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RECENT RULING PROVIDES ROADMAP FOR POTENTIAL DODD-FRANK CHALLENGES

August 30, 2011

Last month's ruling by the U.S. Court of Appeals for the District of Columbia Circuit (the "Court") in the closely watched case of *Business Roundtable v. SEC*[1] not only overturned the landmark Securities and Exchange Commission (the "SEC") shareholder proxy access rule, but also created a potential roadmap for businesses and industry groups seeking to challenge many other rules to be issued by the SEC and other federal regulators under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"). In holding that the SEC acted "arbitrarily and capriciously" and failed to adequately assess the economic effects of the new proxy access rule, the Court put the SEC and other regulators on notice that future rulemaking by the agencies must meet a much higher standard with respect to cost-benefit analysis and justification.

Businesses and industry groups have been quick to seize on the Court's holding as a basis for challenging other Dodd-Frank rulemaking by the SEC and the Commodity Futures Trading Commission (the "CFTC") – especially those rules that received considerably less cost-benefit analysis than the proxy access rule.[2] Observers believe that controversial rules such as the new or pending SEC conflict minerals disclosure rules,[3] compensation disclosure rules[4] and whistleblower rules[5] may be particularly vulnerable to a challenge

[1] Business Roundtable and Chamber of Commerce of the United States of America v. Securities and Exchange Commission (D.C. Cir. July 22, 2011), available at http://www.cadc.uscourts.gov/internet/opinions.nsf/89BE4D084BA5EBDA852578D5004FBBBE/$file/10-1305-1320103.pdf. Our client alert discussing the case may be found at http://www.wcsr.com/resources/pdfs/cs072811.pdf.

[2] Ben Protess, *Court Ruling Offers Path to Challenge Dodd Frank* (August 17, 2011), available at http://dealbook.nytimes.com/2011/08/17/court-ruling-offers-path-to-challenge-dodd-frank.

[3] The SEC's conflict minerals proposals would require annual disclosures from any company for which the use of "conflict minerals," such as tantalum, tin, gold or tungsten, is necessary to the functionality or production of a product manufactured by that company. Our client alert discussing the proposals may be found at http://www.wcsr.com/resources/pdfs/cs010511.pdf.

[4] Dodd-Frank requires the SEC to adopt rules requiring companies to include in their proxy statements information discussing (i) the relationship between compensation actually paid to its executives and the financial performance of the company, (ii) internal pay equity ratios and (iii) whether any employee or director of the company is permitted to hedge against any decrease in the market value of the company's securities held by the employee or director. Our client alert discussing these requirements – which have not yet been the subject of SEC rulemaking – may be found at http://www.wcsr.com/resources/pdfs/cs092010.pdf.

[5] The SEC's new whistleblower rule (i) requires the SEC to pay an award of between 10 and 30 percent of monetary sanctions aggregating at least $1,000,000 to eligible whistleblowers who voluntarily provide the SEC with original information about a violation of the federal securities laws and (ii) prohibits retaliation by employers against

along the same lines as the SEC's proxy access rule.[6] Because it is generally not cost-effective or politically desirable for a single company to challenge the rules directly, it is expected that the majority of these suits will be brought by influential trade groups, such as the U.S. Chamber of Commerce.

Dodd-Frank contains more than 300 provisions that expressly require or permit rulemaking by federal agencies. Many of the mandatory rulemaking provisions specify the details of the rules to be issued, but some discretionary provisions allow agencies to issue such rules as may be necessary. Most of the rulemaking provisions in Dodd-Frank do not indicate how the regulations should be developed.[7] However, the Administrative Procedure Act imposes certain procedural requirements on rulemaking by federal agencies, and the Securities Exchange Act of 1934 and the Investment Company Act of 1940 both require regulatory authorities to consider a rule's effect on efficiency, competition and capital formation when determining whether it is necessary or appropriate or in the public interest.

In *Business Roundtable v. SEC*, the plaintiffs challenged the Dodd-Frank-mandated proxy access rule, arguing that the SEC failed adequately to consider the rule's effect upon efficiency, competition and capital formation, including, among other things, the costs companies would have incurred in opposing shareholder nominees and the consequences of union and state pension funds using the rule. Despite the more than 60 pages of cost-benefit analysis contained in the new rule and the approximately 21,000 SEC staff hours dedicated to drafting the rule over a two-year period,[8] the Court held that the SEC "inconsistently and opportunistically framed the costs and benefits of the rule; failed adequately to quantify the certain costs or to explain why those costs could not be quantified; neglected to support its predictive judgments; contradicted itself and failed to respond to substantial problems raised by commenters."

The Court's decision in *Business Roundtable v. SEC* may not only encourage legal challenges to Dodd-Frank rulemaking by federal agencies, but may also delay the rulemaking process itself. As of July 2011, less than 13% of the new regulations required by Dodd-Frank had been fully adopted.[9] The SEC recently announced yet another new timeline for adoption of future rules, pushing back final adoption dates for many rules well into 2012. Similarly, the CFTC announced that it would delay the effectiveness of certain Dodd-Frank regulations until as late as the end of 2011 in order to re-examine the status of final rulemaking in light of the changed regulatory landscape.

We will continue to monitor future rulemaking actions in the Dodd-Frank arena. If you have any questions regarding these recent developments, please contact Elizabeth Southern (http://www.wcsr.com/ElizabethSouthern), or Charles A. Edwards (http://www.wcsr.com/lawyers/charles-edwards), the principal drafters of this client alert, or you may contact the Womble Carlyle attorney with whom you usually work or one of our Corporate and Securities attorneys at the following link:

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individuals who provide the SEC with information about possible securities violations. Our client alert summarizing the whistleblower rule may be found at http://www.wcsr.com/resources/pdfs/cs061311.pdf.

[6] See S. Lynch and C. Doehring, *Factbox: Five Endangered Dodd-Frank Rules* (August 4, 2011), available at http://www.reuters.com/article/2011/08/04/us-financial-regulation-courts-fb-idUSTRE7730KU20110804, and Jean Eaglesham, *As Business Takes Aim at Dodd-Frank, Battle Shifts to Courts* (July 29, 2011), available at http://online.wsj.com/article/SB10001424053111904772304576470313933175814.html?mod=WSJ_hp_MIDDLENexttoWhatsNewsThird.

[7] Curtis W. Copeland, *Rulemaking Requirements and Authorities in the Dodd-Frank Wall Street Reform and Consumer Protection Act* (November 3, 2010), available at http://www.llsdc.org/attachments/files/255/CRS-R41472.pdf.

[8] Bloomberg News, *Proxy Access, Deere-FCPA, Basel Capital Rules: Compliance* (August 12, 2011), available at http://www.bloomberg.com/news/2011-08-12/proxy-access-rule-deere-fcpa-basel-capital-rules-compliance.html.

[9] Reese Darragh, *SEC Faces More Scrutiny After Court Spiked Rule* (Compliance Week, August 23, 2011).

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