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## SEC Charges the Cheesecake Factory in First Enforcement Action for Misleading COVID-19 Disclosures

On December 4, 2020, the Securities and Exchange Commission announced that it had settled charges against The Cheesecake Factory for making material misstatements concerning the impact of COVID-19 on its business operations and financial condition.<sup>1</sup> The settlement resolved charges pursuant to Section 13(a) of the Securities Exchange Act of 1934 and Rules 13a-11 and 12b-20 thereunder concerning statements that The Cheesecake Factory had made in press releases attached to Current Reports on Form 8-K dated March 23 and April 3, 2020. Of particular concern to the SEC were statements by The Cheesecake Factory that its restaurants were “operating sustainably” despite internal documents painting a much different picture and showing actual losses of approximately \$6mm per week. This settlement constitutes the first action charging a public company for misleading statements regarding the impact of COVID-19 on business operations and may presage a number of enforcement actions based on COVID-19-related disclosures.

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### Background

At the outset of the pandemic, the SEC published guidance reminding “all companies to provide investors with insight regarding their assessment of, and plans for addressing, material risks to their business and operations.”<sup>2</sup> The SEC emphasized that COVID-19-related disclosures concerning “risks and effects, including how the company and management are responding to them, should be specific to a company’s situation.”<sup>3</sup> The purpose of such disclosures is to “allow investors to evaluate the current and expected impact of COVID-19 through the eyes of management.”<sup>4</sup> The SEC put on notice companies to be proactive and to revise and update their disclosures “as facts and circumstances change.”<sup>5</sup>

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<sup>1</sup> See SEC Charges The Cheesecake Factory for Misleading COVID-19 Disclosures (Dec. 4, 2020), *available at*: <https://www.sec.gov/news/press-release/2020-306>; SEC Order No. 3-20158, *available at* <https://www.sec.gov/litigation/admin/2020/34-90565.pdf>.

<sup>2</sup> SEC Provides Conditional Regulatory Relief and Assistance for Companies Affected by the Coronavirus Disease 2019 (COVID-19) (Mar. 4, 2020), *available at*: <https://www.sec.gov/news/press-release/2020-53>.

<sup>3</sup> SEC: Division of Corporation Finance – Disclosure Guidance: Topic No. 9 (Mar. 25, 2020), *available at*: <https://www.sec.gov/corpfin/coronavirus-covid-19>.

<sup>4</sup> *Id.*

<sup>5</sup> *Id.*

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## Relevant Conduct.

The SEC focused on two Forms 8-K issued by The Cheesecake Factory on March 23 and April 3, 2020. The March 23 Form 8-K indicated that the company was “operating sustainably” during the COVID-19 pandemic and attached a press release, also dated March 23, announcing that it was transitioning to an “off-premise model” that was “enabling the Company’s restaurants to operate sustainably at present under this current model.” The April 3 Form 8-K attached a copy of an April 2, 2020 press release, which provided a preliminary Q1 2020 sales update and once again reiterated that “the restaurants are operating sustainably at present under this [off-premise] model.” Despite these optimistic statements and projections, internal documents painted a different picture of the company’s financial health.

On March 27, 2020, following media reports of the landlord letter, The Cheesecake Factory furnished information to the SEC in another Form 8-K, which disclosed that the company was not planning to pay rent in April and that “it was in various stages of discussions with its landlords regarding ongoing rent obligations, including the potential deferral, abatement and/or restructuring of rent otherwise payable during the period of COVID-19 related closure.”

The SEC alleged that The Cheesecake Factory’s public disclosures on March 23 and April 3 regarding the sustainability of its restaurant operations did not disclose to investors an accurate portrayal of the company’s financial health. In particular, the SEC alleged the Forms 8-K did not disclose: (1) that The Cheesecake Factory was excluding expenses attributable to corporate operations from its claim of sustainability; (2) that the company was, in fact, losing approximately \$6 million in cash per week; and (3) that it had only approximately 16 weeks of cash remaining, even after the \$90 million revolving credit facility.

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## SEC Enforcement Action

Based on the conduct described above, the SEC contended that The Cheesecake Factory’s March 23 and April 3, 2020 Forms 8-K were materially false and misleading and, therefore, violated Section 13(a) of the Exchange Act and Rules 13a-11 and 12b-20 thereunder, which collectively require every issuer of a security registered pursuant to Section 12 of the Exchange Act to file with the Commission accurate current reports on Form 8-K and that such reports contain material information necessary to make the statements made in the reports not misleading.

Without admitting the allegations in the SEC’s Order, The Cheesecake Factory agreed to pay a \$125,000 penalty and to cease-and-desist from further violations of the charged provisions. The SEC considered the cooperation afforded by Cheesecake Factory in accepting the settlement.

In the SEC’s press release, then-Director of the Division of Enforcement said “When public companies describe for investors the impact of COVID-19 on their business, they must speak accurately.”<sup>6</sup> The Enforcement Director added “The Enforcement Division, including the Coronavirus Steering Committee, will continue to scrutinize COVID-related disclosures to ensure that investors receive accurate, timely information, while also giving appropriate credit for prompt and substantial cooperation in investigations.”<sup>7</sup>

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<sup>6</sup> See SEC Charges The Cheesecake Factory for Misleading COVID-19 Disclosures (Dec. 4, 2020), available at: <https://www.sec.gov/news/press-release/2020-306>.

<sup>7</sup> *Id.*

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## Conclusion

Publicly-traded companies should take care to ensure the accuracy of all public disclosures, and The Cheesecake Factory example makes clear that COVID-19-related disclosures are no exception. Due to the fluidity of the situation, care must be taken to update COVID-19 disclosures regularly and on a timely basis as the facts demand. Companies should be aware that the need to update such disclosures may be more frequent in some circumstances than with regard to typical business-related disclosures. The SEC has demonstrated that it will not hesitate to enforce the securities laws as companies continue to navigate the COVID-19 pandemic, and enforcement actions based on COVID-19-related disclosures are likely to continue and could increase under the new administration.

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to call or email authors Bradley J. Bondi at 202.862.8910 or [bbondi@cahill.com](mailto:bbondi@cahill.com); Peter J. Linken at 212.701.3715 or [plinken@cahill.com](mailto:plinken@cahill.com); or Connor Shea at 212.701.3756 or [cshea@cahill.com](mailto:cshea@cahill.com); or email [publications@cahill.com](mailto:publications@cahill.com).

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