SEC: Social Media May be Used for Company Announcements if Investors are Alerted

In a Report of Investigation (the "Report") issued on April 2, 2013, the Securities and Exchange Commission ("SEC") issued guidance to the effect that a public company may use social media such as Facebook and Twitter as distribution channels for announcements provided investors are alerted it is the company's intention to do so.[1]

The Report arose out of an investigation concerning the use in July 2012 by Reed Hastings ("Hastings"), the chief executive officer of Netflix, Inc. ("Netflix"), of his personal Facebook account to announce company metrics. The SEC found that neither Hastings nor Netflix had previously used Hastings' account to disseminate company information, nor had they previously informed investors that they would do so. The SEC determined not to pursue an enforcement action in the case (although it did not explain why), but instead decided to take the opportunity to issue clarifying guidance that acknowledged the evolution of the development and use of social media as distribution channels for company information.

The issues considered in the Report were (a) the applicability of Regulation FD to Hastings' July 2012 post, and (b) the applicability of the SEC's 2008 Guidance on the use of company web sites to this matter.[2]

Background

Regulation FD[3] and Section 13(a) of the Securities Exchange Act of 1934 (the "Exchange Act") prohibit public companies, or persons acting on their behalf, from selectively disclosing material, non-public information to certain securities professionals and shareholders ("enumerated persons") where it is reasonably foreseeable that they will trade on that information, before it is made available to the general public. The SEC's 2008 Guidance explained that for purposes of complying with Regulation FD, a company makes public disclosure when it distributes information "through a recognized channel of distribution." In the 2008 Guidance, the SEC explained that it had "long recognized the vital role of the Internet and electronic communications in modernizing the disclosure system under the federal securities laws and in promoting transparency, liquidity and efficiency in our trading markets."[4] Whether a company's web site would be a recognized channel of distribution for Regulation FD purposes would depend "on the steps that the company has taken to alert the market to its web site and its disclosure practices, as well as the use by investors and the market of the company web site."[5] The SEC stated that the 2008 Guidance was intended to be flexible and adaptive by providing issuers with a "factor-based framework for analysis, rather than static rules applicable only to web sites."[6]

---

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

[2] SEC Release No. 34-58288, *Commission Guidance on the Use of Company Web Sites* (Aug. 7, 2008) ("2008 Guidance"), available at http://www.sec.gov/rules/interp/2008/34-58288.pdf.

[3] 17 C.F.R. § 243.100 et seq.

[4] 2008 Guidance at 6.

[5] 2008 Guidance at 18-19.

[6] Report at 3.

Facts[7]

Over a period of two years, Netflix had stated that it was increasingly focused on expanding its internet streaming business. In a January 4, 2012 press release, Netflix announced that it had streamed two billion hours of content in the fourth quarter of 2011. Netflix made a similar disclosure in a January 25, 2012 letter to shareholders that accompanied its fourth quarter earnings report. The letter was filed with the SEC on a Form 8-K. In June 2012, a statement on Netflix's official blog stated that people were "enjoying nearly a billion hours per month of movies and TV shows from Netflix." Between January 25, 2012 and early July 2012, Netflix did not make any "milestone announcements" regarding streaming.[8]

On July 3, 2012, Hastings posted the following message on his personal Facebook page:

> "Congrats to Ted Sarados, and his amazing content licensing team. Netflix monthly viewing exceeded 1 billion hours for the first time ever in June. When House of Cards and Arrested Development debut, we'll blow these records away. Keep going, Ted, we need even more!"

This announcement disclosed a nearly 50% increase in streaming hours from Netflix's January 25, 2012 announcement. Netflix did not file a Form 8-K or issue a press release through "its standard distribution channels" disclosing the information posted by Hastings. Netflix's stock continued a rise that began when the market opened on July 3, increasing from $70.45 at the time of Hastings' Facebook post to $81.72 at the close of the following trading day.[9] The SEC noted that the news posted by Hastings reached the market "incrementally" as Hastings' personal Facebook page had over 200,000 followers. Thus, several reporters and research analysts picked up the information and wrote pieces about it. The SEC also noted that in December 2012 Hastings publicly stated that Netflix did not "currently use Facebook and other social media to get material information to investors, we usually get that information out in our extensive investor letters, press releases and SEC filings."[10]

Discussion

In analyzing and expanding on its 2008 Guidance, the SEC made two points.

First, issuer communications through social media channels require careful Regulation FD analysis comparable to communications through more traditional channels. The SEC noted that Regulation FD applies when an issuer discloses material, non-public information to enumerated persons and prohibits selective disclosure "[w]henever an issuer, or any person acting on its behalf, discloses any material non-public information regarding that issuer" to any such person.[11]

Accordingly, the SEC emphasized for issuers that all disclosures to groups that include an enumerated person should be analyzed for compliance with Regulation FD. Specifically, if an issuer makes a disclosure to an enumerated person, including to a broader group of recipients through a social media channel, the issuer must

---

[7] Section 21(a) of the Exchange Act authorizes the SEC to investigate violations of the federal securities laws, and, in its discretion, "to publish information concerning any such violations." The SEC stated that the Report did not constitute an adjudication of any fact or issue and the facts discussed in the Report were matters of public record or based on documentary records. Report at 2, note 2. The facts set forth in this memorandum are derived from the Report.

[8] Report at 4.

[9] Id.

[10] Report at 5.

[11] 17 CFR § 243.100(a).

consider whether that disclosure implicates Regulation FD. This would include determining whether the disclosure includes material, non-public information. Further, if the issuer were to elect not to file a Form 8-K, the issuer would need to consider whether the information was being disseminated in a manner "reasonably designed to provide broad, non-exclusionary distribution of the information to the public."[12]

Second, in light of the direct and immediate communication from issuers to investors that is now possible through social media channels, the SEC stated it expects issuers to examine rigorously the factors indicating whether a particular channel is a "recognized channel of distribution" for communicating with their investors. The SEC emphasized that it was "critical to the fair and efficient disclosure of information" that issuers take steps to alert the market about:

- which forms of communication a company intends to use for the dissemination of material, non-public information, including the social media channels that may be used, and
- the types of information that may be disclosed through these channels.

Without such notice, the investing public would be forced to keep pace with a changing and expanding universe of potential disclosure channels, a virtually impossible task.[13]

The SEC cautioned that although every case must be evaluated on its own facts, disclosure of material, non-public 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. This is true even if the individual in question has a large number of subscribers, friends, or other social media contacts, such that the information is likely to reach a broader audience over time. It was the SEC's view that personal social media sites of individuals employed by a public company would not ordinarily be assumed to be channels through which the company would disclose material corporate information.[14]

Conclusion

While the SEC's 2008 Guidance was primarily directed at the use of corporate web sites for the disclosure of material, non-public information, the SEC used that guidance as an analytic framework for permitting issuers to use social media to satisfy Regulation FD disclosure requirements, provided that issuers give adequate notice to investors of the intention to use social media for such purpose.

* * *

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, please do not hesitate to call or email Charles A. Gilman at 212.701.3403 or cgilman@cahill.com; Jon Mark at 212.701.3100 or jmark@cahill.com; or John Schuster at 212.701.3323 or jschuster@cahill.com.

[12] 17 CFR § 243.100(e)(1)-(2).

[13] Report at 7.

[14] Id.