SECURITIES AND EXCHANGE COMMISSION

SECURITIES AND EXCHANGE ACT OF 1934
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Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: Netflix, Inc., and Reed Hastings

I. Introduction

The Division of Enforcement has investigated whether Netflix, Inc. ("Netflix") and its Chief Executive Officer, Reed Hastings ("Hastings") violated Regulation FD (17 C.F.R. §243.100 *et seq.*) and Section 13(a) of the Securities Exchange Act of 1934 ("Exchange Act"). The Commission has determined not to pursue an enforcement action in this matter. The investigation concerned Hastings's use of his personal Facebook page, on July 3, 2012, to announce that Netflix had streamed 1 billion hours of content in the month of June. Neither Hastings nor Netflix had previously used Hastings's personal Facebook page to announce company metrics, and Netflix had not previously informed shareholders that Hastings's Facebook page would be used to disclose information about Netflix. The post was not accompanied by a press release, a post on Netflix's own web site or Facebook page, or a Form 8-K.

The investigation raised questions regarding: 1) the application of Regulation FD to Hastings's post; and 2) the applicability of the Commission's August 2008 Guidance on the Use of Company Web Sites[1] to emerging technologies, including social networking sites, such as Facebook.

Regulation FD and Section 13(a) of the Exchange Act prohibit public companies, or persons acting on their behalf, from selectively disclosing material, nonpublic information to certain securities professionals, or shareholders where it is reasonably foreseeable that they will trade on that information, before it is made available to the general public. The Commission's 2008 Guidance explained that for purposes of complying with Regulation FD, a company makes public disclosure when it distributes information "through a recognized channel of distribution."

In its investigation, the SEC staff learned (and some public commentary further suggested) that there is uncertainty concerning how Regulation FD and the Commission's 2008 Guidance apply to disclosures made through social media channels. Since the issuance of the 2008 Guidance, the use of social media has proliferated and the Commission is aware that public companies are increasingly using social media to communicate with shareholders and the market generally. The ways in which companies may use these social media channels, however, are not fundamentally different from the ways in which the web sites, blogs, and RSS feeds addressed by the 2008 Guidance are

[1] Commission Guidance on the Use of Company Web Sites, Release No. 34-58288 (Aug. 7, 2008) ("2008 Guidance").

used. Accordingly, the Commission deems it appropriate and in the public interest to issue this Report of Investigation ("Report") pursuant to Section 21(a) of the Exchange Act to provide guidance to issuers regarding how Regulation FD and the 2008 Guidance apply to disclosures made through social media channels.[2]

II. Background of Regulation FD and the 2008 Commission Guidance on the Use of Company Web Sites

Regulation FD provides that when an issuer, or a person acting on its behalf, discloses material, nonpublic information to securities market professionals or shareholders where it is reasonably foreseeable that they will trade on the basis of the information, it must distribute that information in a manner reasonably designed to achieve effective broad and non-exclusionary distribution to the public.[3] When the disclosure of material, nonpublic information is intentional, distribution of the same information to the public must be made simultaneously. When the disclosure of material, nonpublic information is inadvertent, distribution of the same information to the public must be made promptly afterwards. Regulation FD was adopted out of concern that issuers were selectively "disclosing important nonpublic information, such as advance warning of earnings results, to securities analysts or selected institutional investors before making full disclosure of the same information to the general public."[4] In our previous statements on Regulation FD, we have recognized that the "regulation does not require use of a particular method, or establish a 'one size fits all' standard for disclosure."[5] We did, however, "caution issuers that a deviation from their usual practices for making public disclosure may affect our judgment as to whether the method they have chosen in a particular case was reasonable."[6] We have since encouraged "honest, carefully considered attempts to comply with Regulation FD."[7]

In August 2008, in response to the changing electronic landscape of issuer disclosure and the wide-spread use of web sites to disseminate information electronically

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[2] Section 21(a) of the Exchange Act authorizes the Commission to investigate violations of the federal securities laws, and, in its discretion, "to publish information concerning any such violations." This Report does not constitute an adjudication of any fact or issue addressed herein. The facts discussed in Section III, *infra*, are matters of public record or based on documentary records.

[3] 17 C.F.R. § 243.100. Final Rule: Selective Disclosure and Insider Trading, Exchange Act, Release No. 34-43154, 65 Fed. Reg. 51,716 (Aug. 15, 2000) (the "Adopting Release"). Regulation FD applies generally to selective disclosures made to persons outside the issuer who are (1) a broker or dealer or persons associated with a broker or dealer, (2) an investment advisor or persons associated with an investment advisor, (3) an investment company or persons affiliated with an investment company, or (4) a holder of the issuer's securities under circumstances in which it is reasonably foreseeable that the person will trade in the issuer's securities on the basis of the information. 17 CFR § 243.100(b)(1).

[4] *Id*., at 51,716.

[5] *Id*., at 51,724.

[6] *Id*.

[7] Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: Motorola, Inc., Release No. 34-46898 (Nov. 25, 2002).

to investors and the market, the Commission issued its 2008 Guidance.[8] As the 2008 Guidance explained, the Commission has "long recognized the vital role of the Internet and electronic communications in modernizing the disclosure system under the federal securities laws and in promoting transparency, liquidity and efficiency in our trading markets."[9] Additionally, the guidance detailed the many steps we have taken over the years to encourage the dissemination of information electronically, "as we believe that widespread access to company information is a key component of our integrated disclosure scheme, the efficient functioning of the markets, and investor protection."[10]

The Commission has not explicitly addressed the application of Regulation FD and the 2008 Guidance to disclosures made through social media channels. The 2008 Guidance was directed primarily at the use of issuer web sites as a method of disseminating information in compliance with Regulation FD. Yet the guidance also contemplated other "push" technology forms of communication such as email alerts and RSS feeds, along with "interactive" communication tools such as blogs.[11] In light of the rapid "development and proliferation of company web sites since 2000" and with the expectation of "continued technological advances," the 2008 Guidance was designed to be flexible and adaptive.[12] Accordingly, the guidance provided issuers with a factor-based framework for analysis, rather than static rules applicable only to web sites.

As explained in the 2008 Guidance, "whether a company's web site is a recognized channel of distribution will depend on the steps that the company has taken to alert the market to its web site and its disclosure practices, as well as the use by investors and the market of the company's web site."[13] The guidance offered a non-exhaustive list of factors to be considered in evaluating whether a corporate web site constitutes a recognized channel of distribution.[14] The central focus of this inquiry is whether the company has made investors, the market, and the media aware of the channels of distribution it expects to use, so these parties know where to look for disclosures of material information about the company or what they need to do to be in a position to receive this information.

III. Facts

Netflix is an on-line entertainment service that provides movies and television programming to subscribers by streaming content through the internet and by distributing DVDs through the mail. Over the last two years, Netflix has stated that it is increasingly focused on expanding its internet streaming business.

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[8] 2008 Guidance, at 10.

[9] *Id.*, at 6.

[10] *Id.*, at 7.

[11] *Id.*, at 9 n.20, 21, & n.51.

[12] *Id.*, at 5.

[13] *Id.*, at 18-19.

[14] *Id.*, at 20-22.

On January 4, 2012, Netflix announced by press release that it had streamed two billion hours of content in the fourth quarter of 2011. Netflix also featured the two billion hours streaming metric in the opening paragraph of the January 25, 2012, letter to shareholders signed by Hastings that accompanied Netflix's quarterly financial results included in its earnings release, a copy of which was also furnished on EDGAR on a Current Report on Form 8-K. During Netflix's 2011 year-end and fourth quarter earnings conference call on January 25, 2012, Hastings was asked why this streaming metric was relevant (since Netflix's revenues are derived through fixed subscriber fees, not based on the number of hours of programming viewed). Hastings explained that streaming was "a measure of an engagement and scale in terms of the adoption of our service and use of our service. . . . . It [two billion hours streaming in a quarter] is a great milestone for us to have hit. And like I said, shows widespread adoption and usage of the service." He also stated that although he did not anticipate that Netflix would regularly report the number of hours of streamed content, Netflix would update the metric "on a milestone basis."

In an early June posting on Netflix's official blog, Netflix made a brief reference to people "enjoying nearly a billion hours per month of movies and TV shows from Netflix." The blog was technical in nature, announcing a new content delivery network available to Internet Service Providers, and there was no further detail given about the streaming metric. Beyond that, Netflix did not make any milestone announcements regarding streaming hours between January 25, 2012 and the beginning of July 2012.

On July 3, 2012, just before 11:00 a.m. Eastern time, Hastings posted the following message on his personal Facebook page:

> Congrats to Ted Sarados, and his amazing content licensing team. Netflix monthly viewing exceeded 1 billion hours for the first time ever in June. When House of Cards and Arrested Development debut, we'll blow these records away. Keep going, Ted, we need even more!

This announcement represented a nearly 50% increase in streaming hours from Netflix's January 25, 2012 announcement that it had streamed 2 billion hours over the preceding three-month quarter.

Prior to his post, Hastings did not receive input from Netflix's chief financial officer, the legal department, or investor relations department. Netflix did not file with or furnish to the Commission a Current Report on Form 8-K, issue a press release through its standard distribution channels, or otherwise announce the streaming milestone. Also on July 3, 2012, and after the Facebook post, Netflix issued a press release announcing the date of its second quarter 2012 earnings release but did not mention Hastings's Facebook post. Netflix's stock continued a rise that began when the market opened on July 3, increasing from $70.45 at the time of Hastings's Facebook post to $81.72 at the close of the following trading day.

The announcement of the streaming milestone reached the securities market incrementally. The post was picked up by a technology-focused blog about an hour later and by a handful of news outlets within two hours. Approximately an hour after the post, Netflix sent it to several reporters, but did not disseminate it to the broader mailing list normally used for corporate press releases. After the markets closed early at 1:00 p.m., several articles in the mainstream financial press picked up the story. Research analysts also wrote about the streaming milestone, describing the metric as a positive measure of customer engagement, indicative of a reduction in the rate Netflix is losing customers, or "churn," and possibly suggesting that quarterly subscriber numbers would be at the high end of guidance.[15]

Facebook members can subscribe to Hastings's Facebook page, which had over 200,000 subscribers at the time of the post, including equity research analysts associated with registered broker-dealers, shareholders, reporters, and bloggers. Neither Hastings nor Netflix had previously used Hastings's Facebook page to announce company metrics. Nor had they taken any steps to make the investing public aware that Hastings's personal Facebook page might be used as a medium for communicating information about Netflix. Instead, Netflix has consistently directed the public to its own Facebook page, Twitter feed, and blog and to its own web site for information about Netflix. In early December 2012, Hastings stated for the public record that "we [Netflix] don't currently use Facebook and other social media to get material information to investors; we usually get that information out in our extensive investor letters, press releases and SEC filings."

IV. Discussion

A fundamental question raised during the staff's investigation was the application of Regulation FD and the 2008 Guidance to issuer disclosures through rapidly changing forms of communication, including social media channels. We do not wish to inhibit the content, form, or forum of any such disclosure, and we are mindful of placing additional compliance burdens on issuers. In fact, we encourage companies to seek out new forms of communication to better connect with shareholders. We also remind issuers that the analysis of whether Regulation FD was violated is always a facts-and-circumstances analysis based on the specific context presented.

We take this opportunity to clarify and amplify two points. First, issuer communications through social media channels require careful Regulation FD analysis comparable to communications through more traditional channels. Second, the principles outlined in the 2008 Guidance — and specifically the concept that the investing public should be alerted to the channels of distribution a company will use to disseminate material information — apply with equal force to corporate disclosures made through social media channels.

[15] On July 24, 2012, after the close of market, Netflix announced its second quarter earnings, including quarterly subscriber numbers on the low end of guidance. The stock dropped from the previous day's close of $80.39 to $60.28 per share on July 25, 2012.

A. Disclosures Triggering Regulation FD

Regulation FD applies when an issuer discloses material, non-public information to certain enumerated persons, including shareholders and securities professionals.[16] It prohibits selective disclosure "[w]henever an issuer, or any person acting on its behalf, discloses any material nonpublic information regarding that issuer *to any person* described in paragraph (b)(1) of this section."[17] Although the Regulation FD Adopting Release highlights the Commission's special concerns about selective disclosure of information to favored analysts or investors, the identification of the enumerated persons within Regulation FD is inclusive, and the prohibition does not turn on an intent or motive of favoritism. Nor does the rule suggest that disclosure of material, non-public information to a broader group that includes both enumerated and non-enumerated persons but that still falls short of a public disclosure negates the applicability of Regulation FD. On the contrary, the rule makes clear that public disclosure of material, nonpublic information must be made in a manner that conforms with Regulation FD whenever such information is disclosed to any group that includes one or more enumerated persons.

Accordingly, we emphasize for issuers that all disclosures to groups that include an enumerated person should be analyzed for compliance with Regulation FD. Specifically, if an issuer makes a disclosure to an enumerated person, including to a broader group of recipients through a social media channel, the issuer must consider whether that disclosure implicates Regulation FD.[18] This would include determining whether the disclosure includes material, nonpublic information.[19] Further, if the issuer were to elect not to file a Form 8-K, the issuer would need to consider whether the information was being disseminated in a manner "reasonably designed to provide broad, non-exclusionary distribution of the information to the public."[20]

B. Broad, Non-Exclusionary Distribution of Information to the Public

Our 2008 Guidance was directed primarily at the use of corporate web sites for the disclosure of material, non-public information. Like web sites, corporate social media pages are created, populated, and updated by the issuer. The 2008 Guidance, furthermore, specifically identified "push" technologies, such as email alerts and RSS feeds and "interactive" communication tools, such as blogs, which could enable the automatic electronic dissemination of information to subscribers.[21] Today's evolving social media channels are an extension of these concepts, whereby information can be

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[16] *See supra* n.3.

[17] 17 CFR § 243.100(a) (emphasis added).

[18] We reiterate that nothing in Regulation FD is intended to interfere with "legitimate, ordinary-course business communications" or communications with the press. Adopting Release, 65 Fed. Reg. at 51,718.

[19] 17 CFR § 243.100(a).

[20] 17 CFR § 243.100(e)(1)-(2).

[21] *See supra* n.10.

disseminated to those with access. Thus, the 2008 Guidance continues to provide a relevant framework for applying Regulation FD to evolving social media channels of distribution.

Specifically, in light of the direct and immediate communication from issuers to investors that is now possible through social media channels, such as Facebook and Twitter, we expect issuers to examine rigorously the factors indicating whether a particular channel is a "recognized channel of distribution" for communicating with their investors.[22] We emphasize for issuers that the steps taken to alert the market about which forms of communication a company intends to use for the dissemination of material, non-public information, including the social media channels that may be used and the types of information that may be disclosed through these channels, are critical to the fair and efficient disclosure of information. Without such notice, the investing public would be forced to keep pace with a changing and expanding universe of potential disclosure channels, a virtually impossible task.

Providing appropriate notice to investors of the specific channels a company will use for the dissemination of material, nonpublic information is a sensible and expedient solution. It is not expected that this step would limit the channels of communication a company could use after appropriate notice or the opportunity for a company and investors to benefit from technological innovation and changes in communications practices. The 2008 Guidance encourages issuers to consider including in periodic reports and press releases the corporate web site address and disclosures that the company routinely posts important information on that web site. Similarly, disclosures on corporate web sites identifying the specific social media channels a company intends to use for the dissemination of material non-public information would give investors and the markets the opportunity to take the steps necessary to be in a position to receive important disclosures — e.g., subscribing, joining, registering, or reviewing that particular channel. These are some, but certainly not all, of the methods a company could use, with minimal burden, to enable evolving social media channels of corporate disclosure to be used as recognized channels of distribution in compliance with Regulation FD and the 2008 Guidance.

Although every case must be evaluated on its own facts, disclosure of material, nonpublic information on the personal social media site of an individual corporate officer, without advance notice to investors that the site may be used for this purpose, is unlikely to qualify as a method "reasonably designed to provide broad, non-exclusionary distribution of the information to the public" within the meaning of Regulation FD.[23] This is true even if the individual in question has a large number of subscribers, friends, or other social media contacts, such that the information is likely to reach a broader audience over time. Personal social media sites of individuals employed by a public company would not ordinarily be assumed to be channels through which the company would disclose material corporate information. Without adequate notice that such a site

[22] 2008 Guidance, at 20-22.

[23] 17 CFR § 243.101(e)(2).

may be used for this purpose, investors would not have an opportunity to access this information or, in some cases, would not know of that opportunity, at the same time as other investors.

V. Conclusion

There has been a rapid proliferation of social media channels for corporate communication since the issuance of the Commission's 2008 Guidance. An increasing number of public companies are using social media to communicate with their shareholders and the investing public. We appreciate the value and prevalence of social media channels in contemporary market communications, and the Commission supports companies seeking new ways to communicate and engage with shareholders and the market. This Report is not aimed at inhibiting corporate communication through evolving social media channels. To the contrary, we seek to remind issuers that disclosures to persons enumerated in Regulation FD, even if made through evolving social media channels, must still be analyzed for compliance with Regulation FD. Moreover, we emphasize that the Commission's 2008 Guidance, though largely focused on the use of web sites, is equally applicable to current and evolving social media channels of corporate communication. The 2008 Guidance explained that issuers must take steps sufficient to alert investors and the market to the channels it will use for the dissemination of material, nonpublic information. We believe that adherence to this guidance will help, with minimal burden, to assure compliance with Regulation FD and the fair and efficient operation of the market.

By the Commission.