CLIENT ALERTS & INSIGHTS

New Warnings from SEC About the Use of Social Media by Public Companies

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Beware how you or your company uses social media---you might be violating federal securities law.

The Securities and Exchange Commission (SEC) is remaining active in its efforts to prevent the selective release of material non-public information, most recently turning its attention to the dissemination of material information by means of social media.

Netflix

On December 5th, Netflix disclosed in a Form 8-K filing that the SEC was considering taking action against the company for a Facebook post by its chief executive officer, Reed Hastings. The SEC has made it clear that it is monitoring social media for any potential violations of Regulation Fair Disclosure, or Regulation FD.

If a public company discloses material non-public information to certain specific types of audiences (broker, dealers, investment advisors, investment managers, investment companies or other holders of the company's securities), the company must disclose that same information publicly. If the company intentionally discloses material non-public information privately, it must simultaneously do so to the public. If the initial disclosure is unintentional, the company must make the disclosure public "promptly", which has been defined as "as soon as reasonably practicable (but in no event after the later of twenty-four hours or the commencement of the next day's trading on the New York Stock Exchange)." Information is deemed disclosed publicly when it is either filed with the SEC or disclosed through a channel "reasonably designed to provide broad, non-exclusionary distribution of the information to the public."

In this case, Mr. Hastings posted in July 2012 on his personal Facebook page that Netflix users were enjoying "nearly a billion hours per month" of streaming video, and proceeded to congratulate Netflix's chief content officer, Ted Sarandos, for reaching such a number. As a result, the SEC issued a "Wells Notice", indicating that the SEC staff planned to recommend instituting proceedings against the company and/or Mr. Hastings for violations of Regulation FD, Section 13(a) of the Securities Exchange Act and various rules issued thereunder. Mr. Hastings and Netflix responded to the notice in a Form 8-K filing, stating that they believed a post to over 200,000 people (Mr. Hastings' Facebook subscribers) was indeed public, and that in any event they did not believe the posted statement was "material" to investors. The Form 8-K filing also stated that the company remained "optimistic that this can be cleared up quickly through the SEC's review process," a statement Mr. Hastings later echoed on his Facebook page.

WebMediaBrands Inc.

This was not the first time that the SEC has used Regulation FD to target a company in its use of social media. For example, in December of 2010, the SEC sent a comment letter to WebMediaBrands Inc., questioning the company about the use of Twitter by Alan Meckler, its CEO. Mr. Meckler had used Twitter frequently to disseminate information regarding future acquisitions and the company's performance. The company responded that it believed the information was not material, but that even if it was material, it was not unreasonable to think that its website (which contained Mr. Meckler's tweets) was the most obvious and recognized channel of distribution for information regarding the company. To date the SEC has not taken any further public action in regard to WebMediaBrands or Mr. Meckler.

Francesca's Collections

In another instance, a company chose to fire its Chief Financial Officer after he used Twitter to disseminate potentially material information. On March 7th, 2012, in advance of the company's earnings release, Gene Morphis, the former CFO of Francesca's Collections, tweeted "Board Meeting. Good numbers=Happy Board." Francesca's Collections claims that it did not find out about the tweet until May 11, at which point it chose to fire Mr. Morphis, perhaps in an attempt to avoid liability under Regulation FD. As of today, no formal action has been taken by the SEC.

Analogous Guidance

The SEC has not given official guidance on how a company's use of social media may impact its obligations under Regulation FD. However the SEC did issue guidance in 2008 on the use of a company website to disseminate information. The guidance provided the following three considerations that would be taken into account to determine if publication on a website would be deemed a public dissemination; (1) whether its website is a recognized channel of distribution; (2) whether the posting of information on its website disseminates the information in a manner making it available to the securities marketplace in general; and (3) whether there is a reasonable waiting period for investors and the market to react to the posted information. While it is possible to analogize these considerations to the universe of social media, there are significant differences between the two, and companies and management should carefully determine whether the information they are disseminating through social media could be considered material.

Thomas Kim, Chief Counsel of the SEC's Division of Corporation Finance, speaking in his personal and unofficial capacity, did shed some light on the possibility of a social media outlet being deemed a public disclosure. Mr. Kim stated that, somewhat analogous to the website guidance, for a social media post to be compliant with Regulation FD, it must (1) be published through a "recognized channel" of distribution and (2) be disseminated in a way that is designed to reach the general public. Although Mr. Kim did seem to indicate that one may be able to disseminate material information through social media, he did mention that the best way to avoid any issues is to first publish the information on the SEC's EDGAR website.

Some companies have included material regarding social media in their Regulation FD compliance and education programs. For example, IBM prohibits its employees from mentioning any type of confidential company information on blogs, websites or other forms of social media, providing guidelines on how to identify such information.

Conclusion

These recent actions by the SEC show that they are paying attention to the use of social media and the implications of social media use under Regulation FD. While social media may be helpful and important to a company's image, it is recommended at this time that a company not use social media to announce material information. A company should first file the information with the SEC or disseminate it through an already recognized public forum prior to publishing information by way of social media. Companies and management need to stay current on new developments in this rapidly evolving area. In addition, companies should continue to review and enhance their social media policies and public reporting processes and procedures. For assistance in developing or reviewing your policies, processes and procedures or if you have questions regarding this area of disclosure and enforcement, please contact any of our securities attorneys below.

Additional Information

For assistance in developing or reviewing your policies, processes and procedures or if you have questions regarding this area of disclosure and enforcement, please contact any of our securitis attorneys below.

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