

Regulation FD (Fair Disclosure) Enforcement Actions Are Back After Five-Year Absence

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Over the past six months, the Securities and Exchange Commission (SEC) commenced two formal actions against corporate spokespersons and an issuer alleging violations of Regulation FD. While these two recent actions do not present novel fact patterns, they certainly suggest that the SEC has renewed its focus on Regulation FD after a five-year hiatus. As a result, public companies should continue to review and monitor their Regulation FD compliance policies, training procedures and controls to prevent selective disclosure and maintain response teams to address potential violations through prompt action.

Regulation FD and its Enforcement History

The SEC adopted Regulation FD in August 2000 in response to concerns that public companies were selectively disclosing material, non-public information to certain institutional market participants at the expense of individual investors. Regulation FD prohibits a public company and any person acting on its behalf from privately disclosing material, non-public information about the company or its securities to certain persons outside the company (such as securities analysts and institutional investors) where it is reasonably foreseeable that investors will trade the company's securities on the basis of the information. In the event such information is disclosed privately, it must also be disclosed publicly, either simultaneously, if the private disclosure is intentional, or promptly (generally within 24 hours) if the private disclosure is unintentional.

From 2002 to 2005, to highlight the priority that the SEC would be giving to the enforcement of Regulation FD, the SEC brought seven enforcement actions against companies and certain officers and investor relations representatives. Five of the seven actions involved similar fact patterns related to the selective disclosure of earnings guidance. In almost all instances, the actions were resolved through settlements with penalties (typically including monetary fines) and cease-and-desist orders. In 2005, however, the SEC unsuccessfully brought a second Regulation FD action against Siebel Systems, Inc. (Siebel II). In Siebel II, the SEC claimed that the private remarks of Siebel's chief financial officer regarding business activity levels and the company's transaction pipeline were materially different from public statements made

by Siebel's chief executive officer earlier in the month. The district court disagreed and dismissed the SEC's complaint. From 2006 to September 2009, the SEC brought only one Regulation FD enforcement action. The SEC, however, did update its Compliance and Disclosure Interpretations relating to Regulation FD in August 2009 to provide some additional guidance regarding selective disclosure.

Two Recent SEC Enforcement Actions

Black

In September 2009, the SEC filed a civil action against the former chief financial officer of American Commercial Airlines, Inc. (ACL) for selectively disclosing material, non-public information. The complaint alleged that ACL's chief financial officer, Christopher Black, sent an e-mail to eight sell-side analysts from his home on a weekend, stating that the company's earnings per share would likely be lower than the guidance that the company publicly forecasted only a few days earlier. Black did not provide his e-mail to anyone at ACL or to counsel prior to sending it to analysts. On the first trading day after Black's e-mail, ACL's stock price dropped 9.7% on unusual volume. ACL learned of Black's e-mail the same day and filed a Form 8-K disclosing the information at the end of the trading day. In contrast to Siebel II, the Black action marked a return by the SEC to enforcement that squarely fell within the scope of Regulation FD as Black's comments on earnings could not be viewed as previously disclosed public information. The SEC, however, did not bring an enforcement action against ACL for several reasons. First, according to the SEC, ACL "cultivated an environment of compliance" by providing training regarding the requirements of Regulation FD and adopting policies that implemented controls to prevent violations. Second, ACL publicly disclosed the material information the same day it became aware of the selective disclosure, self-reported the incident to the SEC staff, and provided extraordinary cooperation with the staff's investigation. Last, ACL took remedial measures to prevent such conduct in the future, including implementing additional controls.

Presstek/Marino

On March 9, 2010, the SEC filed a civil injunction action against Presstek, Inc. and its former chief executive officer, Edward Marino, for violations of Regulation FD. The complaint alleges that Marino, two days before the end of the company's third quarter, had a telephone conversation with a registered investment adviser and negatively commented on the company's third quarter performance. In contrast to Siebel II, where the court determined that the comments regarding business activity levels and the company's transaction pipeline were already publicly known, Marino's comments regarding the company's financial performance made immediately prior to the end of the company's quarter were non-public information at the time of the disclosure. Within minutes of the call ending, the adviser sold substantially all of its Presstek holdings and the stock price dropped 19%. Presstek did not disclose the negative material, non-public information until the next day. According to the complaint, Presstek had an internal policy that prohibited authorized spokespersons from having discussions with outside parties about non-public information during designated blackout periods. Presstek agreed to settle the SEC's charges and pay a fine of \$400,000. The SEC's civil action against Marino remains ongoing. In connection with the SEC's settlement against Presstek, the SEC took into account remedial measures taken by Presstek, which included revising its corporate communications policies and corporate governance principles, replacing its management team, and appointing new independent board members.

Issuers Should Continue to be Vigilant When it Comes to Regulation FD

The Black and Presstek actions indicate that the SEC has renewed its Regulation FD enforcement efforts. However, unlike in Siebel II, the conduct of the defendants in these actions presented relatively straightforward Regulation FD enforcement cases. As a result, public companies can use these actions as good educational tools and reminders for their officers and investor relations representatives who are responsible for communications with the market. In addition, in light of these actions by the SEC, companies are well-advised to take the following steps:

- Review your Regulation FD compliance programs. Taken together, the two recent SEC enforcement actions indicate that an effective, up-to-date, and active compliance program could benefit a company in dealing with the SEC regarding a potential Regulation FD violation and could either result in no SEC action against the company or limited penalties. Training, refresher courses and certifications should be administered on a continuous basis.
- Maintain a crisis management plan to limit company exposure. Public companies should have in place a response team to quickly ascertain whether an intentional or unintentional Regulation FD violation has occurred and the remedial actions that may need to be taken, including the filing of a Form 8-K as soon as possible. The crisis management plan should also include consideration of self-reporting to, and extensive cooperation with, the SEC and its staff – two additional key factors that have proven to be important to the SEC in considering whether to limit the action it may take against a company in connection with a potential Regulation FD violation.

If you have any questions about the content of this advisory, please contact the Pillsbury attorney with whom you regularly work or the authors below.

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