Client Alert

September 2013

SEC Brings Enforcement Action Under Regulation FD Against Investor Relations Professional

Since its adoption in 2000, Regulation FD has prohibited public companies and personnel acting on their behalf from selectively disclosing material, nonpublic information to groups such as brokers, analysts and investors without concurrently making widespread public disclosure. In its latest enforcement action under Regulation FD, the Securities and Exchange Commission (Commission) targeted the former vice president of investor relations (the Vice President) of a publicly traded solar energy company (the Company) for making selective disclosure of material, nonpublic information to analysts and institutional investors. The Commission chose not to pursue charges against the Company itself because of the Company's strong compliance program and high degree of cooperation in the investigation.

According to the Commission's order[1], the Company obtained conditional commitments from the Department of Energy (DOE) in June 2011 for loan guarantees on three separate solar projects; these guarantees were expected to lower the Company's total cost of financing. Between June and September 2011, many analysts authored reports speculating that the Company would meet the conditions for obtaining two of the three guarantees, though there was uncertainty as to whether the Company would meet the conditions for the third (and largest) guarantee. As late as September 13, 2011, the Company's CEO publicly expressed confidence that it would receive all three guarantees.

On September 15, 2011, several executives of the Company, including the Vice President, learned that DOE had decided not to provide the loan guarantee with respect to the third project. The executive team then began a dialogue with in-house counsel as to how to manage disclosure of these developments in a manner consistent with Regulation FD. Between September 16 (a Friday) and September 21 (a Wednesday), the Company began framing a press release announcing that the third guarantee would not be forthcoming. On September 20, an inquiry from a congressional committee to DOE concerning the loan guarantee program generally and more specifically the status of unclosed obligations such as the Company's three guarantees caused a stir in the market. At the market's open on September 21, the Company's stock price dropped nearly 8 percent. The Company also began to receive inquiries from analysts and investors as to the status of its DOE guarantees.

Arriving at work on September 21, the Vice President knew the Company's press release regarding the third project had not been published. But he set to work at drafting talking points he and a subordinate would use throughout the day in fielding calls from the analyst and investor communities. In particular, the talking points indicated a higher probability of receiving the first two guarantees, but a lower probability of receiving the third guarantee, contrary to the Company CEO's message a week earlier. The Vice President also referred to a rumor circulating in the market, which the Company had not previously confirmed, that another large company would purchase the third project, mitigating the failure to receive a DOE guarantee in respect of that project. Moreover, the Vice President went beyond the "high probability/low probability" message and told at least one analyst and one institutional investor that to be

[1] The complete order is available at http://www.sec.gov/litigation/admin/2013/34-70337.pdf. Our description of the factual background to the Commission's investigation is derived from the narrative in this order.

conservative they should assume the Company would not receive the third guarantee at all. Analysts on several occasions communicated these messages to their equity sales teams.

On the evening of September 21, the Company's management learned from a news article about the Vice President's selective disclosures. Accordingly, they finalized the press release regarding the failure to obtain the third guarantee and issued it prior to the market's open on September 22. The Company's stock price opened that morning down 6 percent.

According to the Company's Form 10-K filed in February 2012, the Company immediately self-reported the potential violation to the Commission on September 23, 2011. The Company then began an internal investigation conducted on behalf of the Company's board of directors by independent outside counsel. The Company also reported in its Form 10-K that on November 17, 2011, the Commission issued a formal order of investigation into the matter, though it is likely that the Commission's staff had been informally investigating it prior to that date.[2]

As a result of the Vice President's conduct, the Commission alleged that his selective disclosure of material, nonpublic information caused the Company to violate Section 13(a) of the Securities Exchange Act of 1934 and Regulation FD promulgated thereunder. The Commission's order did not analyze the materiality of the information disclosed, but presumably an email authored by the Vice President noting its materiality was part of the overall analysis. The Vice President settled the Commission's charges on a neither admit nor deny basis, agreeing to pay a $50,000 civil monetary penalty and to cease and desist from committing or causing future violations of Section 13(a) and Regulation FD.

The Commission decided not to bring any enforcement action against the Company due to what it described as "extraordinary" cooperation during the investigation and other factors. The Commission's press release announcing settlement with the Vice President noted that before his violation, the Company promoted a culture of compliance through its use of a disclosure committee focused on Regulation FD compliance. When the Vice President made his selective disclosure, the Company immediately discovered it and issued a press release before the market opened the next morning. Notably, the Company then self-reported the misconduct to the SEC quickly. Further, during the Commission's investigation of the case, the Company undertook remedial measures to address the misconduct, including conducting supplemental Regulation FD training for employees with public disclosure responsibilities.

Enforcement actions under Regulation FD are relatively infrequent, but each is generally instructive. Developing a strategy to communicate sensitive information is a task every public company confronts at one time or another. This case serves as a good reminder for investment relations and public relations personnel not to get ahead of management in publicly disseminating such information. The Commission's factual narrative seems to suggest that the Vice President had some level of awareness that his actions were violative of Regulation FD during the period in question, but it is also important to note that the Commission need not prove any particular state of mind in pursuing a Regulation FD violation. Here, the decision to self-report within two days of the violation (and the day after the issuance of the definitive press release) demonstrates the potential value of such immediate action, though there is no consensus among practitioners as to how quickly one must self-report relative to the status of an internal investigation in order to obtain favorable treatment from the Commission. Finally, the decision not to charge the Company also underscores the importance of robust internal compliance mechanisms and the value of responding promptly and comprehensively to deviations from the Commission's regulations.

[2] A "formal order" of investigation grants Commission staff subpoena power to collect evidence, but the Commission staff can conduct an "informal" investigation without that authority at any time. Indeed, the Commission has delegated authority for issuing formal orders to senior leadership in the Division of Enforcement, meaning the Commission no longer votes whether to issue them. In any event, enforcement recommendations to the Commission can come from either type of investigation.

Contacts

Susan S. Failla
sfailla@hunton.com

Scott H. Kimpel
skimpel@hunton.com

W. Lake Taylor, Jr.
tlake@hunton.com