

Bank Settles Action under Regulation FD

On November 22, 2011, the SEC announced a settlement with Fifth Third Bancorp over allegations that, in violation of Regulation FD, it selectively disclosed its decision to redeem a class of trust preferred securities. Based in part on the bank's cooperation, the SEC obtained only a cease-and-desist order and did not impose a civil penalty.

As a result of changes in the capital treatment of trust preferred securities, the bank elected to redeem the securities in advance of what otherwise would have been the first optional call date. After receiving the necessary approval from the Federal Reserve Bank of Cleveland, the bank was required to instruct the trustee to provide notice to the holders at least 30 days in advance of the redemption date. The governing trust instrument required only that notice be provided to the Depository Trust Company (DTC) as the sole registered holder of the securities. At the time the bank made its decision to redeem, the securities were trading at a premium to the redemption price (\$26.50 vs. \$25.18).

On May 16th, the bank instructed the trustee to redeem the securities and send the required notice to DTC. DTC informed the beneficial owners of the securities by posting the redemption notice in the early morning hours of May 17th on its Legal Notification System (LENS).¹ Apparently the posting did not affect the trading price on that day. On May 18th, however, the securities opened at \$26.66 but closed that day at \$25.20. Volume increased from a daily average of 38,000 shares to over 2 million. During that day, apparently in response to investor calls and the trading activity, the bank disclosed the redemption by filing a Form 8-K.

The SEC order states that although the bank knew that the securities were trading at a premium to the redemption price and that holders would be "very interested" in the redemption, it failed to issue a Form 8-K or other public notice of the redemption.

It is not hard to imagine that the bank thought it needed simply to follow the procedures outlined in the declaration of trust for redeeming the securities. That was not the SEC's view, and this enforcement action ensued. The key takeaways here are:

- **Compliance with a security's governing documents may not be sufficient to comply with Regulation FD.** Even a redemption notice sent to all holders of a series of securities may not be adequate; in general, disclosure to "the investing public" is required.
- **Information disseminated by the Trustee and DTC was "on behalf of" the issuer.** The SEC order characterizes the bank's actions as having disclosed information "through the Trustee and DTC, but not initially to the public . . ." The SEC necessarily took that position because Regulation FD only applies to communication made by an issuer or "any person acting on its behalf . . ." It might have come as a surprise to the bank that DTC was its agent for these purposes.
- **If material information is being disclosed to anyone, follow the chain of dissemination.** The bank got caught here for failing to think through exactly how the information about the redemption was to be disseminated to the market. At least for Regulation FD purposes, it appears that the SEC believes that the issuer is responsible for making sure that communications by other entities in the process are FD-compliant.

¹ The LENS system is a library of notices that are published and made available to DTC member banks, brokers and non-member subscribers, who may elect to receive customized e-mail alerts.

The SEC has obtained civil penalties in other FD enforcement actions, and the fact that they did not here suggests it believed the bank's conduct was neither intentional nor egregious. It does serve as a reminder to issuers, however, that when disclosing material information to anyone it is important to consider carefully all the ways in which that information may be disseminated and to make sure it is disclosed to the investing public in general.

Please contact your usual Ropes & Gray adviser with any additional questions about Regulation FD issues.