Client Alert

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SEC Offers Guidance on Use of Social Media for Public Disclosure

By David M. Lynn

On April 2, 2013, the SEC issued guidance in the form of the Report of Investigation under Section 21(a) of the Securities Exchange Act of 1934 (the "Exchange Act") which indicates that social media channels − such as Twitter and Facebook − could be used by public companies to disseminate material information, without running afoul of Regulation FD.[1] The SEC emphasized that companies should apply the guidance from its 2008 interpretive release regarding the disclosure of material information on company websites when analyzing whether a social media channel is in fact a "recognized channel of distribution," including the guidance that investors must be provided with appropriate notice of the specific channels that a company will use in order to disseminate material nonpublic information.[2]

WHY DID THE SEC PROVIDE THIS GUIDANCE IN THE FORM OF A SECTION 21(A) REPORT?

Section 21(a) of the Exchange Act authorizes the SEC to investigate violations of the federal securities laws and, in its discretion, "to publish information concerning any such violations." Section 21(a) reports are informational, in that they do not represent an adjudication of the facts or issues addressed, but rather express the SEC's views regarding the matters discussed in the report. Because the Report of Investigation under Section 21(a) describes the views of the SEC, it can serve as authoritative interpretive guidance on the matters discussed, much like an SEC interpretive release. In the course of an investigation of a potential Regulation FD violation arising from a CEO's Facebook post, the SEC staff learned that there was uncertainty as to how the 2008 Guidance should apply in the context of releasing information through social media channels, so the SEC determined that the 21(a) Report would serve as a vehicle for communicating how to apply Regulation FD and the 2008 Guidance to communications made through social media channels. The SEC did not initiate an enforcement action or allege wrongdoing in connection with issuing the 21(a) Report.

HOW DOES REGULATION FD POTENTIALLY APPLY TO COMMUNICATION THROUGH SOCIAL MEDIA CHANNELS?

In response to the concerns about the threat of selective disclosure of material nonpublic information by companies, the SEC adopted Regulation FD in 2000. Regulation FD requires an issuer that discloses material nonpublic information to certain individuals (generally holders of the issuer's securities and securities market professionals) to also make the information publicly available. The required timing of the public disclosure depends on whether the issuer selectively disclosed the information intentionally or not. For an intentional selective disclosure, the issuer must simultaneously present the information to the public. If the issuer made the selective disclosure unintentionally, the information has to be presented to the public promptly thereafter.

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[1] *Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: Netflix, Inc., and Reed Hastings*, Release No. 34-69729 (April 2, 2013) (the "21(a) Report").

[2] *Commission Guidance on the Use of Company Web Sites*, Release No. 34-58288 (August 7, 2008) (the "2008 Guidance").

In order to comply with Regulation FD, a company must consider whether information is adequately disseminated to the public. When Regulation FD was adopted, the SEC indicated that public disclosure "may be made by filing or furnishing a Form 8-K, or by another method or combination of methods that is reasonably designed to effect broad, non-exclusionary distribution of the information to the public."[3]

In the time since the SEC adopted Regulation FD, there has been a substantial increase in the amount of information that companies are regularly providing on the Internet, including on company websites. In 2000, the SEC stopped short of stating that disclosure on a company's website could be considered adequate public dissemination. At the time, the SEC indicated that "[a]s technology evolves and as more investors have access to and use the Internet," the SEC may consider a website posting to meet the public disclosure requirements of Regulation FD.

When communicating information through social media channels, a company has had to consider whether material nonpublic information is being selectively disclosed to the persons enumerated in Regulation FD, or more broadly disseminated through what would be considered a recognized channel of distribution. Prior to the release of the 21(a) Report, concerns had been expressed that: (1) social media channels did not disseminate information broadly because they are essentially "closed" channels (given that users must sign up and follow a company to get access to the information), and (2) it was not likely that investors would be inclined to first turn to a company's Facebook or Twitter account for material information about the company, instead of more established sources such as a press release, the company's website, or the SEC's EDGAR website.

WHAT DID THE 2008 GUIDANCE SAY REGARDING THE USE OF COMPANY WEBSITES?

In 2008, the SEC provided three considerations for determining whether information posted on a corporate website is considered "public":

- Is an issuer's website a "recognized channel of distribution"?
- Is information posted in a manner calculated to reach investors?
- Is information posted for a reasonable period of time so that it has been absorbed by investors?

In determining whether a company's website is a recognized channel of distribution, the analysis focuses on what the company has done to notify investors and the market of its website and disclosure policy. The SEC indicated that steps a company can take to establish its website as a recognized channel for disclosing information include:

- listing a company's website address on periodic reports and press releases;
- establishing a pattern of posting important information on its website; and
- informing investors that they can find important information about the company on its website.

In evaluating whether the posting of information on a company website disseminates the information in a manner that makes it available to the public in general, the SEC indicated that companies should focus on the manner in

[3] *Selective Disclosure and Insider Trading*, Release No. 34-43154 (August 15, 2000).

which the information is posted on a company's website and the accessibility of such information. Questions that a company should consider include:

- Is the website designed to effectively direct visitors to important information?
- Is information for investors prominently displayed on the website?
- Does the media regularly pick up and report information posted on the company's website?

The SEC also noted that a company can also improve the accessibility of information on its website by utilizing "push" technology. Push technology is a type of communication that originates with a publisher of the information such as RSS feeds, in contrast to the concept of a "pull" communication, which originates with the consumer of information.

In determining if there has been a reasonable waiting period for investors to react to information posted on a company's website, the SEC indicated that the analysis depends on the circumstances of the dissemination. For a website, this means evaluating the traffic that the site generates, how often investor specific information is accessed, and the complexity of the information presented. For example, simple information posted on a website with heavy traffic that is routinely used by investors would likely be considered disseminated to the public sooner than complex information that is posted on a website with little traffic and that is not routinely used by investors.

Rule 101(e) of Regulation FD specifies that the filing or furnishing of information on a Form 8-K is sufficient to make the information public for the purposes of Regulation FD, notwithstanding any other efforts on the part of a company to utilize some broad, nonexclusionary means to disseminate that information. In public forums, the SEC Staff has indicated that an effective model for accomplishing the dissemination of information in a Regulation FD-compliant manner, at least with earnings announcements, would be to first furnish an earnings release with an Item 2.02 Form 8-K and then, following confirmation of the appearance of the filing on EDGAR, proceed with website posting of the earnings release.

The factors for determining if information has been adequately disseminated to the public for the purposes of Regulation FD are equally applicable for determining if information is publicly available for antifraud purposes. For example, a potential plaintiff or the SEC would likely not be able to successfully allege that material nonpublic information had not been adequately disclosed to the market in the course of trading by a company in its own securities if the company had taken the necessary steps discussed above to disseminate the information.

In order to facilitate an ongoing determination that a company's website is a recognized channel of distribution of material information concerning the company, the 2008 Guidance suggested that the company take the following steps:

- In all company communications to investors, include a statement that the company routinely posts all important information about the company on its website, and include a reference to the URL of the company's website.
- Consider including a separate means to access the investor relations pages of the company's website from the main page of the website so that it is more readily apparent where investors may locate important information about the company that is posted on the company's website.

- Monitor the dissemination of information to determine the extent to which information reaches intended audiences and the extent to which persons access the company's website for material information about the company.

Issuers have continued to struggle with applying the SEC's guidance in practice, given the difficulty in making judgments about the nature of an issuer's website as a communications channel. As a result, practices have not significantly changed regarding how information is disseminated in order to make the information public or to comply with Regulation FD's public disclosure requirement.

HOW DOES THE 21(A) REPORT APPLY THE 2008 GUIDANCE IN THE CONTEXT OF SOCIAL MEDIA CHANNELS?

The SEC confirmed in the 21(a) Report that Regulation FD applies to social media and other emerging means of communication used by public companies in the same way that it applies to company websites as discussed in the 2008 Guidance, which clarified that websites can serve as an effective means for disseminating information if investors have been made aware that they can locate the company information on the website.

The 21(a) Report indicates that, while every situation must be evaluated on its own facts, disclosure of material nonpublic information on the personal social media site of an individual corporate officer, without advance notice to investors that the social media site may be used for this purpose, is unlikely to qualify as an acceptable method of disclosure under securities laws. In this regard, the SEC notes that it would not normally be assumed that the personal social media sites of public company employees would serve as channels through which the company discloses material nonpublic information.

The SEC acknowledges in the 21(a) Report that the ways in which companies may use social media channels are not fundamentally different from the ways in which the websites, blogs, and RSS feeds addressed by the 2008 Guidance are used. In revisiting the 2008 Guidance in the context of social media channels, the SEC notes that the 2008 Guidance was designed to be flexible and adaptive, and therefore provides issuers "with a factor-based framework for analysis, rather than static rules applicable only to web sites." In analyzing whether a website is recognized channel of distribution, the SEC notes:

The central focus of this inquiry is whether the company has made investors, the market, and the media aware of the channels of distribution it expects to use, so these parties know where to look for disclosures of material information about the company or what they need to do to be in a position to receive this information.

In analyzing the applicability of Regulation FD to any communications, the SEC notes that while the Regulation FD adopting release highlighted concerns about "selective" disclosure of information to favored analysts or investors, "the identification of the enumerated persons within Regulation FD is inclusive, and the prohibition does not turn on an intent or motive of favoritism." The SEC also emphasizes that nothing in the Regulation FD would suggest that disclosure of material nonpublic information to a broader group that includes *both* enumerated and non-enumerated persons, but that still would not constitute a public disclosure, would somehow result in Regulation FD being inapplicable. Rather, the SEC states that "the rule makes clear that public disclosure of material nonpublic information must be made in a manner that conforms with Regulation FD whenever such information is disclosed to any group that includes one or more enumerated persons." As a result, whenever a company makes a disclosure to an enumerated person, including to a broader group of recipients through a social media channel, the company must consider whether that disclosure implicates Regulation FD, including determining whether the disclosure includes material nonpublic information and whether the information was

being disseminated in a manner "reasonably designed to provide broad, non-exclusionary distribution of the information to the public" in the event that the issuer did not choose to file a Form 8-K.

Drawing on the reference to "push" technologies (such as email alerts, RSS feeds and interactive communication tools, such as blogs) in the 2008 Guidance, the SEC acknowledged that social media channels are an extension of these concepts, and therefore the guidance should apply equally in the context of social media channels. Given the "direct and immediate communication" possible through social media channels, such as Facebook and Twitter, the SEC expects companies to examine whether such channels are recognized channels of distribution. In particular, the SEC emphasized the need to take steps to alert the market about which forms of communication a company intends to use for the dissemination of material nonpublic information. The SEC notes that without this sort of notice, the investing public would have to keep pace with a "changing and expanding universe of potential disclosure channels." The ways in which such notice could be provided would include: (1) references in periodic reports and press releases on the corporate website and disclosures that the company routinely posts important information on that website and (2) disclosures on corporate websites identifying the specific social media channels a company intends to use for the dissemination of material nonpublic information (thereby giving people the opportunity to subscribe to, join, register for, or review that particular channel).

WHAT SHOULD PUBLIC COMPANIES DO NOW IN LIGHT OF THIS GUIDANCE?

In light of the SEC's guidance, companies should consider whether to specifically address the use of social media in Regulation FD policies, including whether prohibitions, restrictions or editorial oversight should be implemented to govern the use of social media by those persons authorized to speak for the company. This will remain an evolving area that must be continually monitored, as the methods for interacting with shareholders, analysts and others continue to evolve. As with the 2008 Guidance, companies may not be in a position to implement the 21(a) Report's guidance in such a way that they could do away with more traditional forms of public dissemination, but the guidance may provide more comfort for companies using social media to supplement other more traditional forms of communication. Companies should carefully evaluate what social media channels may be useful for communicating information, and begin providing notice that information about the company may be found on those social media channels, while using those channels as a regular source of information. At the same time, companies should advise individual officers, directors and employees that posting information about the company on social media channels could potentially implicate Regulation FD, and therefore such persons must exercise caution when communicating through social media.

Whenever using social media channels as a means of communicating information, companies should also be cognizant of other securities law considerations that were not addressed in the 21(a) Report, such as:

- identifying forward-looking statements and accompanying them with meaningful cautionary statements identifying important factors that could cause actual results to differ materially from the forward-looking statements;
- addressing the requirements of Regulation G, which requires that the companies reconcile non-GAAP financial information to a comparable GAAP financial measure;
- avoiding the risks of "entanglement" when referencing, and especially when linking to, online content that a company does not control (including activity such as "friending" an analyst on Facebook or tweeting an analyst's tweets on Twitter), which could potentially be construed as adoption of any statements about a company included in that content;

- avoiding potential liability for a material misstatement or omission in public communications, particularly given the rapid and often informal nature of the communications through social media channels;
- addressing filing and other requirements in the event communications through social media may be deemed proxy solicitations under the SEC's rules; and
- avoiding potential problems in connection with public and private securities offerings, including social media communications that could potentially result in impermissible general solicitation or general advertising in connection with a private offering and gun-jumping or conditioning the market in connection with public offerings.

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