

Tackling Standard Of Review For Compelled Corporate Speech

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The U.S. Securities and Exchange Commission is hoping for another bite at the apple in the legal controversy surrounding its conflict minerals rule (“CM rule”). At the same time, an unrelated case raising nearly identical First Amendment issues is currently awaiting rehearing en banc in the D.C. Circuit. The case, *American Meat Institute v. U.S. Department of Agriculture*, involves an industry challenge to the USDA’s country-of-origin labeling (“COOL”) requirements for meat.[1]

The panel’s decision in *American Meat* may impact the court’s recent ruling in *National Association of Manufacturers (“NAM”) v. SEC*, which stayed one of the CM rule’s reporting requirements — that some products be described as “not found to be DRC conflict free” — on First Amendment grounds.[2] On May 29, 2014, the SEC and intervenor Amnesty International petitioned for rehearing en banc of the portion of the NAM opinion addressing First Amendment arguments, and to hold that case in abeyance pending the *American Meat* decision. Both cases turn on the same question: What is the appropriate standard of review in First Amendment cases involving compelled corporate speech?



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Separate D.C. Circuit three-judge panels previously reached opposing conclusions on the First Amendment issue in the two cases. On March 28, 2014, the court decided *American Meat* in favor of the USDA after applying rational basis review, the lowest standard of review, to the agency’s COOL requirements. Under rational basis review, an agency needs only to show that its rule is “reasonably related” to a legitimate state interest. Just two weeks later, the D.C. Circuit subjected the SEC’s CM rule to a heightened standard of intermediate scrutiny, which requires any speech restriction to be “narrowly tailored” to achieve the government’s goal.

Because the SEC did not show that less restrictive means (such as allowing companies to use their own language to describe their products) would fail to meet the government’s goal, certain disclosure requirements under the CM rule were found to violate the free speech rights of covered companies. By the time *NAM* was decided, the D.C. Circuit had vacated the earlier *American Meat* decision and granted rehearing en banc on the question of whether corporate disclosure mandates are subject to rational basis or intermediate scrutiny review.[3]

To answer the question as to which standard of review is appropriate, the D.C. Circuit must decide how it will interpret the U.S. Supreme Court's holding in *Zauderer v. Office of Disciplinary Counsel*.^[4] In *Zauderer*, the Supreme Court stated that "[t]he right of a commercial speaker not to divulge accurate information regarding his services is not ... a fundamental right" and applied rational basis review to advertising disclosure requirements designed to prevent consumer deception. ^[5] The court did not specify the scope of disclosure requirements to be reviewed under *Zauderer*'s rational basis standard. Nevertheless, all parties agree that *Zauderer* requires at least the following three criteria to be met for the lower standard of rational basis review to apply:

1. The affected speech is commercial speech;
2. The requirement is restrictive only in the sense of requiring a disclosure; and
3. The required disclosure is of "purely factual and non-controversial" information.

Both the COOL and CM rule reporting requirements clearly satisfy conditions 1 and 2. The COOL rule fulfills the third criteria as well since the content of its mandated disclosures is value-neutral (something the AMI challengers do not dispute). However, the NAM parties debate whether the CM rule meets this prerequisite. As the panel majority in NAM pointed out, the CM rule's disclosure requirements may amount to forcing a company to confess to "blood on its hands." This is the key distinction between NAM and American Meat and is likely the biggest weakness in the SEC's petition. Thus, even if the American Meat review panel upholds the finding that *Zauderer* rational basis applies to the COOL rule, the First Amendment ruling in NAM may not be affected.

Since all parties agree that the COOL rule meets each of these criteria, however, the issue in the American Meat rehearing is whether *Zauderer* requires a fourth precondition for rational basis review:

4. The disclosure requirement must be related to the state's interest in preventing consumer deception.

There is a circuit split on this issue. The First, Second and Sixth Circuits interpret *Zauderer* as applying to corporate speech restrictions concerning a broad range of government interests. In contrast, the D.C. Circuit's decision in *R.J. Reynolds* arguably limited *Zauderer*'s rational basis standard to apply only to those commercial disclosure mandates aimed at avoiding consumer deception.^[6] The original three-judge panel in American Meat rejected this interpretation of *R.J. Reynolds*, while the NAM panel accepted it.

The American Meat en banc panel must therefore decide if D.C. courts are indeed bound by a reading of *R.J. Reynolds* that restricts *Zauderer*'s application to a narrow subset of commercial free speech cases. If the en banc panel confirms a broad reading of *Zauderer* in light of *R.J. Reynolds*, then the court will apply rational basis to the COOL rule and is likely to uphold it once more. Such a holding could also provide grounds for reviewing the NAM decision to determine if the court should re-analyze the CM rule under rational basis instead of intermediate scrutiny review. (First, though, the court would need to find that the CM rule fulfills condition 3 above.)

On the other hand, the American Meat review panel may agree with the NAM majority and hold that *R.J. Reynolds* limits *Zauderer*'s application to cases involving rules intended to prevent consumer deception. This would confirm the circuit split and establish that in the D.C. Circuit, *Zauderer*'s rational basis standard only applies to commercial speech mandates concerning a government interest in curing consumer deception. The court must then apply intermediate scrutiny — and not rational basis — to

both the COOL and CM rule rules, since no party has suggested that either rule is related to consumer deception. Under these circumstances, there are likely no grounds for rehearing NAM.

Conclusion: What Does This Mean for Covered Companies?

Covered companies should not expect relief from CM rule obligations as a result of American Meat. At best, the D.C. Circuit will decline to reconsider the First Amendment issues in NAM. In that scenario, the partial stay — which means that covered companies are not required to designate their products as “DRC conflict free,” having “not been found to be DRC conflict free,” or “DRC conflict undeterminable” — will presumably continue.

However, companies should not expect significant new burdens either. At worst, the court will review the CM rule disclosure requirements under a lower standard of scrutiny. If the court finds that the mandated disclosures are constitutional under rational basis review, it will presumably lift the partial stay. Companies will be then required to make disclosures using the SEC terminology instead of their own words.

At least two hurdles must be overcome for the D.C. Circuit to reconsider NAM’s partial stay: (1) the American Meat panel must decide that Zauderer rational basis review applies broadly to compelled factual corporate speech and not just mandates aimed at preventing consumer deception; and (2) the court, upon agreeing to rehear NAM, must find that the CM rule requires only “purely factual and noncontroversial” disclosures. Because of this second factor, the American Meat outcome is not necessarily dispositive of NAM. If both findings do not occur, the partial stay resulting from NAM will remain in force.

In any event, covered companies will remain on the hook for the bulk of the CM rule’s filing and reporting requirements. The initial D.C. Circuit NAM decision upheld the vast majority of the CM rule’s provisions, and these portions of the opinion are likely to remain intact. Therefore, covered companies should continue with their reasonable country of inquiry, due diligence, and audit efforts as before.

In fact, companies may benefit from describing their products using SEC terminology even if the partial stay remains in place. Voluntarily identifying products by these designations can indicate a commitment to transparency. Furthermore, the “DRC conflict free” label signals good corporate social responsibility practices. While a company that elects to use this classification must obtain an independent private sector audit, getting products verified as “DRC conflict free” may actually reduce future reporting burdens.

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[1] Am. Meat Inst. v. USDA, No. 13-5281 (D.C. Cir. Mar. 28, 2014) (en banc oral argument held May 19, 2014).

[2] Nat'l Ass'n of Mfrs. v. SEC, No. 13-5252 (D.C. Cir. Apr. 14, 2014).

[3] Judge Srinivasan -- the only judge to sit on the 3-judge panels in both American Meat and NAM -- issued a concurrence in NAM noting that the panel should have held its consideration of the First Amendment claims in abeyance pending the en banc court's decision in American Meat.

[4] Zauderer v. Office of Disciplinary Counsel, 471 U.S. 626 (1985).

[5] *Id.* at 651.

[6] R.J. Reynolds Tobacco Co. v. FDA, 696 F.3d 1205 (D.C. Cir. 2012).