

2013

Regulation FD: An Alternative Approach to Addressing Information Asymmetry

Jill E. Fisch

University of Pennsylvania Law School, jfisch@law.upenn.edu

Follow this and additional works at: http://scholarship.law.upenn.edu/faculty_scholarship

 Part of the [Administrative Law Commons](#), [Business and Corporate Communications Commons](#), [Business Organizations Law Commons](#), [Corporate Finance Commons](#), [Science and Technology Law Commons](#), and the [Securities Law Commons](#)

Recommended Citation

Fisch, Jill E., "Regulation FD: An Alternative Approach to Addressing Information Asymmetry" (2013). *Faculty Scholarship*. Paper 407.

http://scholarship.law.upenn.edu/faculty_scholarship/407

This Article is brought to you for free and open access by Penn Law: Legal Scholarship Repository. It has been accepted for inclusion in Faculty Scholarship by an authorized administrator of Penn Law: Legal Scholarship Repository. For more information, please contact PennlawIR@law.upenn.edu.

Regulation FD: An Alternative Approach to Addressing Information Asymmetry

Jill Fisch*

Abstract

This chapter traces the development of the SEC's use of Regulation Fair Disclosure (FD) to address information asymmetry in the securities markets. The chapter describes the SEC's developing enforcement policy and notes, in particular, the SEC's efforts, through its selection and settlement of Regulation FD cases, to provide guidance to corporations and corporate officials about areas of key concern. The chapter concludes by highlighting current areas of particular importance, including disclosure of information through private meetings and the implications of technological innovations such as the internet and social media. The chapter is forthcoming in *Research Handbook on Insider Trading* (Stephen Bainbridge, editor).

Although commentators have identified various reasons to regulate insider trading,¹ one rationale is to reduce the existence of information asymmetries in the securities markets. In its litigations in *Chiarella* and *Dirks*, the government attempted to use fraud-based theories of liability to address information asymmetries. The Supreme Court limited the effectiveness of this approach by requiring a predicate breach of duty for a violation of Rule 10b-5.²

The SEC responded in August 2000, by adopting Regulation Fair Disclosure.³ Regulation FD took an alternative approach to information asymmetry that was not grounded in theories of fraud but, instead, in issuer disclosure obligations.⁴ Specifically the Rule focused on corporate issuers and corporate officials as the source of such asymmetries, reasoning that if

* Perry Golkin Professor of Law, University of Pennsylvania Law School. I am grateful to Charlotte Newell, Univ. of Pennsylvania Class of 2012, for excellent research support.

¹ See, e.g., Stephen M. Bainbridge, *Insider Trading*, in 5650 ENCYCLOPEDIA OF LAW AND ECONOMICS 772 (Boudewijhn Bouckaert & Gerrit De Geest, eds. 2000), available at <http://encyclo.findlaw.com/5650book.pdf>.

² See *id.* at 773-774 (describing the Supreme Court's decisions in *Chiarella* and *Dirks* as requiring an insider's breach of a fiduciary duty as a predicate to insider trading liability).

³ SEC Regulation FD, 17 C.F.R. § 243.100 (2000).

⁴ See Proposed Rule: Selective Disclosure and Insider Trading, SEC [Release Nos. 33-7787, 34-42259, IC-24209](#) (Dec. 20, 1999), 64 Fed. Reg. 72590-01 (Dec. 28, 1999) [hereinafter *Proposing Release*]; (“The approach we propose does not treat selective disclosure as a type of fraudulent conduct or revisit the insider trading issues addressed in *Dirks*.”).

selective disclosures by corporate insiders could be prevented at the source, regulators would have less need to address trading by the recipients of that information.⁵

Although critics initially raised concerns that Regulation FD would chill information flow to the market, empirical studies suggest that changes in corporate policies did not meaningfully reduce disclosure. At the same time, the effects of Regulation FD remain unclear. After an initial series of enforcement actions, the SEC faced a stunning defeat in the Seibel Systems case and virtually ceased to use Regulation FD for several years. Private meetings and similar opportunities for selective disclosure continue to present the potential for information asymmetries, however,⁶ and the SEC has responded with by showing renewed attention to enforcement of Regulation FD. The SEC's most recent approach reflects an effort to provide ongoing guidance to issuers about its key concerns in this area.

I. The SEC's adoption of Regulation FD

The SEC has traditionally expressed concern about insider trading and the effect of that trading on the fairness and integrity of the securities markets.⁷ One focus of this concern has been selective disclosure – the practice of issuers and corporate officials, in some cases, of disclosing corporate information to select analysts, institutional investors or other market participants, prior to disclosing that information to the general public. The ability of issuers to control the manner and timing of information disclosures, in the view of the SEC, offered corporate officials the opportunity to treat information as a commodity to curry favor with particular market participants, create analyst conflicts of interest, or engage in self-dealing.

⁵ *Id.* at 72574 (“we propose to use our authority to require full and fair disclosure from issuers We believe this approach would further the full and fair public disclosure of material information, and thereby promote fair dealing in the securities of covered issuers.”)

⁶ See David Enrich & Dana Cimilluca, *Banks Woo Funds With Private Peeks*, WALL ST. J., May 16, 2011, available at <http://online.wsj.com/article/SB10001424052748703841904576256520217477678.html>

⁷ See, e.g., Cady, Roberts & Co., Release No. 34-6668, 40 SEC 907 (1961) (opinion of Chairman Cary) (explaining importance of insider trading liability in protecting the securities markets from abuses, “including specifically improper transactions by officers, directors, and principal stockholders”).

More generally, the SEC viewed selective disclosure, like other insider trading, as a threat to market integrity and investor confidence.⁸

As the SEC explained in its proposing release, it had previously addressed selective disclosure through the general antifraud provision – SEC Rule 10b-5.⁹ The SEC’s ability to treat selective disclosure as securities fraud was compromised, however, by the Supreme Court’s decisions in *Chiarella*¹⁰ and *Dirks*.¹¹ In particular, these decisions imposed a requirement, for insider trading to be fraudulent, that the trader receive the information as the result of a breach of duty.¹² This legal standard created particular difficulties of application in connection with research analysts. The SEC found that public companies were “disclosing important nonpublic information, such as advance warnings of earnings results, to securities analysts or selected institutional investors or both, before making full disclosure of the same information to the general public.”¹³ Nonetheless, the evidence in most cases of selective disclosure did not seem to support the “personal benefit” required under *Dirks*.¹⁴

Consequently, in October 2000, the SEC adopted Regulation FD.¹⁵ Regulation FD was promulgated as an “issuer disclosure rule.”¹⁶ Rather than being addressed to insider trading or fraudulent conduct, Regulation FD was, in the SEC’s words, “similar to existing Commission rules under Exchange Act Sections 13(a) and 15(d).”¹⁷ Nonetheless, the SEC explicitly

⁸ See Panel Discussion: The SEC’s Regulation FD, 6 Fordham J. Corp. & Fin. L. 273, 278 (2001) (remarks of Professor Harvey J.L. Goldschmid) (explaining that the same policy rationale applied to regulating selective disclosure as for insider trading).

⁹ 17 C.F.R. § 240.10b-5 (2011). See *Proposing Release*, *supra* note 4; Final Rule: Selective Disclosure and Insider Trading, SEC [Release Nos. 33-7881, 34-43154, IC-24599](#), 65 Fed. Reg. 51716 (Aug. 24, 2000) [hereinafter *Adopting Release*].

¹⁰ *Chiarella v. United States*, 445 U.S. 222 (1980).

¹¹ *Dirks v. SEC*, 463 U.S. 646 (1983).

¹² Cite to elsewhere in book where *Chiarella* and *Dirks* are discussed.

¹³ *Adopting Release*, *supra* note 7, at 51716.

¹⁴ See *Dirks v. SEC*, 463 U.S. at 662 (requiring a personal benefit to the tipper for tipper/tippee liability).

¹⁵ See Regulation Fair Disclosure, 17 C.F.R. § 243.100 (2000); *Adopting Release*, *supra* note 7.

¹⁶ *Adopting Release*, *supra* note 7, at 51716.

¹⁷ *Proposing Release*, *supra* note 4, at 72594.

explained that the Rule targeted conduct that had been the subject of insider trading enforcement actions prior to *Dirks* and *Chiarella*.¹⁸

The structure of Regulation FD is straightforward. Regulation FD addresses the disclosure of information rather than its subsequent use, and is expressly directed to the sources of the information: issuers and corporate officials.¹⁹ The Rule applies only to disclosures to four categories of recipients: “(1) brokers and dealers; (2) investment advisors and certain institutional investment managers; (3) investment companies and hedge funds; and (4) holders of the issuer's securities in circumstances in which it is reasonably foreseeable that the holder will purchase or sell the issuer's securities on the basis of the information.”²⁰ Thus the Rule focuses on investor and capital market disclosures rather than ordinary business communications with a firm’s customers, suppliers and the like. The rule also exempts communications to recipients who owe a duty of confidentiality to the issuer, including lawyers, accountants and, at the time of its adoption, credit-rating agencies.²¹ In conjunction with the passage of Dodd-Frank, the exemption for communications to credit rating agencies was eliminated.²²

Rather than explicitly prohibiting selective disclosure, Regulation FD takes the form of a disclosure mandate, requiring public disclosure of all material information that is disclosed by the issuer or its agents to someone within the enumerated categories of recipients. If the issuer intentionally discloses material non-public information to such a recipient, it is required to disclose that information, simultaneously, to the public. If the initial disclosure of the

¹⁸ *Id.* at 72593. Similarly, the rule was adopted in conjunction with two other rules designed to clarify the application of Rule 10b-5 to certain types of insider trading. *Id.* at 72591.

¹⁹ The rule applies to disclosures by issuers and their agents. The term “person acting on behalf of an issuer” is defined to include senior management, investor relations personnel and people who communicate regularly with market participants, but not all corporate employees. 17 C.F.R. § 243.101(c) (2011).

²⁰ SEC Regulation FD, 17 C.F.R. § 243.100(a)-(b)(1) (2011).

²¹ 17 C.F.R. § 243.101(b)(2)(i) (2011).

²² Dodd-Frank § 939B removes the CRA exemption from Regulation FD. The SEC has implemented section 939B through formal rule-making. See Removal from Regulation FD of the Exemption for Credit Rating Agencies, Securities Act Release No. 33-9146, 75 Fed. Reg. 61050, 61050 (Oct. 4, 2010) (to be codified at 17 C.F.R. pt. 243).

information is inadvertent, the issuer must publicly disclose the information “promptly,” which the rule defines to mean “as soon as reasonably practicable (but in no event after the later of 24 hours or the commencement of the next day's trading on the New York Stock Exchange).” The rule allows the issuer to make public disclose by filing a Form 8-K or through another means of disclosure that is “that is reasonably designed to provide broad, non-exclusionary distribution of the information to the public.”

Regulation FD incorporates the materiality standard of federal securities fraud. Nonetheless, the Rule does not involve a fraud-based conception of liability. In addition, Regulation FD specifically provides that its violation does not constitute a violation of SEC Rule 10b-5.²³

Many comments submitted in response to the proposed Rule reflected a concern about identifying when “material” information had been disclosed and would require corrective public disclosure. In response, the adopting release included seven categories of information that the Commission indicated were likely to be considered material.²⁴ These categories included (1) earnings information, (2) mergers and acquisitions, (3) new products or discoveries, (4) change in control or management, (5) change in auditors, (6) events regarding the issuer's securities, such as a default or stock split, and (7) bankruptcies or receiverships.²⁵

The SEC also announced, in the adopting release, its intention to retain the so-called mosaic theory in its analysis of materiality under Regulation FD.²⁶ The mosaic theory posits that information does not become material merely because it can “assume heightened significance

²³ 17 C.F.R. § 243.102 (2011).

²⁴ See *Adopting Release*, *supra* note 7, at 51721.

²⁵ *Id.*

²⁶ The mosaic theory is not a creation of the SEC, but a judicially imposed limitation on the scope of materiality for purposes of insider trading analysis. See *SEC v. Bausch & Lomb, Inc.*, 565 F.2d 8, 14 (2d Cir. 1977) (holding that “corporate management may reveal to securities analysts or other inquirers non-public information that merely fills ‘interstices in analysis,’ or tests ‘the meaning of public information.’”).

when woven by the skilled analyst into the matrix of knowledge obtained elsewhere.”²⁷ As the SEC explained, “an issuer is not prohibited from disclosing a non-material piece of information to an analyst, even if, unbeknownst to the issuer, that piece helps the analyst complete a “mosaic” of information that, taken together, is material.”²⁸

II. Initial experience under Regulation FD

Early reactions to the rule were highly critical. In particular, the business community expressed concern that Regulation FD would chill disclosure.²⁹ Commentators warned that issuer fears about potential liability would reduce or eliminate their informal communications with the market.³⁰

In the months after the SEC adopted Regulation FD, however, predictions of widespread market disruptions were not borne out.³¹ Although issuers reported changing their disclosure policies and practices in response to the Rule, the market did not experience dramatic reductions in the dissemination of information³² or substantial increases in price volatility.³³ Instead, issuers

²⁷ *Id.* at 9; see also *Elkind v. Liggett & Myers, Inc.*, 635 F.2d 156, 165-66 (2d Cir. 1980) (warning that the assessment of materiality in the context of the mosaic theory must be evaluated on a case-by-case basis).

²⁸ See *Adopting Release*, *supra* note 7, at 51722. The SEC has only explicitly recognized the mosaic theory in the context of Regulation FD, but defendants in recent insider trading cases have argued that their actions analogously constituted the mere “piecing together” of “multiple tidbits of non-public information.” See Andrew Ross Sorkin, *Just Tidbits, or Material Facts for Insider Trading?*, N.Y. TIMES, Dec. 29, 2010, available at <http://dealbook.nytimes.com/2010/11/29/just-tidbits-or-material-facts-for-insider-trading/>

²⁹ See, e.g., *Adopting Release*, *supra* note 7, at 51718; Scott Russell, *Regulation Fair Disclosure: The Death of the Efficient Capital Market Hypothesis and the Birth of Herd Behavior*, 82 B.U.L. REV. 527, 545 (2002) (summarizing concerns articulated by commentators about “inappropriate liability and the chilling effect on issuer disclosures”); Michael Schroeder, *Raytheon's Disclosure to Analysts Is Investigated*, WALL ST. J., Mar. 15, 2001, at A3 (quoting SEC Commissioner Laura Unger reporting complaints about Regulation FD and concerns about the effect on corporate communications); see also Peter Talosig III, *Regulation FD - Fairly Disruptive? An Increase in Capital Market Inefficiency*, 9 FORDHAM J. CORP. & FIN. L. 637 (2004).

³⁰ See *Adopting Release*, *supra* note 7, at 51726 (“Several [commentators] suggested, however, that the language in the Proposing Release offered insufficient protection from private lawsuits”); Peter Talosig III, *Regulation FD - Fairly Disruptive? An Increase in Capital Market Inefficiency*, 9 FORDHAM J. CORP. & FIN. L. 637 (2004).

³¹ See, Panel Discussion: *The SEC's Regulation FD*, 6 FORDHAM J. CORP. & FIN. L. 273, 291-92 (2001) (remarks of Richard Anderson, Senior Vice President, Thomson Financial/Carson Global Consulting).

³² See, e.g., Jeff D. Opdyke, *How Much Are Stocks Hurting From Recent Rash of Profit Preannouncements Tied to New Rule*, WALL ST. J., Mar. 2, 2001, at C1 (“First Call/Thompson Financial statistics show that through the end of February, 551 companies have offered up earnings guidance for the current quarter. That is nearly five times the volume of the year-earlier period.”).

adapted their disclosure practices in response to the adoption of Regulation FD. For the most part, these adaptations resulted in increased public access to issuer information. Issuers began to open their earnings conference calls to the general public and to broadcast their analyst meetings on their websites.³⁴ An early report indicated that, following adoption of the rule, issuer use of webcasts quadrupled.³⁵ Issuers began to develop best practices under Regulation FD that included, in addition to granting the general public access to information sessions that had previously been open only to invited participants, more frequent updating of their public disclosures.³⁶ These practices were enhanced by contemporaneous advances in technology that permitted greater use of the internet and corporate websites by virtually all investors.

Researchers rapidly sought to evaluate the effects of Regulation FD, and early studies reported conflicting results.³⁷ One survey by PricewaterhouseCoopers, conducted a year after Regulation FD was adopted, found that top executives were largely supportive of the rule. Nearly 90% of the executives surveyed supported the rule, 75% reported that it had not impacted their company's stock price, and roughly half of respondents reported no increase in compliance costs while those who reported an increase described it as "low to moderate."³⁸

³³ *Id.*

³⁴ See Panel Discussion: *The SEC's Regulation FD*, 6 FORDHAM J. CORP. & FIN. L. 273, 292 (2001) (remarks of Richard Anderson, Senior Vice President, Thomson Financial/Carson Global Consulting).

³⁵ See SEC, Commissioner Laura S. Unger, Special Study: Regulation Fair Disclosure Revisited (2001) available at <http://www.sec.gov/news/studies/regfdstudy.htm> [hereinafter *Unger Special Study*] ("between October 1, 2000 and April 23, 2001, the number of corporate webcasts on its service nearly quadrupled from the same period twelve months earlier (3,000 to 11,000).")

³⁶ See, e.g., Stanley Keller, SEC Regulation FD -- The Selective Disclosure Rules, ALI-ABA Course of Study Materials, Postgraduate Course in Federal Securities Law (July 2002) (describing evolving best practices for corporate compliance with Regulation FD).

³⁷ See Richard Walker, Director, Division of Enforcement, Remarks Before the Rocky Mountain Securities Conference (May 18, 2001) available at <http://www.sec.gov/news/speech/spch492.htm> (describing multiple studies reporting effects of Regulation FD on information disclosure, issuer compliance costs and stock price volatility); see also *Unger Special Study*, supra note __, (summarizing the findings of 8 surveys about Regulation FD conducted in 2001).

³⁸ See PricewaterhouseCoopers, Regulation FD Significantly Improves Disclosure, PricewaterhouseCoopers Survey Finds (Oct. 17, 2001) available at <http://www.barometersurveys.com/vwAllNewsByDocID/EC0DF4912CF1BFFD45256B8E00013366/index.html>

At the same time, market participants expressed concern that, in making their disclosures more widely available, issuers were decreasing the quality of the information that they released. An AIMR survey conducted in 2001 revealed that market professionals – analysts and portfolio managers – reported receiving less information and lower quality information from issuers.³⁹ The survey suggested that research analysts and other securities professionals were responding by conducting more independent research rather than relying primarily on issuer disclosures.⁴⁰

The first formal empirical study of the impact of the rule was conducted by academics at the business schools at University of Southern California and Purdue University.⁴¹ The study, which examined more than 2000 firms immediately after the adoption of Regulation FD, found “no evidence that Regulation FD impaired the quality and quantity of investors’ information.”⁴² The study found an increase in the informational efficiency of stock prices and “a marked increase in firms’ voluntary disclosure frequency.”⁴³

Finally, SEC Commissioner Unger released a study examining Regulation FD one year after its effective date.⁴⁴ The study summarized the testimony at an April 2001 SEC Roundtable and identified various issues of concern, including a need for further guidance on materiality, the incorporation of technological developments to facilitate public disclosure and the effect of the rule on the quality of disclosure, particularly with respect to forward-looking information. The study’s primary recommendation called for the SEC to continue to evaluate corporate disclosure post-FD to determine if modifications to the Regulation were necessary.

III. Early enforcement actions

³⁹ See The CPA Journal, *Research studies show differing views on Regulation FD* (Dec. 2001), available at <http://www.nysscpa.org/cpajournal/2001/1200/nv/nv2.htm>.

⁴⁰ *Id.*

⁴¹ Frank Heflin, K. R. Subramanyam & Yuan Zhang, *Regulation FD and the Financial Information Environment: Early Evidence*, 78 ACCT’G REV. 1 (2003).

⁴² *Id.* at 4.

⁴³ *Id.*

⁴⁴ See *Unger Special Study*, supra note __.

In conjunction with its adoption of Regulation FD, the SEC announced that it would attempt to enforce the rule in a way that minimized its chilling effect on issuer communications with the market.⁴⁵ Nonetheless, the Commission rapidly brought a number of enforcement actions.⁴⁶ From 2002 to 2005, the SEC brought seven enforcement actions against issuers and corporate officials and published one report of investigation.⁴⁷ Most of these actions concerned private communications about corporate earnings⁴⁸ and all but one, *Siebel Systems*, were settled and not contested.

The actions rapidly demonstrated the scope of the SEC's commitment to the new rule and its intention, through its selection of cases, to provide broader guidance to issuers and the market about the scope of communications that it viewed as problematic. The SEC's cases, in particular, revealed the Commission's intention not to limit its application of the rule to cases involving literal factual inconsistencies between private communications and public disclosures.⁴⁹ Instead, the SEC's actions targeted more subtle methods – winks and nods -- for providing selected recipients with informational advantages. These methods included, for example, a corporate official's reaffirmation of earnings estimates that had previously been

⁴⁵ See, e.g., Letter from then-SEC Chairman designee Harvey L. Pitt to the Chief Clerk, United States Senate, Committee on Banking, Housing & Urban Affairs, July 23, 2001 ("The Commission's Enforcement Staff has stated that it will not attempt to second-guess reasonable, good faith judgments by persons who honestly attempt to comply with Regulation FD. I agree with that approach."); Speech of then-Enforcement Director Richard H. Walker, "Regulation FD: An Enforcement Perspective," before the Compliance and Legal Division of the Securities Industry Association, New York, Nov. 1, 2000 (stating that, at least in the early stages, the Enforcement Division will focus its efforts on "egregious violations" and that the division is "not looking to frustrate the purpose of the rule – which is to promote broader and fairer disclosure of information to investors – by second-guessing reasonable disclosure decisions made in good faith, even if we don't agree with them..").

⁴⁶ See SEC Brings First Regulation FD Enforcement Actions, No. 2002-169, (Nov. 25, 2002) available at <http://www.sec.gov/news/press/2002-169.htm> (announcing the first four enforcement actions brought under Regulation FD).

⁴⁷ See Marc H. Folladori, *Interlude for Regulation FD*, Practising Law Institute Course Handbook, October 2008.

⁴⁸ The SEC had previously stated, in its adopting release, that a corporate official that provides earnings guidance during private meetings with analysts "takes on a high degree of risk under Regulation FD." Adopting Release, supra note 7, at 51,721.

⁴⁹ See William S. Lamb et al., *SEC Continues to Define Regulation FD Parameters Through Enforcement Actions: Reaffirmation of Guidance Can Constitute Violation*, 24 No. 5 BANKING & FIN. SERV. POL'Y REP. 3, 4 (2005).

publicly released (*Flowserve*)⁵⁰, reviewing and correcting drafts of analyst reports (*Senetek*)⁵¹, disclosure made through a combination of statements and a corporate official's conduct, tone and demeanor (*Schering-Plough*),⁵² and the use of code words in public statements that were subsequently clarified through private conversations (*Motorola*)⁵³. The SEC's choice of enforcement actions reflected its view that officials could violate Regulation FD not just by what they said, but by how they said it.⁵⁴

IV. *Siebel Systems*

The SEC faced a critical juncture in its enforcement of Regulation FD with the federal court litigation in the *Siebel Systems* case. Siebel was actually a repeat offender. In November 2001, Siebel's CEO made optimistic statements at a private technology conference that, according to the SEC, differed materially from the statements made by the CEO on a public conference call. Following the optimistic private statements, Siebel's trading volume doubled and its stock price increased by 16.5%. The SEC brought an enforcement action (*Siebel I*) that Siebel settled by agreeing to a cease and desist order and paying a \$250,000 penalty.

Only six months after the cease and desist order was entered, in April 2003, Siebel engaged in conduct that the SEC viewed as similar to its prior Regulation FD violation.⁵⁵ Siebel communicated a negative outlook for the company in early April 2003 through a series of public

⁵⁰ See Order Instituting Cease-and-Desist Proceedings, In the Matter of Flowserve Corp., Release No. 51427, Admin. Proceeding File No. 3-11872, at 3 (Mar. 24, 2005).

⁵¹ See Order Instituting Cease-and-Desist Proceedings, In the Matter of Senetek P.L.C., Release No. 50400, Admin. Proceeding File No. 3-11668, at 2 (Sept. 16, 2004).

⁵² See Order Instituting Cease-and-Desist Proceedings, In the Matter of Schering-Plough Corp., Exchange Act Release No. 48,461, Admin. Proceeding File No. 3-11,249, at 3-7 (Sept. 9, 2003); SEC Files Settled Regulation FD Charged Against Schering-Plough Corp. and its Former Chief Executive, Litigation Release No. 18,330, Case No. 1:03CV01880 (D.D.C.) (CKK) (Sept. 9, 2003); Jon Jordan, *Corporate Issuers Beware: Scherling-Plough and Recent SEC Enforcement Actions Signal Vigorous Enforcement of Regulation FD*, 58 U. MIAMI L. REV. 751 (2004).

⁵³ Motorola, Inc., Exchange Act Release No. 46,898, 2002 WL 31650174 (Nov. 25, 2002).

⁵⁴ See Pepper Hamilton, *Regulation FD Compliance after Schering-Plough – You're your Mannerisms*, (Nov. 10, 2003) available at http://www.pepperlaw.com/publications_article.aspx?ArticleKey=250 (“the SEC also chose this set of facts to reinforce its views about the role non-verbal cues and signals can play in a Regulation FD violation”).

⁵⁵ Complaint, at ¶ 4, SEC v. Siebel Systems, Inc., 384 F. Supp. 2d (No. 04 CV 5130) (2004), available at <http://www.sec.gov/litigation/complaints/comp18766.pdf>.

disclosures. Following those communications, on April 30, 2003, Siebel's CFO and IR Director met privately with several institutional investors. At the private meetings, which were organized by Morgan Stanley, Siebel's CFO, Kenneth Goldman, characterized Siebel's business activity levels as "good" and "better" and disclosed that new deals were coming into the company's pipeline. According to the SEC's complaint, which carefully parsed these statements against the company's prior disclosures, these descriptions of Siebel's business were inconsistent with and affirmatively more positive than the prior public statements.⁵⁶

Morgan Stanley subsequently communicated Goldman's remarks from the meetings to its other institutional clients. Morgan Stanley personnel characterized the tenor of the communications as "the body language was positive."⁵⁷ The SEC's Complaint documented that the investors that attended the meetings and other institutional investors responded by purchasing Siebel stock.⁵⁸ The day after the meetings, Siebel's stock price increased by 8%, and its trading volume doubled.⁵⁹

When the SEC brought a second enforcement action against Siebel and its officials, the defendants filed a motion to dismiss the complaint. Although the defendants raised a variety of arguments, the court did not reach most of them because it concluded that the defendants' private statements did not differ materially from information that had been publicly released.⁶⁰ As a result, the court held that the SEC's complaint failed to state a claim.⁶¹

⁵⁶ *Id.* at ¶ 49 ("These statements materially contrasted with the public statements that Thomas Siebel had made during the April 4 and 23 conference calls and at the Deutsche Bank conference on April 28. For example, in contrast to the apocalyptic economic environment that Thomas Siebel described at the Deutsche Bank conference, Goldman's disclosures at the April 30 Alliance meeting and Morgan Stanley dinner were significantly more positive and upbeat."); see also SEC's opposition to Siebel's motion to dismiss at 8 (stating that Siebel's private statements "materially contrasted with the Company's prior public statements").

⁵⁷ *Id.* at ¶ 52.

⁵⁸ *Id.* at ¶ 53.

⁵⁹ *Id.* at ¶ 54.

⁶⁰ SEC v. Siebel Systems, Inc., 384 F.Supp.2d 694, 709 (S.D.N.Y. 2005)

⁶¹ *Id.* at 710.

In arguing that Goldman's private statements were material, the SEC emphasized the reaction by investors to those statements. As the SEC stated, "[t]he materiality of the information is confirmed by the actions of those who attended the private meetings."⁶² Thus Siebel presented the issue of the extent to which stock price movements and investor trading reactions to the information could be used to establish materiality as opposed to a comparison of the precise wording used by corporate officials in different contexts. The issue was important because of the potential for corporate officials to convey information indirectly -- through winks, nods and body language.⁶³

With respect to this important aspect of Regulation FD, the court's decision dealt the SEC a substantial blow. Although the court stated that stock movement and investor reactions to information could be considered relevant factors in determining the materiality of Siebel's statements, the court stated that they were not sufficient.⁶⁴ Instead, the court engaged in a precise comparison of Siebel's public and private statements and concluded that the SEC had been too demanding, requiring in essence that companies examine their statements with the precision of a "lexicologist."⁶⁵ Because the court concluded that Siebel's private statements were "equivalent in substance to the information publicly disclosed [by the company]," it found no violation.⁶⁶

More problematic was the freedom created by the *Siebel* opinion for corporate officials to engage in subjective characterizations that were not disclosed to the public even if investors

⁶² Plaintiff's Brief in Opposition to Motion to Dismiss, at 2, SEC v. Siebel Systems, Inc., 384 F. Supp. 2d (2005) (No. 04 CV 5130), 2004 WL 3142263.

⁶³ See *Adopting Release*, *supra* note 7 at 51721 (noting that corporate officials can violate Regulation FD "whether the information about earnings is communicated expressly or through indirect 'guidance,' the meaning of which is apparent though implied.").

⁶⁴ See SEC v. Siebel Systems, Inc., 384 F.Supp.2d 694, 707 (S.D.N.Y. 2005) (noting that "although stock movement is a relevant factor to be considered in making the determination as to materiality, it is not, however, a sufficient factor alone to establish materiality.")

⁶⁵ *Id.* at 705.

⁶⁶ *Id.*

viewed those characterizations as altering the total mix of information available to the market.⁶⁷ The court stated that “[t]he regulation does not prohibit persons speaking on behalf of an issuer, from providing mere positive or negative characterizations, or their optimistic or pessimistic subjective general impressions, based upon or drawn from the material information available to the public.”⁶⁸ This analysis seemed directly in tension with the Supreme Court’s guidance in *Virginia Bankshares*, that expressions by corporate officials of their reasons, opinions or beliefs were likely to be particularly important to investors in light of the “knowledge and expertness” of those officials.⁶⁹

V. After *Siebel Systems*

The SEC’s immediate response to *Siebel Systems* was to cease bringing enforcement actions based on Regulation FD. Following the decision, the SEC did not bring another Regulation FD enforcement action for more than four years.⁷⁰ This reluctance can be seen as a reaction not just to the loss, but to the nature of the *Siebel* court’s opinion which commentators described a “public scolding.”⁷¹

⁶⁷ As one commentator characterized the decision, “The fact that nonpublic subjective general impressions may cause movement in stock price or trading volume does not, in and of itself, create a presumption that material information was disclosed and Regulation FD was violated.” Robert F. Carangelo & Jaclyn G. Braunstein, Weil Gotshal, *Siebel Systems: A Speed Bump for the SEC on the Road to Regulation FD Enforcement?*, at 11 (Dec. 2005) available at <http://www.weil.com/news/pubdetail.aspx?pub=8086>.

⁶⁸ *Siebel Systems*, 384 F.Supp.2d at 707.

⁶⁹ *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 1090-91 (1991).

⁷⁰ See Kit Addleman & Tracy G. Smith, Haynes and Boone LLP, *SEC’s Regulation FD Enforcement Actions Bring Compliance Lessons to Light*, Bloomberg Law Reports: Federal Securities Law. The SEC did bring a cease and desist action, in 2007, against Electronic Data Systems (EDS); Order Instituting Cease-and-Desist Proceedings, In the Matter of Electronic Data Systems Corp., Release No. 56519, Admin. Proceeding File No. 3-12825 (Sept. 25, 2007), available at www.sec.gov/litigation/admin/2007/34-56519.pdf. The EDS case was brought as an administrative proceeding, however, rather than an enforcement action thereby avoiding the risk for the SEC of litigating in federal court if the defendants did not agree to settle the charges. See Gibson Dunn, 2011 Mid-Year Securities Enforcement Update, at 11, (July 18, 2011), available at <http://www.gibsondunn.com/publications/pages/2011Mid-YearSecuritiesEnforcementUpdate.aspx> (explaining, in the context of insider trading charges filed against Rajat Gupta, why “An administrative proceeding is generally viewed as a more favorable venue for the Enforcement Division”).

⁷¹ Kristen A. Truver, Note, *Cutting the Party Line: How the SEC Can Silence Persisting Phone Call Tips*, 39 HOFSTRA L. REV. 447, 470 (2010).

Following this hiatus, the SEC resumed its efforts to use Regulation FD, but cautiously.⁷² Although the SEC has not formally retreated from its concern about implicit disclosures, it resumed its enforcement efforts with a case involving private statements that were explicitly inconsistent with the issuer's public disclosures. In addition, the SEC issued several compliance and disclosure interpretations to provide guidance concerning the SEC's policies. The releases focused, in particular, on the extent to which informal communications with analysts create potential problems under Regulation FD.⁷³

In 2009, the SEC filed its first Regulation FD enforcement action since the *Siebel Systems* decision against Christopher Black, the former CFO of American Commercial Airlines (ACL). According to the SEC's litigation release, Black sent private e-mails to eight sell-side analysts from his home, on a weekend, disclosing that earnings would be lower than the guidance that had been disclosed by the company just days before. In contrast to the *Siebel* case, Black's comments were both written and clearly inconsistent with the company's public statements.

Notably as well, the SEC did not bring an enforcement action against ACL. According to the SEC, ACL had maintained compliance systems reasonably designed to educate corporate

⁷² See *id.* at 470 (describing SEC as "hesitant and conservative in pleading Regulation FD in actions through 2009"). Commentators have also suggested that, in some cases, the SEC failed to bring allegations of an FD violation, even when supported by the facts, in favor of relying on other provisions of the federal securities laws. See *id.* at 471 (offering, as an example of the SEC's reluctance to use Regulation FD, 2010 enforcement action against State Street); *id.* at 481 (describing cases in which, according to the author, the SEC should have used Regulation FD, but did not).

⁷³ See SEC Compliance and Disclosure Interpretations: Regulation FD, June 4, 2010, available at <http://www.sec.gov/divisions/corpfin/guidance/regfd-interp.htm> In particular, the SEC noted that issuer confirmation of prior forecasts may trigger an FD reporting obligation depending on the amount of time that had passed since the prior forecast and the extent to which intervening events had occurred. The SEC also noted that issuers may comment on analyst models, including correcting historical facts and sharing inconsequential data, without triggering obligations under Regulation FD.

employees and to prevent Regulation FD violations.⁷⁴ In contrast to Siebel, ACL filed an 8-K on the first trading day after it learned of Black's disclosures. ACL also self-reported the violation to the SEC and cooperated with the SEC's investigation. In addition, ACL took remedial measures to prevent future violations. The SEC's decision can be understood as a message to corporate issuers as to the value of adopting compliance procedures, cooperating with any SEC investigation and remedying any potential selective disclosures promptly.

In March, 2010, the SEC brought an enforcement action against Presstek, Inc. and its former CEO, Edward Marino.⁷⁵ Marino, according to the SEC, selectively disclosed negative financial information to a registered investment adviser two days before the end of the quarter and one day before Presstek publicly announced that its earnings would be below prior estimates. Like the *Black* case, *Presstek* involved what might be considered an egregious or a clearly material selective disclosure – tipping investors or analysts right before the public disclosure of an earnings surprise is precisely the type of disclosure to which Regulation FD was addressed. Unlike the *Black* case, the SEC did sanction Presstek despite the existence at the company of FD disclosure policies. Although the SEC's rationale for proceeding against the issuer was not clear, it may have been concerned about sending a message that the mere existence of a compliance program would not insulate an issuer from liability.⁷⁶

Office Depot was the third Regulation FD enforcement action within a period of slightly more than a year.⁷⁷ *Office Depot* reflected a somewhat more aggressive enforcement decision by

⁷⁴ See Litigation Release, SEC v. Christopher A. Black, Lit. Rel. No. 21222 (Sept. 24, 2009, available at <http://www.sec.gov/litigation/litreleases/2009/lr21222.htm>). The SEC stated that ACL "cultivated an environment of compliance."

⁷⁵ See Litigation Release, SEC v. Presstek, Inc., Lit. Release 21443 (Mar. 9, 2010), available at <http://www.sec.gov/litigation/litreleases/2010/lr21443.htm>.

⁷⁶ See, e.g., Kimberley D. Krawiec, *Cosmetic Compliance and the Failure of Negotiated Governance*, 81 WASH. U. L.Q. 487 (2001) (warning of the potential for ineffective compliance programs).

⁷⁷ See Order Instituting Cease-and-Desist Proceedings, In the Matter of Office Depot, Inc., Release No. 63152, Admin. Proceeding File No. 3-14094 (Oct. 21, 2010).

the SEC. Faced with the concern that the company would not meet analysts' earnings estimates, Office Depot's CEO and CFO coordinated a strategy for privately contacting 18 analysts in order to lower the analysts' expectations. The strategy included the preparation of talking points that referenced comparable companies' lower than expected performance and weakening economic conditions.⁷⁸ Six days later, the company publicly announced that earnings would be "negatively impacted due to continued soft economic conditions."

Notably, *Office Depot* involved issuer signaling rather than issuer statements that directly contradicted public disclosures. The specific statements contained in Office Depot's talking points and communicated privately to the analysts were reminders about negative information contained in the company's prior public statements or references to other issuers whose earnings were negatively affected by economic downturn. Accordingly, although the company engaged in a deliberate campaign to persuade analysts to lower their earnings estimates through private communications, it is unclear how a court would have analyzed the SEC's claims under *Siebel*.⁷⁹ The case is also notable in that the SEC brought its enforcement action against the CEO and CFO although the selective disclosures were made by their subordinates.⁸⁰

One of the SEC's most recent enforcement actions involved an unusual fact pattern.⁸¹ In *First Third Bancorp*, the defendant decided to redeem certain trust preferred securities on the

⁷⁸ *Id.* at 3-4.

⁷⁹ Both executives settled with the SEC and agreed to pay civil penalties of \$50,000. Office Depot agreed to pay a \$1 million penalty. In imposing the latter penalty, the SEC observed that Office Depot had no formal written Regulation FD policies or procedures and had conducted no formal employee training on Regulation FD. The statement implied that the existence of such policies might have reduced the size of the penalty.

⁸⁰ Of course the CEO and CFO were the ones who developed the plan and created the talking points communicated by their subordinates.

⁸¹ The SEC's enforcement action in *China Voice* also differs markedly from prior cases. *China Voice* involved a Ponzi scheme, and the SEC's complaint alleged a massive fraud in which the defendants raised money through false statements and used the proceeds to repay prior investors. The FD claims involved allegations that corporate officials selectively disclosed non-public information to a *China Voice* shareholder who was himself a participant in the fraud. The complaint does not reveal the SEC's rationale for including Regulation FD among the claims, and the implications of the case with respect to future enforcement actions are unclear. *See* Complaint, *SEC v. David Ronald Allen*, No. 11CV00882, 2011 WL 1599661 (N.D. Tex.), Apr. 28, 2011.

basis that a provision of Dodd-Frank had created a “capital treatment event.” First Third instructed the trustee to redeem the securities and to provide “all appropriate” notices of redemption. In accordance with the governing trust documents, the trustee provided such a notice to the Depository Trust Company, the only registered holder of record. DTC then posted the notice of redemption on its website which was password protected and available only to subscribers. When First Third became aware of unusual trading volume in the securities, it filed an 8-K. The SEC’s settlement with First Third included only a cease and desist order and no civil penalty, and noted the defendant’s cooperation and remedial actions once it became aware of the significance of the selective disclosure. It is likely that the SEC’s decision to bring the action was motivated, in part, by a desire to call attention to the potential for selective disclosures even when information is disclosed over the internet or through a website. These concerns are considered in more detail in the SEC’s release on internet disclosures discussed below.

As this book goes to press, the SEC’s most recent Regulation FD investigation appears to involve Avon. In October 2011, Avon disclosed in its quarterly report that it had received an SEC subpoena relating to an investigation of possible violations of Regulation FD.⁸² Media reports state that the focus of the investigation is a private meeting between Avon’s CFO and a Citigroup research analyst.⁸³ The analyst’s report referred to information supplied by the CFO at that meeting. The Avon investigation reflects the SEC’s ongoing suspicion over private meetings between corporate officials and analysts or investors. Although the facts of the case remain unclear, the information available should suggest to issuers that such meetings are likely to trigger scrutiny. This message is reinforced by remarks made by SEC Official David

⁸² See *Avon Faces SEC Probe of Analyst Contact, China*, REUTERS, Oct. 27, 2011, available at http://www.cnbc.com/id/45060519/Avon_Faces_SEC_Probe_of_Analyst_Contact_China.

⁸³ See *Avon’s Cramb gave Citi Bribery Probe Info*, REUTERS, Nov. 2, 2011, available at <http://www.reuters.com/article/2011/11/02/avon-idUSN1E7A021U20111102>.

Rosenfeld, at a conference in February.⁸⁴ According to media reports, Rosenfeld expressed concern as to whether issuers can participate in the common practice of private meetings and calls consistent with their obligations under Regulation FD.

Despite regulatory concerns, private meetings continue to be a mainstay of Wall Street practice.⁸⁵ Brokerage firms compete for valued commission revenues through their ability to arrange private meetings for their institutional investor clients.⁸⁶ Banks and brokers deny that such meetings are being used to convey material non-public information and claim that they serve legitimate business purposes, and tout their ability to provide “access” as a means of differentiating themselves from their competitors.⁸⁷

VI. The effects of Regulation FD

When Regulation FD was first adopted, commentators widely agreed that it was difficult to predict its long term effects. Scholars have drawn upon the prior ten years of experience with the Rule to produce an extensive body of empirical research. The mixed results of this research make it difficult, however, to draw definitive conclusions about the effects of the regulation.

There is substantial evidence that Regulation FD reduced selective disclosure and information asymmetries.⁸⁸ A study by Bei Dong and others, for example, focuses on leakage of earnings information. The study concludes that, after the Rule’s adoption, information leakages were reduced prior to earnings disclosures and that price volatility increased after the adoption,

⁸⁴ See Charlie Gasparino, *Regulators May Expand Definition of Insider Trading*, FOX BUSINESS, Feb. 15, 2012, available at <http://www.foxbusiness.com/industries/2012/02/15/regulators-may-expand-definition-insider-trading/>.

⁸⁵ See Enrich & Cimilluca, *supra* note __ (describing “longstanding” practice by investment banks of arranging private issuer meetings for their hedge fund clients).

⁸⁶ See Dominic Jones, *Despite Reg FD, study finds traders profit from private CEO meetings*, IR WEB REPORT, Aug. 23, 2011, available at <http://irwebreport.com/20110823/selective-access-profitable-study/> (stating that US investors allocate \$1.4 billion in trading revenues in exchange for private access).

⁸⁷ See David Enrich & Dana Cimilluca, *supra* note __.

⁸⁸ See, e.g., William J. Kross & Inho Suk, *Does Regulation FD work? Evidence from analysts' reliance on public disclosure*, 53 J. of Acct. & Econ. 225 (Feb.-Apr., 2012) (concluding that Regulation FD “levels the playing field between analysts and individual investors”).

suggesting that the public disclosures revealed information not previously available to traders.⁸⁹ Importantly, the study also suggests that the reduction of these asymmetries is beneficial to the market. It finds that Regulation FD reduced bid-ask spreads, reflecting reduced concern by market participants over the potential information advantages possessed by their trading counterparties. Sinha and Gadarowsky report similar results, finding that information leakage around voluntary management disclosures was reduced after Regulation FD.⁹⁰ Another study reports that the ability of analysts to exploit social ties to gain informational advantages virtually disappeared in the post-FD era.⁹¹

Critics had predicted that Regulation FD would reduce information flow as issuers, unwilling to disclose publicly, would reduce the overall amount of their disclosure. The studies of this issue are mixed.⁹² At least some studies have found reduced overall disclosure, especially by smaller firms.⁹³ Scholars also report that Regulation FD delays the disclosure of information, at least in some cases.⁹⁴ On the other hand, studies have found increased reliance by analysts on

⁸⁹ See Bei Dong, Edward Xuejun Li, K. Ramesh & Min Shen, *The Effects of Regulation FD on Informal and Institutionalized Leakages of Information in Earnings Press Releases* (unpublished manuscript) (on file with the Darden School of Business, University of Virginia) (Oct. 7, 2011) *available at* <http://www.darden.virginia.edu/web/uploadedFiles/Paper%20for%20K%20Ramesh%20-%20DLRS%20December%202011.pdf>.

⁹⁰ See Praveen Sinha & Christopher Gadarowski, *The Efficacy of Regulation FD*, 45 FIN. REV. 331 (May 2010). Another study finds that FD reduced analysts' ability to predict earnings surprises. Dan Palmon & Ari Yezegel, *Analysts' Recommendation Revisions and Subsequent Earnings Surprises: Pre-and-Post Regulation FD*, 26 J. ACCT. AUDITING & FIN. No. 3 (2011).

⁹¹ See Andrea Frazzini, Christopher J. Malloy & Lauren Cohen, *Sell Side School Ties* (Harvard Bus. Sch. Fin., Working Paper No. 08-074, Feb. 20, 2008).

⁹² See Brian J. Bushee, Michael J. Jung & Gregory S. Miller, *Do Investors Benefit from Selective Access to Management?* (unpublished manuscript) (on file with the Wharton School of Business) *available at* http://accounting.wharton.upenn.edu/documents/research/BJM2_201112.pdf (finding that Regulation FD did not substantially reduce information disclosures by firms in conference calls); see also Sinha & Gadarowsky, *supra* note ___ (describing mixed results of studies of disclosure quality and quantity post Regulation FD).

⁹³ See Edward R. Lawrence, Gordon Karels, Arun Prakash & Siddharth Shankar, *Effect of regulation FD on disclosures of information by firms*, 21 APPLIED FIN. ECON. 979 (2011).

⁹⁴ See Paul A. Griffin, David H. Lont & Benjamin Segal, *Enforcement and disclosure under regulation fair disclosure: an empirical analysis*, 51 ACCT. & FIN. 947 (2011).

public disclosures, and an increasing use by issuers of earnings guidance as a substitute for selective disclosures.⁹⁵

Some of the Regulation FD studies indicate that Regulation FD reduced information quality.⁹⁶ Lawrence, et al., for example, find that firms release less negative information subsequent to the adoption of Regulation FD.⁹⁷ Agrawal et al. find a reduction in analysts' forecast accuracy.⁹⁸ Another study finds that institutional investors are less able to identify mis-priced public offerings post-Regulation FD.⁹⁹

Perhaps most troublingly, there is evidence that information asymmetries persist after the adoption of Regulation FD and that selective access to management continues to provide investors with trading advantages.¹⁰⁰ For example, one recent study finds that investor trade sizes increase after investors obtain private meetings with corporate officials – and that those sizes further increase if the official involved is the CEO.¹⁰¹ To the extent that, as the SEC argued in Siebel, trading behavior is evidence that the investor has received material information, this data raises the concern that such information continues to be communicated selectively. Moreover, this research supports the SEC's continued focus on private meetings as potential sources for the communication of non-public information.

VII. Technological developments and Regulation FD

⁹⁵ See Anchada Charoenrook & Craig M. Lewis, *Information, Selective Disclosure, and Analyst Behavior*, (Fin. Mkts. Rsch. Center, Working Paper, #04-14 Sept. 2007); see also *id.* at n.3 (describing studies finding increased issuer disclosures of earnings guidance).

⁹⁶ *Id.*

⁹⁷ See Lawrence, et al., *supra* note ____.

⁹⁸ See Anup Agrawal, Sahiba Chadha & Mark Chen, 2006, "Who is afraid of Reg FD? The Behavior and Performance of Sell-Side Analysts Following the SEC's Fair Disclosure Rules," 79 J. BUS. 2811 (Nov. 2006).

⁹⁹ See Douglas O. Cook & Tian Tang, *The Impact of Regulation FD on Institutional Investor Informativeness*, 39 FIN. MGMT. 1273 (2010).

¹⁰⁰ See also David Solomon & Eugene Soltes, *What are we Meeting for? The Consequences of Private Meetings with Investors*, Nov. 2011, available at <http://www-bcf.usc.edu/~dhsolomo/meet.pdf> (describing the use of private meetings by different types of investors and the effect of these meetings on trading).

¹⁰¹ See Bushee, et al., *supra* note ____.

Corporate disclosure practices have been adapted to reflect the selective disclosure concerns reflected in Regulation FD. The world of information and disclosure continues to evolve, however. Some of the most challenging changes that have occurred and are yet to come concern the effect of technological developments on an issuer's ability to make public disclosures.

A. Issuer websites

The SEC adopted Regulation FD, in the middle of a technology revolution. In the years following the Rule's adoption, the SEC noted dramatic increases in investor access to the internet.¹⁰² The SEC also noted that issuers were increasingly likely both to maintain a corporate website and to include links on that website to their SEC filings and other investor-oriented information. The internet offered the potential for issuers to provide broad-based dissemination of information quickly and inexpensively, and some commentators criticized the SEC for failing to incorporate internet-based disclosure into its requirements under Regulation FD.¹⁰³

In 2008, the SEC responded. The Commission issued an interpretive release concerning company web sites that included, in particular, guidance concerning the circumstances under which a website posting could satisfy the public dissemination requirement under Regulation FD.¹⁰⁴ The very recognition that a website posting could be sufficient to comply with the rule reflected a change from the position adopted by the SEC in 2000. The release went on to

¹⁰² Compare Robert A. Prentice, *The Internet and Its Challenges for the Future of Insider Trading Regulation*, 12 HARV. J.L. & T. 263, 286 (1999) (stating in 1999 that a strong argument can be made that "information available only on a corporate website is not 'public.'") with Commission Guidance on the Use of Company Websites, Release Nos. 34-58288, IC-28351, 17 C.F.R. 241, 271 (2008), available at <http://www.sec.gov/rules/interp/2008/34-58288.pdf> (describing growing investor access to the internet).

¹⁰³ See Thomas Ishmael, *Securities and Exchange Commission Regulation Fair Disclosure – A Modern Law with Outmoded Methods: An Appeal for Dissemination of Material Information on Corporate Websites*, 33 OKLA. CITY U.L. REV. 629 (2009).

¹⁰⁴ See Commission Guidance on the Use of Company Websites, Release Nos. 34-58288, IC-28351, 17 C.F.R. 241, 271 (2008), available at <http://www.sec.gov/rules/interp/2008/34-58288.pdf>; see also Lawrence J. Trautman, *The SEC & The Internet: Regulating the Web of Deceit*, 65 CONSUMER FIN. L. Q. REP. (2011) (discussing SEC's release and guidance).

provide guidance concerning the evaluation of whether a website posting constituted the necessary public disclosure required by the Rule. According to the SEC, the primary considerations in determining whether posting information on a company website constituted public disclosure for purposes of Regulation FD were 1) whether the company web site was “a recognized channel of distribution;” 2) whether the website posting made the information available to the general marketplace and 3) whether there was a reasonable waiting period for investors and the market to react to the posted information.¹⁰⁵

The SEC explicitly provided, in contrast to its earlier position, that “for some companies in certain circumstances, posting of the information on the company’s web site, in and of itself, may be a sufficient method of public disclosure under Rule 101(e) of Regulation FD.”¹⁰⁶ The SEC noted that the analysis was issuer-specific and would depend on an evaluation of the particular circumstances. The SEC further noted that the manner and accessibility of information on an issuer’s website were critical factors in evaluating whether a website posting constituted a public disclosure. It is likely that the SEC’s decision to bring an enforcement action in the First Third case was motivated, in part, by a desire to demonstrate to issuers the potential for selective disclosure in cases in which access to a website posting is limited.

B. Social media

Social media presents still another challenge. Corporate executives increasingly discuss their companies using social media tools such as Facebook and Twitter. These methods of disclosure raise challenges over the traditional regulatory categories in that the communications are not typically made to a favored few as in the case of private analyst meetings. Neither,

¹⁰⁵ *Id.* The Release provided a list of factors to guide issuers in evaluating these considerations. The SEC also explained that the considerations were designed to determine whether website postings were “reasonably designed to provide broad, non-exclusionary distribution of the information to the public.” *Id.* at 24.

¹⁰⁶ *Id.* at 25.

however, are they open to the general public in the same way as a press release or Form 8-K would be. Informal and unstructured social media communications also stretch the concept of materiality.

One corporate executive has taken the use of social media communications to a new level. WebMediaBrands CEO Alan Meckler has made a practice of communicating corporate information to investors on a real time basis, using Twitter and his blog.¹⁰⁷ In December 2010, the SEC staff sent WebMediaBrands a comment letter questioning the company about Meckler's social media postings of company information.¹⁰⁸ The company defended Meckler's practices on the grounds that the particular tweet and blogged information at issue did not involve material, nonpublic information. The company also argued that Meckler's tweets and blog posts were equivalent to public distribution and, therefore, were Regulation FD compliant as a "recognized channel" of public distribution, at least for this company and this CEO.¹⁰⁹ To date, Meckler has not stopped his use of social media, and the SEC has not brought an enforcement action against him.¹¹⁰

Although, to date, SEC investigations involving social media postings appear to be uncommon, and it is unclear how the SEC viewed WebMediaBrands' argument that the postings were public rather than selective disclosure. Nonetheless, issuers are beginning to consider such postings in their Regulation FD compliance and education programs. IBM, for example,

¹⁰⁷ See Dominic Jones, *CEO pushes Reg FD limits on Twitter*, IR WEB REPORT, Sept. 15, 2011, available at <http://irwebreport.com/20110915/ceo-pushes-reg-fd-limits-on-twitter/>.

¹⁰⁸ See Letter from H. Christopher Owings, Asst. Dir. SEC, to Alan M. Meckler, Chairman & CEO, WebMediaBrands Inc. Dec. 9, 2010, at 1 available at <http://www.sec.gov/Archives/edgar/data/1083712/000000000010074073/filename1.pdf> (asking issuer to explain whether CEO's blog postings providing updates "on future acquisitions, stock option purchases and new services... conveyed information in compliance with Regulation FD and other Commission rules and regulations.")

¹⁰⁹ See Letter from Donald R. Reynolds, attorney for WebMediaBrands Inc. to the SEC, at 4 (Jan. 7, 2011) available at <http://www.sec.gov/Archives/edgar/data/1083712/000101968711000062/filename1.htm>.

¹¹⁰ See Reese Darragh, *CEO's Tweets Raise Reg FD Questions*, COMPLIANCE WEEK, Nov. 08, 2011, available at <http://www.complianceweek.com/>.

provides guidelines on social computing to its employees.¹¹¹ Among these guidelines, IBM warns its employees not to blog or twitter about confidential company information, including the company's future performance and business plans. It is likely that attention to the implications of Regulation FD for social media will rapidly become a component of best practices for issuer compliance.

VIII. Conclusion

Despite the apparent setback of the *Siebel Systems* decision, the SEC's efforts to address selective disclosure through the promulgation and enforcement of Regulation FD should be understood as successful. Issuers take seriously the applicable regulatory restrictions in engaging in private communications with investors and analysts and have structured compliance and education systems designed to reduce both intentional and unintentional selective disclosures. Although the SEC has brought a limited number of cases enforcing the rule, its selections appear designed less to punish wrongdoers than to announce generally applicable standards of conduct and to expose areas of ongoing regulatory concern.

Several areas are likely to continue to raise SEC concerns. Private meetings are a problematic area. The Commission appears likely to remain suspicious of the claim that private meetings between corporate executives and analysts and investors do not involve selective disclosures. The SEC's concerns are supported by recent empirical studies suggesting that private meetings confer trading benefits on their attendees. Nonetheless, the disclosure-based structure of Regulation FD appears better suited to balancing competing policy considerations in this area than the blunt force of antifraud liability. Similarly, the SEC will need to continue to refine its enforcement of Regulation FD to incorporate technological developments, including growing information transmission through the internet and social media. Responding to these

¹¹¹ *IBM Social Computing Guidelines*, <http://www.ibm.com/blogs/zz/en/guidelines.html> (last visited Mar. 20, 2012).

developments requires a delicate balance in that technology offers the potential to level the informational playing field at the same time that it presents new mechanisms for abuse.