April 3, 2013

SEC Clarifies Position on Corporate Communications through Social Media

On April 2, 2013, the SEC issued a Report of Investigation (the Report) pursuant to Section 21(a) of the Securities Exchange Act of 1934 (the Exchange Act) in connection with an SEC enforcement inquiry into potential violations of Regulation Fair Disclosure (Regulation FD) relating to a post by Netflix CEO Reed Hastings on his personal Facebook page. The Report notes that although every case 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 site may be used for this purpose — is unlikely to qualify as an acceptable method of disclosure for purposes of Regulation FD. The Report makes clear, however, that companies can use social media outlets like Facebook and Twitter to announce key information in compliance with Regulation FD so long as investors have previously been alerted about which social media will be used to disseminate such information.

Background

On December 5, 2012, Netflix, Inc. and its CEO, Reed Hastings both received Wells notices from the SEC asserting violations of Regulation FD in connection with a Facebook post that Mr. Hastings had made in July 2012 on his personal Facebook page. This post congratulated the company's content licensing team for exceeding one billion monthly viewing hours for the first time ever. Netflix did not file a Form 8-K or issue a press release or any other disclosure at the time of this post.

Regulation FD and Section 13(a) of the Exchange Act prohibit public companies, or persons acting on their behalf, from selectively disclosing material, nonpublic information to certain securities professionals or shareholders where it is reasonably foreseeable that they will trade on that information before it is made available to the general public.

In August 2008, the SEC issued guidance explaining that for purposes of complying with Regulation FD, a company makes public disclosure when it distributes information "through a recognized channel of distribution." 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 that 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. Not surprisingly (given the early stages of social media at the time), the 2008 guidance did not explicitly address the application of Regulation FD to disclosures made through social media channels.

Report of Investigation

A fundamental question raised during the staff's investigation was the application of Regulation FD and the 2008 guidance to issuer disclosures made through rapidly changing forms of communication, including social media channels. The staff noted that issuer communications through social media channels require careful Regulation FD analysis comparable to communications through more traditional channels. The staff also noted that the principles outlined in the 2008 guidance — and specifically the concept that the investing public should be alerted to the channels of distribution a company will use to disseminate material information — apply with equal force to corporate disclosures made through social media channels. In light of the direct and immediate communication from issuers to investors that is now possible through social media channels, such as Facebook and Twitter, the staff indicated that it expects issuers to examine rigorously the factors indicating whether a particular channel is a "recognized channel of distribution" for communicating with their investors.

As stated in the Report, providing appropriate advance notice to investors of the specific channels a company will use for the dissemination of material, nonpublic information would not limit the channels of communication a company could use after appropriate notice. The 2008 guidance encourages issuers to consider including in periodic reports and press releases the corporate web site address and disclosures that the company routinely posts important information on that web site. Similarly, disclosures on corporate web sites identifying the specific social media channels a company intends to use for the dissemination of material non-public information would give investors and the markets the opportunity to take the steps necessary to be in a position to receive important disclosures —e.g., subscribing, joining, registering, or reviewing that particular channel. According to the Report, these are some, but not all, of the methods a company could use to enable evolving social media channels of corporate disclosure to be used as "recognized channels of distribution" in compliance with Regulation FD and the 2008 guidance.

Although the staff noted that every case 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 site may be used for this purpose, is unlikely to qualify as a method "reasonably designed to provide broad, non-exclusionary distribution of the information to the public" within the meaning of Regulation FD.

The Report comes as regulators more generally attempt to accommodate the desire of companies to communicate directly with their customers and shareholders and is a further example of the staff catching up with rapidly developing communication technology. For earlier SEC interpretive guidance regarding internet and electronic media use, see Securities Act Release No. 7856 (April 28, 2000), Securities Act Release No. 7288 (May 9, 1996) and Securities Act Release No. 7233 (Oct. 6, 1995).

* * *

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Mark S. Bergman
+44-20-7367-1601
mbergman@paulweiss.com

David S. Huntington
212-373-3124
dhuntington@paulweiss.com

John C. Kennedy
212-373-3025
jkennedy@paulweiss.com

Edwin S. Maynard
212-373-3024
emaynard@paulweiss.com

Hank Michael
212-373-3892
hmichael@paulweiss.com