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## Regulation FD: Recent Developments

Several recent events indicate that the Securities and Exchange Commission is again turning its attention to Regulation FD, and compliance policies with respect to this regulation may need to be reevaluated.

### Overview

Regulation FD requires that when an issuer intentionally discloses material nonpublic information to broker-dealers, investment advisers, investment companies or holders of its securities, the issuer must make a simultaneous public disclosure. A recent rise in enforcement activity, including a high-profile settlement with Office Depot, indicates that the SEC is beginning to clamp down on violations of Regulation FD after years of infrequent enforcement activity. In addition, the Dodd-Frank Act and resulting SEC rulemaking have made Regulation FD's applicability to credit rating agencies an open question, and confusion regarding what qualifies as "fair disclosure" has increased with the growing use of corporate websites for disclosure of earnings information. The purpose of this release is to provide a brief update on each of these three issues.

### Regulation FD Enforcement — Office Depot Settlement

Since September 2009, the SEC has brought four separate Regulation FD

enforcement actions against public companies, compared to only one during the previous four-year period. Most notably, the SEC recently settled an enforcement action with Office Depot for allegedly disclosing material nonpublic information to securities analysts without making simultaneous public disclosures.<sup>1</sup> The Office Depot enforcement action entailed analyst calls allegedly coordinated by the company's then-CEO and then-CFO and carried out by the company's investor relations (IR) director in June of 2007. Concerned about the prospect of Office Depot's falling short of its analysts' earnings per share (EPS) projections for the second quarter of 2007, the then-CEO and then-CFO instructed Office Depot's IR director to call analysts and the company's largest institutional investors in an attempt to reduce their expectations for earnings. While Office Depot's IR director made no explicit statements regarding Office Depot's weaker-than-expected earnings, he in essence conveyed that message by referring the analysts and investors to (i) the company's prior cautionary statements and (ii) announcements by other companies regarding the negative impact of the slow economy on their earnings.

<sup>1</sup> See *SEC v. Office Depot, Inc.*, Litigation Release No. 21703 (Oct. 21, 2010), available at <http://www.sec.gov/litigation/litreleases/2010/lr21703.htm>.

After discovering Office Depot's actions, the SEC charged the company, its then-CEO and then-CFO with violations of Regulation FD. Office Depot chose to settle the charges, agreeing to pay \$1 million without admitting or denying the allegations levied by the SEC. Office Depot's then-CEO and then-CFO also paid \$50,000 each in penalties. In its announcement regarding the settlement of the charges, the SEC emphasized that disclosing material nonpublic information whether "expressly or through signals" is prohibited by Regulation FD. In its initial complaint against Office Depot, the SEC also highlighted the fact that Office Depot did not have a policy for compliance with Regulation FD in place at the time of the alleged violations.

The Office Depot case illustrates an increased focus on enforcement of Regulation FD by the SEC, and companies would be well advised to revisit their Regulation FD compliance policies and related procedures and training.

### **Credit Rating Agency Reform**

The Dodd-Frank Wall Street Reform and Consumer Protection Act amended Regulation FD to remove the exemption for "entities whose primary business is the issuance of credit ratings."<sup>2</sup> Previously, the exemption from Regulation FD specifically allowed issuers to share material nonpublic information with ratings agencies without risking violations of Regulation FD. However, the removal of that exemption does not clearly

<sup>2</sup> Section 939B of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.

subject ratings agencies to Regulation FD, because Regulation FD expressly applies to certain listed entities, such as broker-dealers, shareholders and investment advisers. As ratings agencies are not among the listed entities, the repeal of their exemption under Regulation FD arguably should have no effect on how issuers share information with them if the statute is interpreted narrowly. Nonetheless, the removal of the Regulation FD exemption creates justifiable concerns for issuers who share sensitive information with ratings agencies. The SEC has consistently interpreted Regulation FD broadly, and the legislative history of the Dodd-Frank Act shows some indications that Congress intended to make Regulation FD applicable to ratings agencies.

Regardless of the explicit scope of Regulation FD, issuers should consider implementing necessary protections for the release of highly sensitive information to credit ratings agencies, including potential violations of Rule 10b-5 under the Securities Exchange Act of 1934 and the possibility of leaks and misuse of such information. Notably, Regulation FD specifically permits issuers to share material nonpublic information with an entity, including those covered by Regulation FD, when the issuer and entity have previously entered into a confidentiality agreement. Given the foregoing risks and Regulation FD's specific exemption for information shared under a confidentiality agreement, many issuers currently find it prudent to request confidentiality agreements before sharing information with ratings agencies. Similarly, issuers with preexisting arrangements with credit rating agencies should

consider seeking new confidentiality agreements or revisiting the terms of their current agreements.

### **Recent Trends in Website Postings of Earnings Materials**

Recent announcements by prominent companies have raised the prospect of increased use of corporate websites in disclosing earnings information. Press coverage of these announcements indicated that these companies were relying on an interpretive release, issued by the SEC in 2008, that allowed issuers the option of disclosing material information via their corporate websites to satisfy their Regulation FD obligations, but only if those websites are "recognized channels of distribution of information."<sup>3</sup> The wording of the companies' announcements and related press coverage seemed to suggest that companies might be able to disclose earnings through their corporate websites alone. However, unlike some other disclosures of material nonpublic information, earnings releases are subject to SEC requirements beyond those imposed by Regulation FD and must be submitted to the SEC on Form 8-K (Item 2.02).

While the companies that made such announcements (e.g., Google and Microsoft) stated that their financial disclosures would be made "exclusively via their corporate websites," in practice these companies file or furnish Forms 8-K and issue brief newswire releases announcing earnings and providing a link to their full earnings, which are simultaneously posted on their websites. This approach means that, in essence,

<sup>3</sup> See SEC Release No. 34-58288 (August 1, 2008), available at <http://www.sec.gov/rules/interp/2008/34-58288.pdf>.

companies that adopted “website-only” disclosure simply traded using newswire services for the cheaper option of disclosing full earnings releases through their own websites. Because these companies continue to file or furnish accompanying Forms 8-K and issue announcements prior to the posting of earnings materials, they cannot be said to be relying on the 2008 SEC interpretive guidance for satisfaction of their Regulation FD obligations by corporate website posting alone — the Regulation FD obligation is satisfied by the Form 8-K submission, which is still specifically required for earnings releases.

Nonetheless, some Regulation FD compliance questions remain with respect to website disclosure, such

as: (1) “Can the earnings releases be filed or furnished on Form 8-K after the website posting?” and (2) “When can the company rely on its website for disclosure of information other than earnings for which no Form 8-K disclosure is specifically required?”<sup>4</sup> The recent delays experienced by Google and Microsoft in filing or furnishing their earnings releases on Form 8-K *after* the website posting are testing the SEC’s requirements for “simultaneous” “public disclosure” and bringing the potential issues with website-only disclosure into focus. Furthermore, recent publications highlighted an

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<sup>4</sup> Notably, according to a recent survey posted on [www.thecorporatecounsel.net/blog/index.html](http://www.thecorporatecounsel.net/blog/index.html), only 5.6% of companies reported that they rely on website postings alone to satisfy Regulation FD.

additional issue pertaining to website postings of earnings materials without a newswire dissemination: they are not timely picked up by leading finance-related websites where many investors monitor their investments. Some commentators have argued that without dissemination of earnings information through newswire services or the presence of a real-time web-based newsgathering source to publicize website-only earnings releases, releases that are posted on corporate websites only could put some investors at an informational disadvantage. How the SEC and IR community choose to address the foregoing issues will help determine the future of website postings of earnings materials as a method of Regulation FD compliance.