

regulation FAIR disclosure

Companies are adjusting to new rules requiring broad dissemination of market-moving information.

Since the SEC's implementation of Regulation Fair Disclosure last October, companies are adapting to new regulations on how they communicate with the investing community, particularly with analysts and institutional investors.

The purpose of "Reg FD" is to ensure that select groups of investors are not privy to market-moving information ahead of others. Corporate executives must now avoid divulging material, nonpublic information during their communications with analysts and select shareholders. And if they inadvertently do, they must take steps to broaden public dissemination within 24 hours of discovering the disclosure.

While no violations have yet been found, the SEC is investigating some potential violations. The Commission also is seeking input on ways to possibly improve the new rule.

The rule does not apply to issuer communications with the press, rating agencies and ordinary-course business communications

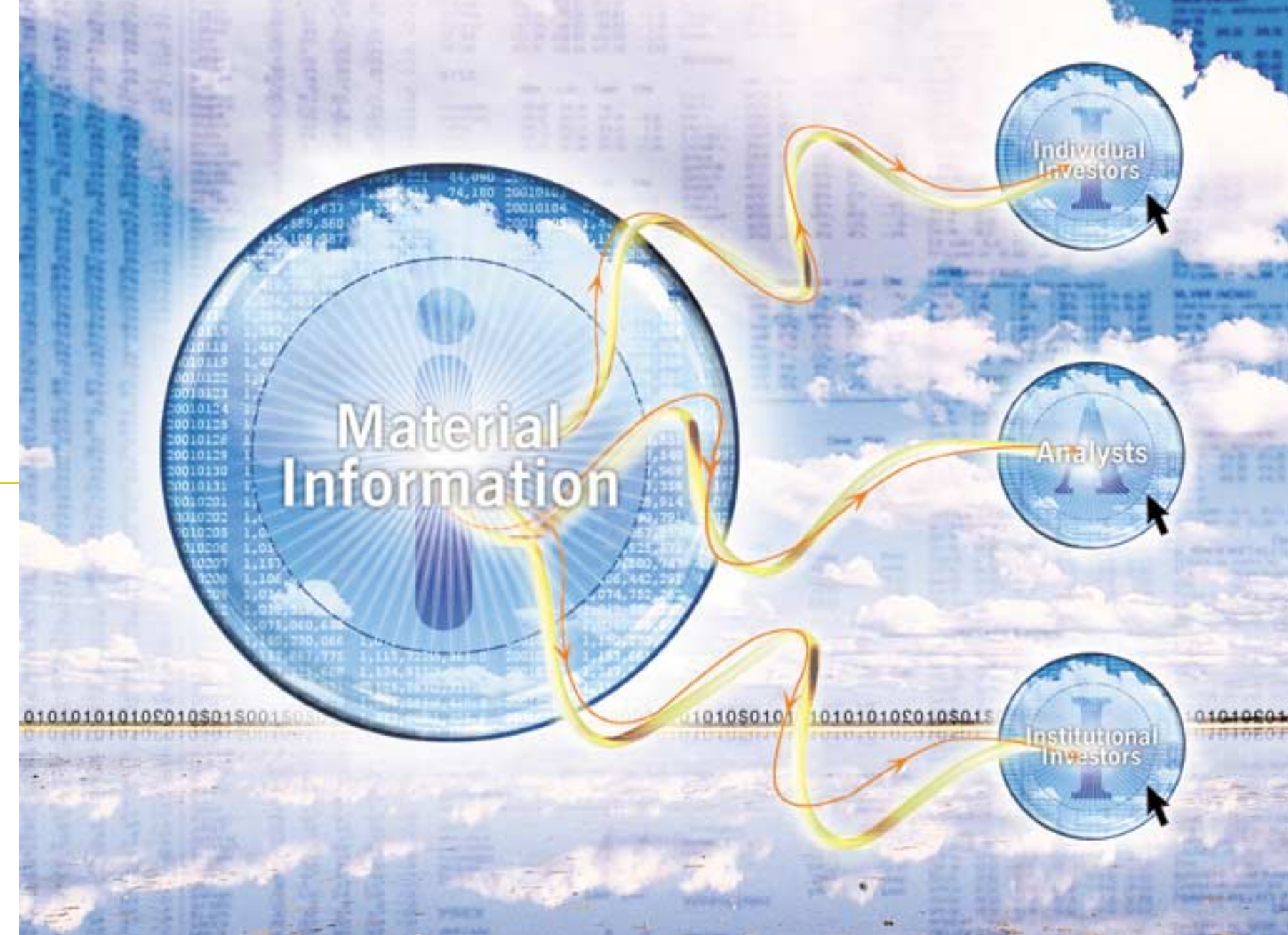
with customers and suppliers. Also, following a recommendation by the NYSE, the SEC exempted foreign private issuers. In addition, the regulation applies only to communications by the issuer's senior management, investor-relations professionals and others who regularly communicate with market professionals and security holders.

Reg FD "places the responsibility for avoiding selective disclosure, and the risks of engaging in it, squarely on the issuer," noted Richard H. Walker, SEC enforcement director, in a recent speech.

The rule also was meant to codify what the SEC considers best practices, according to Walker. For many companies it's business as usual: They're embracing the new regulation and broadening their communications with new technologies, such as Webcasts, streaming conference calls and Internet earnings announcements.

EMC Corp. (EMC), an early adopter of open-access communication with all shareholders, has been openly telecasting earnings conference calls for nearly 10 years and Webcasting the calls since the technology became viable. Polly C. Pearson, EMC's vice president of global investor relations, emphasizes the logic of frequent and consistent communication with as broad an investor base as possible. "We aim to continually build understanding and appreciation for EMC," she said. "Communicating with just a subset of the investing population does not make sense to me. With a supply-and-demand dynamic, why would you want to diminish the demand?"

Reg FD has encouraged EMC to increase its communication with investors, Pearson said. The company recently wanted to share information on the tone of its business in light of speculation on a weakening U.S. economy. A dilemma arose about how to share this information, because the content did not fit classic news-release parameters. EMC opted to distribute a "Statement," with its views written in a straightforward format via BusinessWire. "It made communicating our views with investors swift, open and, if you



can believe it, stress-reducing," Pearson said. "Even though the information wasn't all rosy, we actually received thank-you notes from some of our institutional investors.

"Bottom line," she said, "I aim to build a long-term relationship with EMC's investors. Relationships depend on mutual trust. It is hard to build trust in a relationship without frank and open communication."

Still others have had to change the way they handle information. For example, Reg FD does not consider disclosure of material news during an annual shareholder meeting as broad dissemination. A company must use a press release, open Webcast, teleconference or Form 8-K to publicize material information either before or while the meeting is taking place.

As they attempt to comply with the rule, some companies are relying heavily on their attorneys for advice and are including them in

all their communications with shareholders. Others have become guarded about the information they give out or have stopped talking altogether, eliminating one-on-one analyst meetings and regular conference calls.

"No one wants to be the test case for noncompliance," said Gwenn L. Carr, vice president and secretary, **MetLife Inc. (MET)**. Carr, who chairs the American Society of Corporate Secretaries and the Investor Responsibility Research Center, moderated a panel on Reg FD during the NYSE's Corporate Governance Conference earlier this year.

coping with the changes

So how do companies maintain relationships with analysts and comply with the rule? "If there's a public meeting with notice in which material information is disclosed, there cannot be an FD violation," said Harvey J. Goldschmid, Columbia University's Dwight Professor of Law and former general counsel of the SEC, at the NYSE's conference.

Goldschmid, who presented the original Reg FD draft in December 1999, also recommended confidentiality agreements. "It's perfectly possible, even after something is inadvertently disclosed, to simply tell the analyst that it is confidential," he explained. "If he or she agrees to keep it confidential, there is no selective disclosure problem."

Carr said MetLife's new corporate guidelines in light of Reg FD include a review by general counsel of all presentation materials used in conferences or sessions with analysts, publicized advance notice of all conferences and conference calls with replays

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made available, and a list of those authorized to speak on the company's behalf. "Our advice to employees is, 'If you are not authorized to speak, then don't do so,'" she said. Carr also said that she reminds employees that "revealing material, nonpublic information could expose them to risk under insider-trading laws, which have not disappeared."

Such guidelines, however, do not address what the SEC might consider "material information." Reminding the audience that issuers are protected by Reg FD's culpability standard, Goldschmid said a materiality judgment, or judgment of what is and is not public, must be "intentional" or "reckless" for a violation to occur.

"You have to be way off on a materiality judgment before there can be any possibility of liability," he said. According to Walker, "an issuer's incorrect determination that

information is not material must represent an 'extreme departure' from standards of reasonable care in order for us to allege a violation."

So what information of value can issuers share one-on-one with analysts? Walker referred to so-called mosaic information, noting that "an issuer may convey to an analyst information that might seem inconsequential to the typical investor but which a skilled analyst may use to form a mosaic that reveals a material conclusion."

Some companies are still uncomfortable with the uncertainty of the rule's materiality standard. Eric D. Roiter, senior vice president and general counsel, Fidelity Management & Research Co., another NYSE conference panelist, said this uncertainty has created a "no-fly zone" for companies with information that is not only clearly material, but information that might be material and even what is likely immaterial," he said. "The effect is to cloud the process by which an analyst may probe management."

Both Roiter and Goldschmid encourage analysts to continue pushing for information despite issuers' tendencies to clam up. "The things we want analysts doing—digging, kicking the tires, questioning, building a mosaic—are perfectly appropriate under Reg FD," said Goldschmid.

Auto-industry analyst David Bradley, a managing director of **J.P. Morgan Chase & Co. (JPM)**, told issuers at the conference to fight the tendency to withhold information. "It is a disservice to your investors and your companies, and it goes against your mission statement of maximizing shareholder value." Instead, he encouraged issuers to "find a way to make the communication happen. That is what the best companies are still doing." Walker agrees, noting: "The market will reward companies that provide timely, reliable information and will treat more skeptically those that do not."

DOS AND DON'TS UNDER REG FD

DO:

- Establish corporate guidelines for operating under Reg FD, such as procedures for spotting potential Reg FD issues and market movements that could be a result of inadvertent disclosure.
- Designate key spokespeople for your company and educate them on the rule.
- Open meetings, conferences and teleconferences to the public and provide ample notice of such venues.
- Fight the tendency to withhold information and continue to communicate with analysts and shareholders.
- Explore new ways of regularly communicating with the public, such as through press releases on the general state of the business.
- Promptly disseminate to the public any inadvertently disclosed material news.
- Consider the use of confidentiality agreements if information is disclosed selectively.

DON'T:

- Disclose material, nonpublic information to analysts, institutions or other shareholders who could trade on the information.
- Consider information posted on a corporate Website to be broadly disseminated public information.
- Refrain from talking to analysts and investors altogether.
- Delay more than 24 hours before disseminating to the public material information that is inadvertently disclosed to a select audience.

NYSE timely alert policy

Meanwhile, listed companies must comply with the NYSE's longstanding Timely Alert policy, which also encourages rapid and broad dissemination of material information. Although Reg FD gives companies 24 hours to release a statement following unintentional selective disclosure and permits 8-K SEC filings and Webcasts as suitable public disclosure, the Exchange traditionally has stressed more immediate disclosure by using press releases. It still considers the press release the best way to reach the widest audience quickly.

In fact, the SEC has specifically addressed the interplay between Reg FD and exchanges' policies by stressing that it "did not intend the regulation to supplant the rules of self-regulatory organizations." This means that listed companies must continue to publicly release any information that might materially affect the market for its securities. Listed companies also must notify the Exchange 10 minutes in advance of any release occurring during regular trading hours. This gives the NYSE time to evaluate the significance of the news and determine whether to halt trading.

As the debate over Reg FD continues, one thing for sure is that the quantity and delivery of corporate information is changing. "Analysts are still getting information, but more information is out to the public, more information is getting out earlier, and more conference calls are open," Goldschmid said. Although acknowledging that any evidence is, so far, anecdotal, he added: "There is no doubt that selective disclosure is significantly down, and that's where we want things to be." □