

SEC Emphasizes Anti-Fraud Protections During COVID-19 Pandemic

Article

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On March 23, 2020, the co-directors of the Division of Enforcement of the U.S. Securities and Exchange Commission (SEC) issued a statement regarding market integrity during the COVID-19 pandemic[1]. Specifically, the statement serves to remind public companies of their obligations to maintain disclosure controls and procedures regarding material nonpublic information. The SEC has worked to accommodate disclosure filing deadlines due to the extenuating circumstances. This nonpublic information may be even more valuable now than during times of regular business operations. Because of this, the statement explains, public disclosures that normally occur through filings may be delayed[2], which could give rise to the potential to abuse the nonpublic information due the extended filing period.

The obligation to maintain the confidentiality of nonpublic information, giving rise to what is commonly called “insider trading”, has been heightened recently with allegations that some members of Congress may have sold stocks after early briefings on the business impact of COVID-19. This is not the only time in recent history where members of government have been accused of profiting based on classified or nonpublic briefings. As a result, the SEC has emphasized its commitment to robust investigation and enforcement of its rules and regulations.

It is important to note that the antifraud provisions of securities laws and regulations apply not only to publicly-held companies, but also privately-held “exempt” securities offerings. Additionally, this covers not just equity (stock or partnership/LLC ownership) but debt securities offerings as well. Private companies offering securities during this time of economic uncertainty need to ensure that any disclosures made to potential investors are straightforward and truthful. The SEC has broad investigative powers to investigate false or misleading statements made by private issuers of securities. This applies to statements made orally or in writing and to omission of material information from communications relating to offerings (in addition to the making of false or misleading statements). Keep in mind that the SEC’s antifraud rules carry steep civil and criminal penalties for violation of these rules.

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Entrepreneurship and start-up activity has recently been growing at a healthy pace, and there is no doubt that the challenges presented by COVID-19 will spur new start-ups and economic activity relating to the pandemic in a variety of market sectors, from medical and consumer devices to services. At the same time, the pandemic will also present challenges to many existing early stage business ventures. During this extraordinary time, businesses should be careful to check the validity and accuracy of information disclosed to potential investors. We will continue to work with clients to ensure that accurate and complete material information is disclosed to investors.

[1] <https://www.sec.gov/news/public-statement/statement-enforcement-co-directors-market-integrity>.

[2] <https://www.sec.gov/rules/other/2020/34-88318.pdf>.

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