

E-ALERT | Securities

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SEC ENDORSES SOCIAL MEDIA AS PUBLIC DISCLOSURE CHANNEL

On April 2, 2013, the Securities and Exchange Commission (SEC) issued a report under Section 21(a) of the Securities Exchange Act of 1934 (the Report) that confirms public companies and their officers may use social media sites such as Facebook and Twitter to disclose material information, so long as they alert investors in advance that such information would be disseminated in this manner.¹ Previously, it was unclear what action would be required for a company to safely conclude that disclosure of material information through a social media channel was sufficient for purposes of complying with Regulation FD, the SEC's regulation prohibiting the selective disclosure of material non-public information. The Report confirms that social media disclosures are capable of complying with Regulation FD and clarifies that companies contemplating disclosure through social media should apply the analytic framework articulated by the SEC in its 2008 interpretive release addressing the disclosure of material information on company websites, blogs and RSS feeds (the 2008 Guidance).² (See [Covington Advisory: Company Web Sites and the Securities Laws](#))

BACKGROUND

The Report arose from an SEC enforcement investigation into Netflix, Inc., and its Chief Executive Officer, Reed Hastings, following Hastings' announcement on his personal Facebook page that Netflix users had streamed more than one billion hours of content in a month for the first time in June 2012. Although neither Netflix nor Hastings previously announced that Netflix information would be disclosed in this manner, Hastings' Facebook page had more than 200,000 subscribers, including equity research analysts associated with registered broker-dealers and shareholders, and the news quickly spread to blogs and mainstream financial publications. Between the time of the post and the conclusion of trading on the next business day, the price of Netflix common stock had increased approximately 16%. In December 2012, Netflix disclosed that the SEC staff had issued Wells Notices to it and Hastings indicating its intention to institute cease-and-desist proceedings and/or a civil injunctive action for violation of Regulation FD, Section 13(a) of the Exchange Act and Rules 13a-11 and 13a-15 thereunder.³ However, rather than pursue an enforcement action, the SEC issued the Report in order to provide guidance regarding the application of Regulation FD and the 2008 Guidance to disclosures made through social media channels.

REGULATION FD AND THE SEC'S 2008 GUIDANCE ON USE OF COMPANY WEBSITES

The SEC adopted Regulation FD in 2000 to prohibit the selective disclosure of material non-public information to market participants. Instead, companies are required to make "public disclosure" of such information by filing or furnishing a Current Report on Form 8-K or by disseminating the

¹ *Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: Netflix, Inc., and Reed Hastings*, SEC Rel. No. 69729 (Apr. 2, 2013), available at <http://www.sec.gov/litigation/investreport/34-69279.pdf>.

² *Commission Guidance on the Use of Company Web Sites*, SEC Rel. No. 34-58288 (Aug. 1, 2008), available at <http://www.sec.gov/rules/interp/2008/34-58288.pdf>.

³ Netflix, Inc., Current Report on Form 8-K (Dec. 6, 2012).

information in a manner “reasonably designed to provide broad, non-exclusionary distribution of the information to the public.”⁴ In its adopting release, the SEC noted that Regulation FD did not require a particular method of disclosure, but cautioned issuers that “a deviation from their usual practices for making public disclosure may affect our judgment as to whether the method they have chosen in a particular case was reasonable.”⁵ The SEC rejected the use of company websites as a stand-alone disclosure medium, but concluded that website disclosure could satisfy Regulation FD when combined with other methods, such as a press release. The SEC also allowed that website disclosure could become sufficient for purposes of Regulation FD as technology advanced and more investors had access to the Internet.

The SEC subsequently issued the 2008 Guidance in response to the increasing use of websites to communicate information to investors. The 2008 Guidance established an analytic framework to determine when website disclosure would be sufficiently “public” for purposes of Regulation FD. Specifically, the 2008 Guidance provides that information posted on a company website is public when (1) the company website is a recognized channel of distribution, (2) the website posting disseminates the information to the securities marketplace in general and (3) there has been a reasonable waiting period for investors and the market to react to the posted information. Consideration of these requirements depends on the particular facts and circumstances and the 2008 Guidance identifies a number of factors to assist issuers with each requirement. Importantly, the 2008 Guidance provides that the first and second requirements will be satisfied if a company takes sufficient steps to alert the market to its practice of disclosing material non-public information on its website.

APPLICATION OF 2008 GUIDANCE TO SOCIAL MEDIA DISCLOSURES

The Report confirms that companies may use social media to disclose material information to investors, as the SEC stated that it does not wish to inhibit the content, form, or forum of disclosure through social media channels. As many expected, the SEC extended the 2008 Guidance to confirm its application with equal force to disclosures made through social media channels. Accordingly, the Report directs public companies disclosing material information through social media to perform a careful Regulation FD analysis that is comparable to communications disseminated through traditional channels. In this regard, the SEC emphasized that any disclosure to a group that includes one or more market participants enumerated in Regulation FD should be analyzed for compliance with Regulation FD.

In applying the principles of its 2008 Guidance to disclosure through social media, the SEC stressed that an issuer must adequately notify the investing public, in advance, of the channels of distribution it will use to disclose material information. This advance notice should include information regarding the dissemination channel and the content to be distributed through such channel. In this regard, the Report notes that some social media channels are more likely than others to satisfy the 2008 Guidance criteria. In particular, the SEC stated that it is unlikely that investors would look to the personal social media sites of executives for material corporate information in the absence of advance notice that such sites would be used for this purpose. Accordingly, regardless of the number of subscribers, friends, followers or other social media contacts, it is clear that the SEC and its staff will not view an insider’s social media disclosure of material non-public information about his or her company as a Regulation FD-compliant communication unless the company previously announced that material company information would be disseminated through that medium.

⁴ Regulation FD, Rule 101(e)(2).

⁵ *Final Rule: Selective Disclosure and Insider Trading*, SEC Rel. No. 34-43154 (Aug. 15, 2000), available at <http://www.sec.gov/rules/final/33-7881.htm#>.

CONSIDERATIONS FOR PUBLIC COMPANIES

In light of the guidance contained in the SEC's Report, public companies should consider the following points when contemplating Regulation FD compliance and engaging investors through social media:

- Carefully analyze any potential disclosure of material information that would trigger application of Regulation FD. This analysis should include consulting the factors discussed in the 2008 Guidance.
- Publicly announce the social media channel(s) through which the company will disclose material non-public information and identify the type(s) of information that will be conveyed through such channel(s).
- Revisit disclosure controls and procedures to ensure their application to social media communications by or on behalf of the company and establish ground rules for corporate and personal use of social media. Disclosure controls should prohibit unauthorized disclosure of company-related information.
- Insiders should refrain from posting non-public information on their personal social media accounts unless the company has alerted investors as to the existence of the account, its status as a medium for disclosure of material information regarding the company and the type of information intended to be conveyed through the account.
- Monitor information disclosed through social media channels and its effect on the "total mix" of information available to investors. This information should be considered when making materiality decisions and drafting disclosure for the company's SEC filings.
- Carefully monitor forward-looking statements contained in social media disclosures and include meaningful cautionary language when making such statements.

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