Own Regulatory Choices Would Benefit The DRC, The Commission Could Not Properly Exercise Its Authority 2

B. The Commission's Cost Calculations Were Concededly Arbitrary 8

II. THE COMMISSION MISINTERPRETED THE STATUTE AND ARBITRARILY REJECTED LOWER-COST ALTERNATIVES 8

A. The Statute Does Not Preclude A *De Minimis* Exception, And The Commission Arbitrarily Refused To Create One 10

B. The Rule's Extension To Non-Manufacturers Is Contrary To The Statute 17

C. The Commission Misinterpreted the Statute's "Did Originate" Requirement And Imposed Unnecessary Burdens 20

D. The Phase-in Period Is Arbitrary And Capricious 22

E. The Commission's Errors Require Vacatur 22

III. SECTION 1502 VIOLATES THE FIRST AMENDMENT 23

CONCLUSION 28

CERTIFICATE OF COMPLIANCE 29

CERTIFICATE OF SERVICE 30

TABLE OF AUTHORITIES

Page(s)

CASES

Ala. Power Co. v. Costle,
636 F.2d 323 (D.C. Cir. 1979) 12

Am. Bar Ass'n v. FTC,
430 F.3d 457 (D.C. Cir. 2005) 11, 18

Am. Equity Inv. Life Ins. Co. v. SEC,
613 F.3d 166 (D.C. Cir. 2010) 3

**Ass'n of Admin. Law Judges v. FLRA*,
397 F.3d 957 (D.C. Cir. 2005) 12, 13, 14

Bradford Nat'l Clearing Corp. v. SEC,
590 F.2d 1085, 1105 (D.C. Cir. 1978) 4

**Bus. Roundtable v. SEC*,
647 F.3d 1144 (D.C. Cir. 2011) 2, 3, 6, 10

Comcast Corp. v. FCC,
579 F.3d 1 (D.C. Cir. 2009)....................22

Conference of State Bank Supervisors v. Conover,
715 F.2d 604 (D.C. Cir. 1983) 19

CTIA– The Wireless Ass'n v. City of S.F.,
2012 WL 3900689 (9th Cir. Sept. 10, 2012) 24

Edenfield v. Fane,
507 U.S. 761 (1993) 26

Full Value Advisors, LLC v. SEC,
633 F.3d 1101 (D.C. Cir.)....................25

Gen. Instrument Corp. v. FCC,
213 F.3d 724 (D.C. Cir. 2000) 14

* Denotes authorities most relied upon.

Hui v. Castaneda,
130 S. Ct. 1845, 1853 (2010) 12

Meese v. Keene,
481 U.S. 465 (1987) 24, 25

Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto Ins. Co.,
463 U.S. 29 (1983) 7

Nati'l Ass'n of Home Builders v. EPA,
682 F.3d 1032 (D.C. Cir. 2012) 3

Nat'l Ass'n of Mfrs. v. Taylor,
582 F.3d 1 (D.C. Cir. 2009)..27

Nat'l Elec. Mfrs. Ass'n v. Sorrell,
272 F.3d 104 (2d Cir. 2001) 24

PDK Labs. Inc. v. DEA,
362 F.3d 786 (D.C. Cir. 2004) 9, 10

**Peter Pan Bus Lines, Inc. v. Fed. Motor Carrier Safety Admin.*,
471 F.3d 1350 (D.C. Cir. 2006) 9, 11, 18

Prill v. NLRB,
755 F.2d 941 (D.C. Cir. 1985) 9

Pub. Citizen, Inc. v. Rubber Mfrs. Ass'n,
533 F.3d 810 (D.C. Cir. 2008) 14

Pub. Citizen v. Fed. Motor Carrier Safety Admin.,
374 F.3d 1209 (D.C. Cir. 2004) 8

**R.J. Reynolds Tobacco Co. v. FDA*,
696 F.3d 1205 (D.C. Cir. 2012) 23, 26

Rodriguez v. United States,
480 U.S. 522 (1987) 5

Schiller v. Tower Semiconductor Ltd.,
449 F.3d 286 (2nd Cir. 2006) 12

SEC v. Wall St. Publ'g Inst.,
851 F.2d 365 (D.C. Cir. 1988) 25

Sierra Club v. EPA,
705 F.3d 458 (D.C. Cir. 2013) 13

Spirit Airlines, Inc. v. U.S. Dep't of Transp.,
687 F.3d 403 (D.C. Cir. 2012) 24

Turner Broad. Sys., Inc. v. FCC,
520 U.S. 180 (1997) 26

Zauderer v. Office of Disciplinary Counsel of Supreme Ct. of Ohio,
471 U.S. 626 (1985) 23

STATUTES AND REGULATIONS

Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No.
11-203, 124 Stat. 1376 (2010) 6, 24

15 U.S.C. §78*l*(h) 7, 12

15 U.S.C. §78m(p)(1) 18, 19, 24

15 U.S.C. §78m(p)(2)(B) 18, 19

15 U.S.C. §78m(p)(3)-(4) 6

15 U.S.C. §78m(p)(5) 24

*15 U.S.C. §78mm(a) 7, 12

15 U.S.C. §78mm(b) 12

*15 U.S.C. §78w(a)(2) 2, 3

Release No. 34-63547, 2010 WL 5121983 (Dec. 15, 2010) 16

76 F.R. 6010 (Feb. 2, 2011) 12

77 F.R. 56,274 (Sept. 12, 2012).................... 4, 5, 10, 13, 14, 16, 17, 19, 21, 22, 26, 27

LEGISLATIVE HISTORY

155 Cong. Rec. S4697 (daily ed. Apr. 23, 2009) 6

156 Cong. Rec. H5261-62 (June 30, 2010) 15

156 Cong. Rec. S5933 (July 15, 2010) 15

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GLOSSARY

Br.	Response brief of the Securities and Exchange Commission
Conflict minerals or minerals	Columbite-tantalite, cassiterite, gold, wolframite, and their derivatives tantalum, tin, gold, and tungsten
Congressmen Br.	Brief of Congressman McDermott et al.
DRC	Democratic Republic of the Congo
Dodd-Frank	Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (2010)
Industry Br.	Brief of Industry Coalition
Intervenors Br.	Brief of Amnesty International USA and Amnesty International Ltd.
NAM	The National Association of Manufacturers
OECD	Organisation for Economic Co-operation and Development
Petr. Br.	Opening brief of Petitioners the National Association of Manufacturers, the Chamber of Commerce of the United States of America, and Business Roundtable
The release	*Conflict Minerals*, 77 FR 56,274 (Sept. 12, 2012)
SEC or Commission	The United States Securities and Exchange Commission
Section 1502	Section 1502 of Dodd-Frank

SUMMARY OF ARGUMENT

The Securities and Exchange Commission ("SEC" or "Commission") determined that its final rule will impose billions of dollars in costs on American businesses, but failed to assess whether the rule will provide any benefits. The SEC did not merely fail to *quantify* the benefits, as the agency suggests in its brief, *see* Br. 33-34, but, more fundamentally, it completely failed to determine whether the rule would provide *any* benefits at all—quantitative or qualitative. Indeed, the SEC even failed to address the "fierce[] debat[e]" in the record on whether the rule would be *counter-productive*, harming the very people it was intended to help. Br. 24.

The SEC's response is startling and internally inconsistent. The Commission first blames Congress and argues it lacked authority to second-guess Congress's judgment, which it says tied the agency's hands. Br. 30-31. But, just a few pages later, the Commission insists it made "reasonable" discretionary decisions, warranting "deference" under *Chevron*. Br. 43. The Commission cannot have it both ways. Its arguments are mutually exclusive, irreconcilable, and simply inadequate to defend one of the costliest rules in the agency's history.

Moreover, neither argument is defensible on its own. First, Congress did not mandate the particular challenged aspects of the rule; if anything, it required the opposite. And, second, even where the statute left room for agency discretion, the agency's decisions were still arbitrary and capricious. As the Commission recognized, each of the rule's challenged aspects greatly increases its massive, unprecedented costs

on American businesses, and the Commission failed to assess whether these determinations would yield *any* benefits or instead make a tragic humanitarian situation even worse.

Finally, the rule's authorizing statute violates the First Amendment. A compelled public disclosure suggesting that a company's products contribute to terrible human rights abuses in a foreign land is plainly not designed to avoid a danger of misleading consumers, nor is it "purely factual and uncontroversial," as the Commission argues, Br. 64-65; rather, it is misleading, stigmatizing, and pregnant with political judgments.

ARGUMENT

I. THE COMMISSION VIOLATED ITS STATUTORY OBLIGATIONS TO CONSIDER THE EFFECTS OF ITS RULE AND AVOID UNNECESSARY BURDENS.

A. Without Determining Whether the Rule Or Its Own Regulatory Choices Would Benefit The DRC, The Commission Could Not Properly Exercise Its Authority.

By failing to analyze the benefits of its rule and conducting an inadequate analysis of the costs, the Commission failed once again to fulfill its unique statutory obligations "to consider the effect of a new rule upon 'efficiency, competition, and capital formation,'" *Bus. Roundtable v. SEC*, 647 F.3d 1144, 1148 (D.C. Cir. 2011) (quoting 15 U.S.C. §78c(f)), and not to "impose a burden on competition not necessary or appropriate in furtherance of the purposes of this chapter," 15 U.S.C. §78w(a)(2). Disregarding circuit precedent, the Commission did not adequately

"weigh[] the rule's costs and benefits," or decide whether the "net benefit" justifies the "cost[s] at the margin." *Bus. Roundtable*, 647 F.3d at 1151, 1153.[1]

The Commission contends that it "was not required" to conduct this analysis, because it could not "second-guess the wisdom of Congress's determination that conflict minerals disclosure will yield social benefits in the form of decreasing conflict and violence in the DRC." Br. 30. But it is not enough "to cite Congress's humanitarian goal." *Paredes Dissent*, JA716. Although Congress directed the SEC to promulgate *a* rule, it did not mandate many aspects of the SEC's final rule, including the four particular aspects this petition addresses. And, in its brief, the SEC asserts it made numerous "discretionary choices"—though, to be sure, it is inconsistent in indicating *which* choices it considers to be discretionary. Br. 34-39.

Moreover, the SEC recognized that each challenged aspect of the rule—the refusal to adopt a *de minimis* exception, the extension of the rule to non-manufacturers, the "may have originated" standard, and the shorter phase-in period

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[1] Intervenors and *amici* Better Markets contend that the SEC was not required to conduct a cost-benefit analysis at all. However, their argument is plainly inconsistent with *Business Roundtable*. The cases on which they rely, including *National Ass'n of Home Builders v. EPA*, 682 F.3d 1032, 1039 (D.C. Cir. 2012), involve different agencies subject to different statutory requirements. Unlike those agencies, the SEC has an obligation not only to "consider" the impact of its rule, but also to "not adopt" regulations that impose unnecessary or inappropriate burdens on competition. *See Bus. Roundtable*, 647 F.3d at 1148; 15 U.S.C. §78w(a)(2). Furthermore, because the SEC conducted an economic analysis, albeit a severely flawed one, any contention that such analysis was "not required" must be "reject[ed]." *Am. Equity Inv. Life Ins. Co. v. SEC*, 613 F.3d 166, 177 (D.C. Cir. 2010).

for larger issuers—will increase the burdens on competition. 77 F.R. 56,274, 56,298, 56,344-45 (Sept. 10, 2012). Accordingly, 15 U.S.C. §78w(a)(2) required the Commission to determine whether these burdens are "necessary or appropriate" to further the purposes of the statute—here, "to decrease the conflict and violence in the DRC." 77 F.R. 56,350. The SEC cannot make this determination without analyzing "the likelihood that the [regulatory] action will achieve those [statutory] objectives." *Bradford Nat'l Clearing Corp. v. SEC*, 590 F.2d 1085, 1105 (D.C. Cir. 1978). Yet the SEC failed to conduct this requisite analysis, instead stating that it "was not able to assess how effective Section 1502 will be in achieving those benefits," 77 F.R. 56,350, and avoiding the "fierce[] debat[e]" on whether the rule is counter-productive, *see* Br. 24.

The Commission contends that "[t]he release provides a thorough qualitative analysis of both the costs and benefits of the Commission's discretionary decisions," Br. 30, and that due to "the dearth of quantitative evidence in the record, the Commission's decision not to quantify the benefits was reasonable," Br. 33-34; *see* Intervenors Br. 18-24. But the Commission not only failed to *quantify* the benefits, it failed to assess whether there would *be* any benefits, including from its regulatory choices. Although the SEC claims to have "qualitative[ly]" analyzed the benefits, in fact the only "benefit" the release points to is "the benefit of lowering the … costs of the rule" compared to even more demanding alternatives. *See* 77 F.R. 56,342, 56,345; *see also* Br. 35 (citing same "benefits"). The Commission cannot transform a cost into

a benefit simply by asserting that the cost could have been even worse. At no point did the Commission determine whether the rule overall, or any of its regulatory choices, would benefit the people of the DRC. 77 F.R. 56,350.

In addition, Congress's direction to create a disclosure regime does not mean Congress determined that *any* burden, no matter how high, was justified if it would lead to more disclosure. "[N]o legislation pursues its purposes at all costs." *Rodriguez v. United States*, 480 U.S. 522, 525-26 (1987). To the contrary, "[d]eciding what competing values will or will not be sacrificed to the achievement of a particular objective is the very essence of legislative choice—and it frustrates rather than effectuates legislative intent simplistically to assume that *whatever* furthers the statute's primary objective must be the law." *Id.* at 526. The Commission makes precisely that simplistic assumption, repeatedly stating that the challenged aspects of the rule are necessary to "effectuate[] [congressional] intent," 77 F.R. 56,291, or to "advance … the provision's purpose," 77 F.R. 56,298, *see* 77 F.R. 56,314, even though the statute does not mandate those aspects of the rule and the Commission made no determination they would improve conditions in the DRC.

With as little merit, the Commission argues that Congress intended for "*other* agencies and branches of government [to] assess the efficacy of Section 13(p) and Rule 13p-1 in decreasing violence in the DRC," "*not the Commission*." Br. 32 (emphasis in original). The statute indeed gives other agencies and branches a role; the Comptroller General, for instance, must submit annual reports to Congress assessing

the effectiveness of the statute and rule, while the President under certain circumstances may revise, waive, or terminate the rule. *See* Section 1502(d)(2)(A); 15 U.S.C. §78m(p)(3)-(4). But Congress assigned the SEC the special task of designing the rule in the first place, and it also gave the SEC "unique obligation[s]" to consider the economic impact of its rules and avoid unnecessary burdens. *Bus. Roundtable*, 647 F.3d at 1148.

It is therefore highly implausible that Congress—without saying so—intended to relieve the SEC of those obligations here, and intended for every entity involved *except for the SEC* to analyze the rule's benefits. Rather, Congress's requirement that other agencies and branches analyze the benefits of the disclosure regime on an ongoing basis, as well as Congress's choice of an agency with unique statutory obligations to conduct such an analysis in crafting the rule, show that Congress was especially concerned with obtaining a thorough analysis and curtailing unnecessary regulatory burdens.

Indeed, it was critical for the SEC to provide this analysis given the danger that an overly stringent rule could backfire and unintentionally harm the Congolese people by creating a devastating *de facto* embargo. *See* Petr. Br. 17. Congress was sensitive to this concern, recognizing that "[a]ll-out prohibitions or blanket sanctions could be counterproductive and negatively affect the very people we seek to help." 155 Cong. Rec. S4697 (daily ed. Apr. 23, 2009) (Sen. Feingold). And, as the Commission admits, it "received a number of comments fiercely debating whether the disclosure regime

would actually yield such a benefit" to the DRC, Br. 24, or would instead "exacerbat[e] conditions," Br. 22 n.3. *See id.* 32 ("[T]he comments in the record were decidedly mixed in their predictions of the effects of a disclosure regime on the ground.").[2]

Further, the extensive and detailed data commenters provided regarding the impact that anticipation of the rule was actually having in the DRC was not available to Congress when it passed the statute. There is no reason to think that Congress intended the agency to cover its eyes and ignore entirely this highly relevant new information in designing the rule, rather than taking into account all available factual evidence. Accordingly, it was arbitrary and capricious for the Commission not to consider the rule's impact on the DRC. *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto Ins. Co.*, 463 U.S. 29, 43 (1983) (failure to "consider an important aspect of the problem" makes agency action arbitrary and capricious).

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[2] The Commission asserts that "concerns about a *de facto* embargo stem from the statute itself, and not any details of the Commission's rule," Br. 33, but then admits that regulatory choices such as designing a phase-in period and creating exemptions are highly relevant to the embargo, Br. 22 n.3, 33 n.5. Indeed, the Commission could have used its broad exemptive authority, 15 U.S.C. §§78mm(a)(1), 78*l*(h), as "necessary or appropriate" to avoid an embargo, for instance by exempting from due diligence companies that contractually require suppliers to use certified conflict-free smelters, even if the smelters use minerals from the region. At the very least, the Commission could have chosen not to increase dramatically the costs of a rule that would make the situation in the DRC even worse.

B. The Commission's Cost Calculations Were Concededly Arbitrary.

The Commission compounded these errors by underestimating the rule's costs. Although the Commission's own cost estimate is staggeringly large—$3 to $4 billion for initial compliance, and an additional $207 to $609 million per year for ongoing compliance—it reached this estimate only by arbitrarily discounting the NAM's estimate that initial costs would be between $9 and $16 billion, as well as Tulane University's independent estimate of $7.93 billion. JA378; JA520. The SEC argues that its cost analysis was reasonable, but effectively concedes that it reduced these figures simply because other commenters provided lower estimates. *See* Br. 40-42. The SEC cannot simply pick a number in the middle when commenters provide divergent estimates; rather, it must engage in reasoned analysis and determine which estimate is the most reliable. *See Pub. Citizen v. Fed. Motor Carrier Safety Admin.*, 374 F.3d 1209, 1222 (D.C. Cir. 2004).

II. THE COMMISSION MISINTERPRETED THE STATUTE AND ARBITRARILY REJECTED LOWER-COST ALTERNATIVES.

Turning to the substance of the final rule, the Commission advances inconsistent arguments. As discussed, when defending its failure to analyze costs and benefits, the Commission claims it was not "authorized to second-guess and recalibrate policy judgments Congress made when it ordered the Commission to promulgate th[e] rule." Br. 2. But, when defending the four substantive aspects of the rule at issue, the Commission contends that its positions are "reasonable" and

entitled to "deference." *See* Br. 43. The Commission cannot have it both ways; its request for deference is defeated by its contradictory argument that Congress compelled it to do what it did.

Moreover, the SEC's release itself precludes deference. Because the Commission simply applied "the traditional tools of statutory construction," *PDK Labs. Inc. v. DEA*, 362 F.3d 786, 797 n.4 (D.C. Cir. 2004), examining the statute's text, structure, and purposes, and concluded that Congress required it to create the challenged aspects of the rule, "[t]he law of this circuit requires … that we withhold *Chevron* deference," *Peter Pan Bus Lines, Inc. v. Fed. Motor Carrier Safety Admin.*, 471 F.3d 1350, 1354 (D.C. Cir. 2006). And because the SEC's conclusion that its "interpretation is compelled by Congress" is incorrect, the Court "cannot uphold the [agency's] interpretation under step 1 of *Chevron*." *Id.* Instead, the Court must "remand to the agency," even if the SEC's interpretation would have been permissible under *Chevron* Step 2. *Id.*; *see Prill v. NLRB*, 755 F.2d 941, 948 (D.C. Cir. 1985) ("[A]n agency regulation must be declared invalid, even though the agency might be able to adopt the regulation in the exercise of its discretion, if it was not based on the agency's own judgment but rather on the unjustified assumption that it was Congress' judgment that such a regulation is desirable.") (alterations omitted).

Further, even where the SEC had discretion, and even if it had purported to exercise that discretion, the rule would still be arbitrary, because the SEC failed to perform an adequate analysis. *See supra* at 2-7. When an agency recognizes that an

interpretation is not compelled by Congress, "it is incumbent upon the agency not to rest simply on its parsing of the statutory language." *PDK Labs.*, 362 F.3d at 797-98. Rather, the agency "must bring its experience and expertise to bear in light of competing interests at stake." *Id.* Here, the agency did not apply its expertise, analyze competing interests, or resolve the "fierce[] debat[e]" in the record. Br. 2-3, 24. Because the challenged aspects of the rule substantially increase its burdens, and because the agency failed to determine whether these increased burdens would further the statutory purpose *at all*, the rule is arbitrary and capricious. *Bus. Roundtable*, 647 F.3d at 1148.

A. The Statute Does Not Preclude A *De Minimis* Exception, And The Commission Arbitrarily Refused To Create One.

The Commission surprisingly asserts that it "did not conclude that it 'lacked authority' to create or that it 'was precluded from considering' a *de minimis* exception." Br. 44. The Commission's own statements in the release contradict this assertion: "[W]e are of the view that Congress intended not to provide for a *de minimis* exception," and such an exception "would be contrary to the Conflict Minerals Statutory Provision and Congressional purpose." 77 F.R. 56,298; *see also id.* ("if [Congress] had intended that the provision be limited further, so as not to apply to a *de minimis* use of conflict minerals, we think Congress would have done so explicitly"); *id.* at 56,342-50 (not including *de minimis* issue in discussion of the "Commission's Exercise of Discretion").

Furthermore, the Commission contradicts this assertion even within its own brief, stating "the Commission's broader conclusion that … 'we believe Congress intended the disclosure provisions to apply to the use of even small amounts of conflict minerals originating in the Covered Countries' *necessarily precluded* the adoption of any" of the *de minimis* thresholds commenters proposed. Br. 48 (emphasis added); *see also* Br. 16, 43 (explaining that the SEC refused to create a *de minimis* exception based on its analysis of the "text, structure, and purposes of Section 1502"); Br. 46 ("It was not for the Commission, through *de minimis* exemptive authority, to find that 'Congress overreached' and to bring the statutory 'requirements back into line.'"). The Commission never specifically examined whether any of the *particular* proposals for *de minimis* exceptions would be appropriate because it summarily concluded that Congress categorically foreclosed its authority to adopt *any* such threshold.

The agency's incorrect determination that Congress precluded it from adopting a *de minimis* exception is entitled to no deference and cannot be upheld. *Peter Pan Bus Lines*, 471 F.3d at 1354; *see Am. Bar Ass'n v. FTC*, 430 F.3d 457, 471 (D.C. Cir. 2005) ("[W]e cannot affirm an agency's actions based on the *post hoc* rationale of its litigating position."). The Commission plainly had power to adopt a *de minimis* exception under its general statutory exemptive authority, which provides that "notwithstanding any other provision of this chapter," the Commission can "exempt … any class or classes of persons, securities, or transactions, from any provision or provisions of this chapter or of any rule or regulation thereunder, to the extent that such exemption is

necessary or appropriate in the public interest." 15 U.S.C. §78mm(a)(1). It likewise had that power under 15 U.S.C. §78*l*(h), which authorizes exemptions from several provisions of the Act, including "section 78m," where "such action is not inconsistent with the public interest or the protection of investors." These "similar" exemptive provisions establish that "Congress intended to grant the Commission considerable regulatory discretion in this area" and "flexibility in adopting exemptions." *Schiller v. Tower Semiconductor Ltd.*, 449 F.3d 286, 292 n.5, 296-97 (2d Cir. 2006); *see* 76 F.R. 6010 (Feb. 2, 2011) (granting exemption from statutory requirement).[3]

In addition to its broad statutory exemptive authority, the agency had inherent authority to create a *de minimis* exception. *Ala. Power Co. v. Costle,* 636 F.2d 323 (D.C. Cir. 1979). In arguing to the contrary, the SEC points out that the statute contains no express *de minimis* exception. But even the agency recognizes that this factor is "not dispositive," Br. 44, and indeed this Court has "repeatedly recognized that a *de minimis* exception is generally not express; rather, it is inherent in most statutory schemes, by

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[3] Congress's grant of authority to the *President* to revise or temporarily waive the rule for national security reasons did not *sub silentio* strip the Commission of its exemptive authority, and the Commission does not argue otherwise. *But see* Intervenors Br. 25-29. Section 78m(p)(3) makes no mention of section 78mm(a)(1) or section 78*l*(h), and therefore cannot be read to abrogate them. *Hui v. Castaneda*, 130 S. Ct. 1845, 1853 (2010) ("[R]epeals by implication are not favored."); 15 U.S.C. §78mm(b) (explicitly setting forth sections of the Exchange Act to which the Commission's exemptive authority does not apply). Furthermore, a *de minimis* exception is neither a "revis[ion]" nor a "temporar[y] waive[r]" of the statutory requirements, but simply a limitation upon those requirements. *Ass'n of Admin. Law Judges v. FLRA*, 397 F.3d 957, 962 (D.C. Cir. 2005).

implication." *Ass'n of Admin. Law Judges v. FLRA*, 397 F.3d 957, 962 (D.C. Cir. 2005). The inclusion of an express, mandatory *de minimis* exception in Section 1504 of Dodd-Frank does not change this analysis. As the SEC later points out, "'a congressional mandate in one section and silence in another often 'suggests not a prohibition but simply a decision *not to mandate* any solution in the second context.'" Br. 52 (quoting *Catawba Cnty. v. EPA*, 571 F.3d 20, 36 (D.C. Cir. 2009)).

The Commission argues that a *de minimis* exception would be inconsistent with "the 'express' limitation in Section 1502—that a conflict mineral must be 'necessary to the functionality or production' of an issuer's product." Br. 45 (quoting 15 U.S.C. §78m(p)(2)(B)). But *every* statute is written with some limitations that define the scope of its coverage, and such limitations do not deprive an agency of implicit authority to create a *de minimis* exception unless they are "extraordinarily rigid," which the language here clearly is not. *Sierra Club v. EPA*, 705 F.3d 458, 466 (D.C. Cir. 2013); *see* 77 F.R. 56,293 ("The provision, however, provides no additional explanation or guidance as to the meaning of 'necessary to the functionality or production of a product.'"). Indeed, the Commission provided for a number of *other* exceptions from the language, exempting, for instance, minerals used for decoration when the "primary purpose" of the product is not decorative, as well as minerals not physically present in the product. 77 F.R. 56,296-97. Plainly, the Commission could have created a *de minimis* exception as well. Furthermore, Section 1502 must be read in conjunction with the Commission's statutory obligation not to impose unnecessary burdens, as well as its

statutory exemptive authority. *Cf. Ass'n of Admin. Law Judges*, 397 F.3d at 959, 962 (finding *de minimis* authority where statute separately provided that its provisions should be applied "consistent with the requirement for an effective and efficient Government"). When read together, these provisions make clear that Congress did not intend to impose an "extraordinarily rigid" requirement preventing the SEC from creating reasonable exemptions.

The Commission also relies on a comment letter from two co-sponsors of Section 1502, which asserts that Congress "intentionally" decided not to include a *de minimis* exception. Br. 45; JA103. However, such post-enactment "legislative future" has "almost no value," *Gen. Instrument Corp. v. FCC*, 213 F.3d 724, 733 (D.C. Cir. 2000); *see Pub. Citizen, Inc. v. Rubber Mfrs. Ass'n*, 533 F.3d 810, 819 (D.C. Cir. 2008) ("We see no reason to give greater weight to the views of two Senators than to the collective votes of both Houses, which are memorialized in the unambiguous statutory text."), especially where, as here, other Members of Congress who also voted for the bill contended that the Commission *should* create a *de minimis* exception, *see* JA644. Indeed, the Commission itself recognized that it could not afford special weight to the co-sponsors' post-enactment views, by rejecting their statutory interpretation in numerous respects. *See, e.g.*, 77 F.R. 56,287 (rejecting co-sponsors'

contention that the statute covers non-reporting issuers as inconsistent with "clear" "statutory language").[4]

Even if the Commission could now argue, despite the release, that the agency exercised its independent judgment in declining to create a *de minimis* exception, that decision would be arbitrary. Other than the SEC's erroneous statutory interpretation about its authority, the only justification it offers is that the State Department and other commenters asserted that an exception "could" undercut the rule. Br. 46-47. The State Department's entire discussion of the issue, however, consisted of two sentences: "In light of the nature in which the covered materials are often used in products, *i.e.*, often in very limited quantities, such a change could have a significant impact on the proposed regulations. A *de minimis* threshold should not be considered under current circumstances." JA445. Instead of relying on a conclusory assertion of what "could" happen from the State Department (which has no special expertise regarding supply-chain management), the SEC should have analyzed the wide variety of proposed *de minimis* thresholds and determined whether any might have avoided

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[4] For the same reasons, the arguments of *amici* Congressmen are unpersuasive. The twelve *amici* are less than 5% of the 297 Members of Congress who voted for the law. 156 Cong. Rec. H5261-62 (June 30, 2010) (roll call); 156 Cong. Rec. S5933 (July 15, 2010) (same). No citation to the legislative history—much less to the statutory text—supports their assertion that Congress explicitly considered and rejected "the idea of a *de minimis* exception." Congressmen Br. 11.

the commenters' concern, while also avoiding the massive, pointless expenditures of resources that will result from having no *de minimis* exception at all.

A number of commenters proposed appropriately limited *de minimis* thresholds. Some suggested the SEC could "[s]et[] a very low *de minimis* threshold," JA525, such as for "trace, nominal, or insignificant amounts," 77 F.R. 56,295; *see* JA269 (proposing exception for "trace" amounts); JA397 (proposing exception for minerals whose value is less than 0.1% of component). Others suggested that the SEC could set the threshold based on the *total* amount of minerals an issuer uses annually, thus ensuring that the exception would not apply to issuers who use very small amounts per product, but significant amounts overall. *See* JA623 (proposing exception "if all widgets that an issuer manufactures or contracts for manufacture contain, in the aggregate, only negligible quantities of the subject metals"); JA460 (proposing threshold based on the "fair market value" of the total amount of minerals an issuer uses annually); JA219 (similar); *see also* JA106 (proposing threshold by industry of the lowest percentile users).

Indeed, the SEC's own request for comments raised the possibility of setting a *de minimis* threshold "based on the amount of conflict minerals used by issuers … in their overall enterprise." Release No. 34-63547, 2010 WL 5121983, at *29 (Dec. 15, 2010). In promulgating the final rule, however, the SEC inexplicably failed to consider this alternative, even for companies that have only trace amounts overall, for instance from using catalysts. Petr. Br. 39-40.

The SEC's arbitrary refusal to adopt any *de minimis* exception will greatly increase the rule's costs, requiring companies to expend substantial resources determining whether their products contain trace amounts of minerals added by sub-suppliers, and then to expend further resources in pointless attempts to determine the origin of minerals appearing in "parts per million or less" in a single subcomponent of a complex finished product, which might have tens of thousands of different parts. JA384; *see* ADD 114-15; Industry Br. 11-19. Because the SEC imposed this increased burden with no reasoned basis for concluding that it would help to ameliorate the conflict in the DRC, the rule should be vacated.

B. The Rule's Extension To Non-Manufacturers Is Contrary To The Statute.

Inconsistently with the release, the SEC argues that the statute "does not unequivocally indicate a congressional intent to exclude issuers who contract to have products manufactured," but rather "leave[s] the question to agency discretion." Br. 52. In the release, by contrast, the agency claimed that Congress *compelled* the interpretation, stating "we believe the statutory intent to include issuers that contract to manufacture their products is clear based on the statutory obligation for issuers to describe in their Conflict Minerals Reports products that are manufactured and contracted to be manufactured." 77 F.R. 56,291; *see* 77 F.R. 56,345 ("[T]he final rule applies to issuers that contract to manufacture products. This requirement is based on our interpretation of the statute in light of our understanding of the statutory

intent and a reading of the statute's text."). Because Congress plainly did not compel the SEC's interpretation—as even the SEC now appears to recognize—the rule must be set aside, even if the interpretation could have been permissible as an exercise of agency discretion. *Peter Pan Bus Lines*, 471 F.3d at 1354; *see Am. Bar Ass'n* , 430 F.3d at 471.

In fact, the interpretation is not even permissible, because it is contrary to the plain text of the statute. Section 1502 applies to a company only if "conflict minerals are necessary to the functionality or production of a product *manufactured* by" that company; thus, it applies only to manufacturers. 15 U.S.C. §78m(p)(2)(B) (emphasis added). Congress's intent to cover only manufacturers is further shown by its use of the phrase "contracted to be manufactured" in describing the *products* that reports must cover, but not in describing the *persons* who must file reports. *Compare* 15 U.S.C. §78m(p)(2)(B) *with* 15 U.S.C. §78m(p)(1)(A)(ii).

In its response brief, the Commission for the first time argues that, if 15 U.S.C. §78m(p)(2)(B) "is not read to encompass issuers who contract to manufacture, manufacturing issuers would be required to describe products they contract to have manufactured that are not DRC conflict free in a Conflict Minerals Report without being required to perform the due diligence the statute requires to make this determination," rendering the statute "internally inconsistent." Br. 53. This new argument relies upon an erroneous reading of §78m(p)(1)(A). Section 78m(p)(1)(A) states that a person must disclose "whether conflict minerals that are necessary as

described in paragraph (2)(B) … did originate" in the DRC, and must describe its due diligence measures regarding "such minerals." The provision does not cross-reference §78m(p)(2)(B) in its entirety, but only references "minerals *that are necessary* as described in paragraph (2)(B)"—in other words, minerals that "are necessary to the functionality or production of a product," 15 U.S.C. §78m(p)(1)(A), (p)(2)(B). The Commission's brief's broader reading of §78m(p)(1)(A) to incorporate all the language in §78m(p)(2)(B) would render the words "that are necessary" superfluous, and therefore must be rejected. *Conference of State Bank Supervisors v. Conover*, 715 F.2d 604, 627 (D.C. Cir. 1983) ("[I]n construing a statute, we are obliged to give effect, if possible, to every word Congress used.").

Finally, the SEC's interpretation would be arbitrary and capricious even if the statute were ambiguous and the agency had exercised discretion. As the SEC has admitted, it imposed significant burdens on non-manufacturing issuers without determining whether such burdens are necessary or appropriate or would yield any benefits. 77 F.R. 56,345; *see* ADD-104 (estimating that compliance costs for a single non-manufacturing issuer could be hundreds of thousands of dollars in 2013 alone).[5] That was error, and the rule should be vacated.

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[5] The SEC's suggestion that all the Petitioners agreed with the rule's extension to non-manufacturers in their comments is inaccurate. *See* JA260.

C. The Commission Misinterpreted the Statute's "Did Originate" Requirement And Imposed Unnecessary Burdens.

Although, in the release, the SEC appeared to require companies to trace their supply chains back to the mineral processing facility, the agency now concedes that such tracing is not required, and that companies may alternatively comply with the rule by using flow-down clauses in supplier contracts. Br. 59. However, the SEC's "reasonable country of origin inquiry" still suffers from a separate error: the agency's replacement of the statute's "did originate" standard with a "may have originated" standard. That interpretation is inconsistent with the statutory text, because the statute plainly imposes due diligence and reporting obligations only on issuers whose minerals "did originate" in the DRC region.

Contrary to the SEC's characterization, Petitioners are not arguing that only issuers who "know with certainty" that their minerals originated in the DRC region can be required to conduct due diligence. Br. 55. Rather, Petitioners argue that the SEC's extremely broad standard, requiring due diligence and reports not only when there is "reason to believe" that the minerals "did originate" in the region, but also whenever there is "reason to believe" that the minerals "*may have* originated" in the region, is inconsistent with the statute. While the SEC argues that the "reason to believe" component of this standard is necessary to prevent issuers from ignoring "red flags," Br. 58, it offers no basis for its decision to replace the statutory term "did" with the far looser "may have." Indeed, at points, the SEC appears to

mischaracterize its own standard, stating "under the final rule the disclosure requirement applies only to issuers who know that their conflict minerals originated in the Covered Countries or had reason to believe that they *did*." Br. 64 (emphasis added).

The change from "did" to "may have" vastly broadens the reach of the rule. Any issuer who is unable to determine the origin of its minerals after a reasonable, good-faith inquiry (for instance, because the issuer has an extremely complex supply chain, or its suppliers refuse to provide information), could be said to have a "reason to believe" that the minerals "may have originated" in the DRC region, merely because a certain percentage of the global supply of the minerals originates there. Indeed, the rule requires issuers to conduct due diligence and to submit a report if the origin of their minerals is "undeterminable," even if no red flags are present. 77 F.R. 56,321-22. There is simply no basis in the statute for imposing this requirement, which will greatly increase the rule's costs.[6]

[6] While the SEC claims that recent "advances in infrastructure" will make compliance easier, Br. 57, record evidence from 2011 reflects the extreme difficulty of attempting to determine if minerals "may have originated" in the DRC region. *See* JA630; JA422. Further, while the SEC and *amici* point out that Apple has reportedly mapped its supply chain, Apple's supply chain is relatively simple, consisting of only a few hundred suppliers of the minerals. http://www.apple.com/supplierresponsibility/code-of-conduct/labor-and-human-rights.html. Other companies have tens of thousands of such suppliers, making such mapping far more difficult. *See* JA590; JA571; JA630. And the OECD's 2013 report on its conflict minerals pilot program confirms that while some progress has been made, supply chain tracing remains extremely challenging. OECD, *Downstream*

D. The Phase-in Period Is Arbitrary And Capricious.

The SEC arbitrarily provided a shorter phase-in period for larger issuers, even though it recognized that "smaller companies are part of larger companies' supply chains and would need to provide conflict minerals information so that larger companies could meet their obligations under the rule." 77 F.R. 56,361. The SEC contends that this structure is reasonable because larger companies have "greater leverage," Br. 61, but fails to explain how this supposed leverage will help when small suppliers, as the SEC acknowledges, will be unable to obtain the requested information. 77 F.R. 56,323. Further, the SEC cannot contend that an issuer, simply because it is a larger company, will necessarily have leverage not only over its own direct suppliers, but also over the entire global supply chain, including foreign companies with numerous customers not subject to the rule. *See* Petr. Br. 10; JA160; JA422-23; JA631.

E. The Commission's Errors Require Vacatur.

The deep deficiencies in the Commission's economic analysis and statutory interpretation require vacatur, particularly given the rule's enormous initial compliance costs. *Comcast Corp. v. FCC,* 579 F.3d 1, 8 (D.C. Cir. 2009). Indeed, the Commission

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Implementation of the OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas 35-36, 40-42, 58-59 (Jan. 2013), *available at* http://www.oecd.org/daf/inv/mne/DDguidanceTTTpilotJan2013.pdf.

does not dispute that vacatur is appropriate if the Court grants the petition, and states only that "the appropriate remedy is assessed on a case-by-case basis." Br. 67.

III. SECTION 1502 VIOLATES THE FIRST AMENDMENT.

Section 1502 violates the First Amendment by compelling misleading and unfairly stigmatizing speech connecting a company's products to terrible human rights abuses. The SEC and Intervenors contend that this compelled speech passes *Zauderer* rational basis scrutiny, but that relaxed standard does not apply. *See Zauderer v. Office of Disciplinary Counsel of Supreme Ct. of Ohio*, 471 U.S. 626 (1985). First, *Zauderer* applies only when "the government shows that, absent a warning, there is a self-evident—or at least potentially real—danger that an advertisement will mislead consumers." *R.J. Reynolds Tobacco Co. v. FDA*, 696 F.3d 1205, 1214 (D.C. Cir. 2012). Here, neither the SEC nor Intervenors even argue that there is a danger issuers would mislead consumers in the absence of Section 1502. And for good reason: The purpose of the compelled speech is not to protect consumers, but only to serve as a "scarlet letter," *Gallagher Dissent*, JA710, "stigmatiz[ing] the company and harm[ing] its business," JA246. Intervenors correctly concede that their argument is inconsistent with *R.J. Reynolds*. Intervenors Br. 40-41 (arguing only that the case was wrongly decided).

Furthermore, even in the unlikely event that *R.J. Reynolds* were overturned, the SEC's argument still fails, because the compelled speech is not "purely factual and uncontroversial." *Zauderer*, 471 U.S. at 651. Under the statutory definitions, products are not "DRC conflict free" if they "contain minerals that directly or indirectly finance

or benefit armed groups" that "perpetrat[e] … serious human rights abuses" in the DRC. Section 1502(e)(3); 15 U.S.C. §78m(p)(1)(A)(ii), 78m(p)(5). These disclosures are fraught with uncertainty and "pregnant with political judgments and connotations," JA187; *see* Petr. Br. 8-15, and they unmistakably associate the issuer with human rights abuses, suggesting at least partial responsibility, if not complicity. Moreover, the compelled speech will mislead consumers because it lumps together companies that "directly or indirectly finance or benefit armed groups" with those who have no connection at all with the groups and who simply cannot confirm that their vast web of suppliers and sub-suppliers are "conflict free." JA244-46

This regime is nothing like the "routine disclosures" "designed to forward ordinary regulatory purposes," Br. 62, that courts have upheld under *Zauderer*. *See, e.g.*, *Spirit Airlines, Inc. v. U.S. Dep't of Transp.*, 687 F.3d 403 (D.C. Cir. 2012) (upholding a requirement that airlines display prominently the total final price of airfare); *Nat'l Elec. Mfrs. Ass'n v. Sorrell*, 272 F.3d 104 (2d Cir. 2001) (upholding a requirement that companies label products as containing mercury, and state that the mercury must be removed before disposal); *see also CTIA– The Wireless Ass'n v. City of S.F.*, 2012 WL 3900689 (9th Cir. Sept. 10, 2012) (refusing to apply *Zauderer* review, and striking down a required disclosure suggesting cell phone energy emissions are dangerous to health, because there was an ongoing debate as to their health effects).

Relying on *Meese v. Keene*, 481 U.S. 465 (1987), the SEC argues that the stigmatizing nature of the compelled disclosure does not prevent it from being

"purely factual and uncontroversial." Br. 64-65. But *Meese* was not a compelled speech case: While the *government* characterized the communications at issue as "political propaganda," it did not require any private party to do so. 481 U.S. at 467. Furthermore, the Court upheld the use of the term "political propaganda" precisely because it found that the statute defined the term as a "neutral one rather than a pejorative one." *Id.* at 483. The purpose of the "not DRC conflict free" label, by contrast, is to expose issuers to opprobrium from investors and consumers. *Gallagher Dissent*, JA710.

Intervenors—but not the SEC—additionally argue for a relaxed standard of review on the basis that Section 1502 regulates the "purchase and sale of securities." Intervenors Br. 36-41; *see Full Value Advisors, LLC v. SEC*, 633 F.3d 1101, 1108-09 (D.C. Cir. 2011) (applying doctrine to requirement to disclose to Commission "the names, shares, and fair market value of the securities over which the institutional managers exercise control"); *SEC v. Wall St. Publ'g Inst.*, 851 F.2d 365, 372 (D.C. Cir. 1988) (applying doctrine to requirement to disclose payments accepted in exchange for speech encouraging purchase of securities). But Section 1502 does not regulate "speech employed directly or indirectly to sell securities." *Wall St. Publ'g*, 851 F.2d at 373. Instead, as the SEC itself recognizes, Section 1502 is intended to achieve "social benefits … quite different from the economic or investor protection benefits that our rules ordinarily strive to achieve," and "the objectives of Section 1502 do not appear to be those that will necessarily generate measurable, direct economic benefits to

investors or issuers." 77 F.R. 56,335; *see* Commissioner Daniel M. Gallagher, *Remarks before the Corporate Directors Forum* (Jan. 29, 2013) ("[A]lthough couched as [a] disclosure rule[]," Section 1502 is "in fact meant to affect the behavior of companies and boards rather than to provide information" that would be "material to the general population of investors."). The relaxed *Wall Street Publishing* standard cannot apply here; if it did, then Congress could evade First Amendment scrutiny for *any* speech restrictions on public companies, no matter how far removed from the traditional domain of the securities laws, and no matter how false or misleading, simply by codifying them in chapter 15 of the United States Code.

Accordingly, heightened scrutiny applies, and the statute is unconstitutional. The Court should apply strict scrutiny, because the disclosures are not commercial. But the statute also fails intermediate scrutiny, because it does not "directly and materially advance[]" the government's interest in ameliorating the DRC conflict. *R.J. Reynolds*, 696 F.3d at 1212. "[M]ere speculation or conjecture" is insufficient to uphold a speech restriction. *Id.* at 1219. Rather, Congress must "base its conclusions" about the efficacy of a speech restriction "upon substantial evidence." *Turner Broad. Sys., Inc. v. FCC*, 520 U.S. 180, 196 (1997). Here, "substantial evidence" that disclosure requirements on U.S. public companies will ameliorate the violent conflict in the DRC is plainly lacking. All the SEC points to is Congress's say-so, and that is clearly inadequate. *See, e.g.*, *Edenfield v. Fane*, 507 U.S. 761, 770-71 (1993) ("[A]

governmental body seeking to sustain a restriction on commercial speech must demonstrate that … its restriction will in fact alleviate [harms] to a material degree.”).

Indeed, any assertion that the disclosure regime will improve the situation in the DRC rests not on a “common sense” assumption, *Nat’l Ass’n of Mfrs. v. Taylor*, 582 F.3d 1, 16 (D.C. Cir. 2009), but rather upon a long string of dubious conjectures: for instance, that companies will be able to determine the origins of minerals contained in their products; that the compelled disclosures will result in less sourcing of minerals that benefit armed groups; that the compelled disclosures will *not* result in a devastating *de facto* embargo on the entire region; that demand from foreign companies will not “offset any reduction in the demand from U.S. companies”; and that warlords will not successfully smuggle minerals or find “other ways to finance their violence.” *Paredes Dissent*, JA716; *see* Petr. Br. 17-18, 29-30. As the SEC admits, the accuracy of these conjectures was “fiercely debat[ed]” in the record, Br. 24; *see* JA427; JA669; JA554-55, and the agency itself was “not able to assess how effective Section 1502 will be in achieving those benefits,” 77 F.R. 56,335. Under these circumstances, compelling this highly stigmatizing, misleading, and burdensome speech violates the First Amendment.

CONCLUSION

For the foregoing reasons, Petitioners request that their petition for review be granted, that the conflict minerals rule be vacated, and that 15 U.S.C. §78m(p) be struck down.

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Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

In accordance with Circuit Rule 32(a) and Rule 32(a)(7) of the Federal Rules of Appellate Procedure, the undersigned certifies that the accompanying brief has been prepared using 14-point Garamond Roman typeface, and is double-spaced (except for headings and footnotes).

The undersigned further certifies that the brief is proportionally spaced and contains 6,960 words exclusive of the table of contents, table of authorities, glossary, signature lines, and certificates of service and compliance. The words of Petitioners' Final Reply Brief do not exceed 7,000 words, as mandated by Fed. R. App. P. 32(a)(7)(B)(ii). The undersigned used Microsoft Word 2007 to compute the count.

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CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of March, 2013, I electronically filed the foregoing Final Reply Brief of Petitioners with the Clerk of the Court using the CM/ECF System, which will send notice of such filing to all registered CM/ECF users.

Pursuant to D.C. Circuit Rules 25 and 31, and the Court's Order of November 27, 2012, an original and eight (8) paper copies of the foregoing brief will be hand-delivered to the Clerk of the Court.

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