

SEC settles with IBM for misleading statements regarding stock option expenses

The SEC recently settled an enforcement action against IBM in connection with statements made by IBM during an April 5, 2005 webcast with analysts and later included in a Form 8-K filed with the SEC. The settlement emphasizes the importance of evaluating the total mix of information in presenting clear, accurate and complete information to investors and analysts.

The SEC found that information presented by IBM relating to IBM's decision to expense employee stock options was materially misleading because it created the impression that IBM's stock options expense in fiscal 2005 would be greater than what IBM actually expected it to be. The SEC believed that IBM did not disclose its expected stock options expense because it was concerned that analysts would add back to their EPS estimates any year-to-year reduction in the employee stock options expense instead of using the reduction to offset an unrelated increased pension expense.

As a result, the SEC found that IBM violated Section 13(a) of the Exchange Act and Exchange Act Rules 12b-20 and 13a-11 by filing a materially misleading Form 8-K and ordered IBM to cease and desist from committing or causing any violations and any future violations of these securities laws. No fines or penalties were assessed.

The necessity to present clear, accurate and complete information to investors is reflected by the SEC's order, in which the SEC seemed particularly troubled by two findings. First, IBM's management had formed internal estimates on its 2005 stock option expenses but chose not to disclose these amounts. Second, the SEC believed that IBM's management intended to have analysts conflate the stock options expense with the pension expense, hoping to guide such analysts to set lower growth rates that would have been achievable notwithstanding the increased pension expense.

The SEC's order highlights the importance of evaluating the total mix of information presented to investors and analysts, both what is and is not disclosed. IBM's announced purpose for the disclosure was to allow its investors and analysts to update their financial models to reflect the new reporting basis. The SEC indicated in its press release that disclosures regarding financial results are among the most important factors considered by investors in evaluating a company. Therefore, in presenting such information to investors, it is essential that the information be clear, accurate and complete.

The SEC has posted the order [here](#) and its accompanying press release [here](#). If you would like to learn more about the order and its implications, please contact your usual legal advisor at Ropes & Gray.

