

Tesla, Twitter, and the Good Weed

Insights

December 10, 2018

Originally published by: Harvard Law School Forum on Corporate Governance and Financial Regulation

By: Joe Green, Justin Slane and Sharon Makower

Perhaps no company in the world has the perception of its brand being tied to one person more than Tesla Inc. (Tesla) and its CEO and now former chairman of the board, Elon Musk. As at least one journalist phrased it, “**Elon Musk is Tesla. Tesla is Elon Musk.**” And Musk is not just the face of Tesla, but a co-founder of PayPal and Solar City, the founder and current CEO of SpaceX and founder of its subsidiary, The Boring Company. He has crafted a “**real-life Iron Man**” persona, including all the eccentricity, and is undoubtedly one of the most recognizable and polarizing CEOs in the world.

But 2018 has not been the best year for Elon Musk. In what Musk would call negative propaganda pushed by short sellers, Tesla has faced heightened scrutiny and increasingly negative media attention related to a litany of issues, including **cash burn**, **vehicle safety**, **production capabilities**, and a string of **employment-related lawsuits** and **executive exits (only made worse recently)**. Analysts and investors began to publicly cool on Tesla and question its long-term value, which Musk also **attributed to short sellers**.

In May, citing independence concerns and questioning whether Musk may be stretched too thin, proxy advisory giants Glass, Lewis & Company (Glass Lewis) and Institutional Shareholder Services, Inc. (ISS) opposed the re-election of current Tesla board members and supported splitting Musk’s roles as CEO and chairman.

As the pressure mounted, Musk became increasingly combative, especially on Twitter, lashing out at short sellers and anyone criticizing Tesla or him. Musk’s erratic behavior and obsession with short sellers and critics drew more criticism of **his leadership and that of Tesla’s board of directors**.

But it all came to a head on August 7, when in the middle of the trading day, without notice or warning to anyone (including other executives and directors at Tesla or contacts at Nasdaq, the exchange on which Tesla's common stock is listed), Musk tweeted:



Then, for reasons still unknown, nobody took his phone away, and Musk continued tweeting and interacting with shareholders throughout the day:





The public reaction to Musk's tweets was strong and immediate. Tesla's stock soared before Nasdaq eventually halted trading for several hours later in the day, and there was instant speculation about whether Musk actually had the funding to take Tesla private (spoiler: he did not).

Musk's drastic departure from normal public disclosure standards and the subsequent media circus arising from it unsurprisingly captured the attention of the Securities and Exchange Commission (SEC), which ultimately resulted in an **enforcement action and settlement** with Elon Musk over the tweets. Tesla also settled with the SEC. The end results of the settlements include the following:

- Musk must step down as chairman of the board and be replaced by an independent chairman, but Musk will be allowed to remain as CEO. On November 7, 2018, Tesla **appointed** an independent chairman.
- Musk and Tesla must each pay \$20 million in fines.
- Tesla must add two independent directors and create a formal disclosure committee to oversee communications from Musk.
- Tesla must hire an experienced securities lawyer, subject to approval by the SEC Division of Enforcement (Tesla's current general counsel was **Elon Musk's divorce attorney and worked primarily in family law** before joining Tesla).

This post examines this corporate governance cautionary tale, focusing primarily on the Regulation FD (Reg FD) issues raised by Musk's tweets and public statements. The full article from which this post is excerpted also examines a host of other issues including disclosure controls and procedures, stock exchange requirements, conflicts of interest, board independence, and more, highlighting for each issue where things went wrong and

identifying resources that perhaps could have helped avoid this type of mess. To learn more about these issues, the full article can be accessed [here](#).

Complying with Regulation FD

Much of the initial reporting surrounding Musk's tweets questioned whether the use of his personal Twitter account violated Reg FD. Reg FD, which took effect in 2000, prohibits selective disclosure by requiring that material nonpublic information disclosed to securityholders or market professionals (including research analysts) must also be disclosed to the public in a broad, non-exclusionary manner. And in fact, in finally answering why he tweeted about taking Tesla private, Musk explained in an August 13 blog post that he wanted to have discussions with key shareholders and he felt it "wouldn't be right to share information about going private with just [Tesla's] largest investors." While Musk's intentions are noble and in line with the basic principle of nearly 20-year-old federal securities law, the reports were correct that Reg FD generally requires more than tweets.

SEC guidance issued in 2008 and 2013 regarding the use of company websites and social media for disclosure suggests that companies can still satisfy Reg FD requirements if they notify investors of where they can expect material information to be disclosed online, making it a "recognized channel of distribution." In particular, the 2013 guidance dealt with the Netflix CEO disclosing monthly viewing hours on his personal Facebook page.

The SEC stated that disclosing 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 satisfy Regulation FD because it is not likely a method "reasonably designed to provide broad, non-exclusionary distribution of the information to the public" that Reg FD requires. The SEC stated this is true even if "the individual in question has a large number of subscribers, friends or other social media contacts, so that the information is likely to reach a broader audience over time."

The SEC used its 2013 guidance to highlight the concept that whether a Regulation FD violation occurred will turn on whether the investing public was alerted to the channels of distribution a company will use to disseminate material information. The SEC's 2008 guidance on the use of company websites outlines the factors that indicate whether a particular channel (whether it be a corporate website or a corporate executive's social media account) is a recognized channel of distribution for communicating with investors.

In this case, Tesla and Musk had a few factors in their favor:

- A [Form 8-K filed on November 5, 2013](#), encourages investors to follow Elon Musk's personal Twitter account for material information being disclosed to the public. Ideally the notice would be repeated, including in Tesla's annual reports on Form 10-K or additional Form 8-K reports, but at least some form of notice was provided to shareholders.
- Elon Musk also has nearly 23 million Twitter followers. His original tweet was widely picked up and further broadcast by major news sources within minutes, and within hours, former

SEC Chairman Harvey Pitt was on major cable news networks discussing whether Musk committed securities fraud.

While it was far from a safe use of social media for Reg FD purposes, Musk and Tesla appear to have a decent argument that shareholders had notice that information could be disclosed through Musk's personal Twitter account and his account was reasonably designed to provide broad, non-exclusionary disclosure of the information.

Most public companies typically adopt formal policies regarding compliance with Reg FD (as well as the use of social media by their employees and executives). A strong Reg FD policy should contain:

- A complete outline of the procedures and practices of the company concerning disclosure of information to the public.
- A formal limitation on which company personnel are permitted to communicate with analysts and securityholders on behalf of the company. These people should be well-versed in Reg FD and familiar with the company's public disclosures. Ideally these people should also understand the concept of materiality and what may constitute securities fraud under Rule 10b-5.
- A restatement of the company's policy on confidentiality of information.
- A guide to disclosing material information.

Companies should also address the use of social media by their employees and executives, whether in their Reg FD policies or in separate social media guidelines that cover both personal social media use and social media use as an authorized company spokesperson.

While a Tesla Reg FD policy, set of social media guidelines, or other corporate communications policy addressing these concerns does not seem to be publicly available, the Tesla Code of Business Conduct and Ethics (last revised in December 2017) refers to a "Communication Policy ... [that covers] Tesla's social media guidelines, media relations and marketing guidelines, and the circumstances and the extent to which individuals are allowed to speak on Tesla's behalf." Musk should have been aware of Tesla's communications policy, ideally having been reminded frequently through regular training for Tesla officers regarding the company's policy and their obligations under Regulation FD, and never tweeted to begin with.

Twitter Was Always a Bad Choice

Musk's tweets are also an extreme, yet useful, example of why casual social media use and disclosure of material nonpublic information should not be mixed. Section 10(b) of the Exchange Act prohibits material misstatements and omissions of fact, and companies must always avoid making disclosures in informal social media posts that lack material information or the context necessary for investors to be fully informed. If a company decides that there is

material information that should be disclosed to the public, it must then determine when that information must be disclosed. Information should only be disclosed when it is definitive, accurate, clear, and specific.

Twitter can be an excellent tool for supplementing more formal corporate disclosure, such as linking to SEC filings, the company's website, or attaching a press release as an image. However, individual Twitter posts as the sole medium of disclosure might be the worst form of social media use for disclosing material nonpublic information. The primary differentiating factor between Twitter and other social media platforms is it limits user posts to just 280 characters. Musk used 61 characters in his original going private tweet (if you pro rate his \$20 million SEC fine to the characters in that tweet, Musk spent over \$2.6 million on spaces alone). While some may applaud his succinctness, Musk's August 7 tweets and blog post are textbook examples of public disclosures that lack context and completeness.

What does "funding secured" and "investor support is confirmed" mean? Who is/are the buyer(s)? How was the \$420 per share price calculated? Has the board received or approved a proposal? None of these basic questions had answers. We later learned in the SEC's civil complaint against Musk:

- A Tesla investor texted Musk's chief of staff "What's Elon's tweet about? Can't make any sense of it..."
- A reporter emailed Musk to ask if his tweet was a 420 joke and whether "an actual explanation" was coming.
- The following investor relations exchange happened in real life seven hours, ten tweets, and one blog post after Musk's initial "going private" tweet:

"After Tesla's head of Investor Relations received another inquiry from another investment bank research analyst at approximately 7:20 PM EDT, he asked whether the analyst had read Tesla's 'official blog post on this topic.' The analyst responded, 'I did. Nothing on funding though?' The head of Investor Relations replied, 'The very first tweet simply mentioned 'Funding secured' which means there is a firm offer. Elon did not disclose details of who the buyer is.' The analyst then asked, 'Firm offer means there is a commitment letter or is this a verbal agreement?' The head of Investor Relations responded, 'I actually don't know, but I would assume that given we went full-on public with this, the offer is as firm as it gets.'" (see [SEC Complaint, par. 52.](#))

It took six full days before Musk or Tesla provided any clarification about what Musk meant by "funding secured" and the rest of his going private tweets on August 7.

Corporate Disclosure or Personal Statements?

Musk's claim he was making statements in his personal capacity as a potential buyer of Tesla as opposed to on Tesla's behalf as CEO and Chairman adds another element to this case illustrating why disclosure of material nonpublic information requires full context. If his

personal Twitter account is both a recognized channel for corporate communications and a means for him to make disclosures as a private individual, how are investors supposed to know what is corporate information and what is personal?

Nothing in the August 7 tweets or blog post definitively stated Musk was not speaking on behalf of Tesla as its CEO and Chairman. In fact, in the investor relations exchange mentioned above, Tesla's head of Investor Relations says "... I would assume that given **we** went full-on public with this..." (emphasis added), phrasing that certainly implies he thought the statements were made on Tesla's behalf.

It is generally good corporate governance practice that if a company discovers a Reg FD violation, to minimize risks, it should promptly disclose the information by a Reg FD-compliant method. For example, if an executive officer selectively discloses material nonpublic information, the company can correct the situation by filing a Form 8-K to disclose the information.

Given the potential confusion for investors resulting from Musk's initial tweets and his claim that he made the statements in his "personal capacity," Tesla should have immediately filed a Form 8-K (which also happens to allow for more than 280 characters) to correct any potentially selective or misleading disclosure made by Musk and provide any additional context necessary. No Form 8-K was filed though. Again, it was six days before Musk or Tesla provided any clarification or additional explanation for his statements on August 7.

The SEC Settlement and Ongoing Fallout

The ultimate fallout from Musk's brief foray into a possible going private transaction is still ongoing:

- Class action lawsuits are still pending.
- The Department of Justice is still investigating Musk's tweets.
- Significant investors are **engaging with** Tesla requesting changes to the board of directors (and other corporate governance practices).

Musk doesn't seem to be fazed by any of this, and could do something tomorrow that turns this all on its head again. But the SEC settlement with Musk has now been approved by the Southern District of New York, and Tesla has settled separately with the SEC without a formal enforcement action. The terms of the settlements bring us full circle to where the year started, with the recognition that Tesla was facing an increasing battle between responsible corporate governance and Elon Musk's persona. Tesla lost this round. If the added disclosure controls and expanded board continues losing battles, well, who knows? There is always **Teslaquilla** (or **maybe not**)!

Related People



Joe Green

OF COUNSEL & CHIEF INNOVATION OFFICER

P +1 212 430 3136

Featured Insights

FIRM NEWS

Gunderson Dettmer Commemorates 2025 Asian American and Pacific Islander Heritage (AAPI) Month

CLIENT NEWS

Brazilian Carbon Capture Company Mombak Announces \$30M Financing

CLIENT NEWS

Africa B2B OmniRetail Announces \$20M Financing

CLIENT NEWS

Glacier Announces Series A Financing to Expand Robot Recycling Fleet

CLIENT NEWS

Dataminr Announces \$100M Investment Led by Fortress Investment Group

CLIENT NEWS

Omnidian Announces \$87M Series C for Renewable Energy Performance

INSIGHTS

Splitting the Pie: How Savvy Founders Divide Ownership and Navigate Other Founder Equity Decisions

CLIENT NEWS

Chainguard Announces \$356 Million Series D Led by Kleiner Perkins and IVP

INSIGHTS

Client Insight: California AI Transparency Act

INSIGHTS

Client Insight: Prepare for BE-10 Benchmark Survey of US Direct Investment Abroad

INSIGHTS

Tech Brew Interviews Aaron Rubin in “Where the legal battle stands around copyright and AI training”

CLIENT NEWS

Latin America Fintech Belvo Announces \$15M Funding