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September 16, 2003

SEC Continues to Pursue Regulation FD Violators

Summary

As a result of all the corporate governance initiatives resulting from the high profile corporate scandals of the past few years, Regulation FD has to some extent been forgotten. Last week, the SEC gave a strong reminder that corporate managers act at their own personal peril if they ignore the requirements of Reg FD. Simultaneously with the SEC's filing of charges against Schering-Plough Corporation and its former Chief Executive Officer, Richard J. Kogan, for violating the disclosure requirements of Reg FD and Section 13(a) of the Securities Exchange Act of 1934, the defendants entered into a settlement agreement with the SEC in which they agreed to cease and desist from any future violations. In addition, Schering agreed to pay a penalty of \$1,000,000 and Kogan personally agreed to pay a penalty of \$50,000. In the case of Schering, this will be the largest penalty obtained by the SEC for a violation of Reg FD and, in the case of Kogan, the first penalty obtained from an individual in cases involving selective disclosure.

Facts

According to the SEC's complaint, in late September 2002, Kogan became aware of internal forecasts that projected Schering's earnings below estimates for the quarter and the full year as well as prior earnings guidance. Soon thereafter, Kogan and Schering's senior vice president of investor relations held meetings with four institutional investors, three of whom were Schering's largest investors. During these meetings, Kogan remarked that Schering was going to take a "hard hit" to earnings; that he did not favor Schering buying back its shares (prior statements indicated that the company had not taken a position on whether to buy back its shares); that the street had not sufficiently lowered earnings estimates; and that the coming year would be a difficult one for the company. In addition, participants in these meetings inferred from Kogan's tone and demeanor that things were not good for Schering.

Immediately after these meetings Schering's stock price fell 17% with volume at 4 times the stock's typical daily volume.

Subsequently, according to the SEC's complaint, in early October Schering held a meeting with analysts and portfolio managers at Schering's offices. The meeting was not accessible to the general public or the media. During the meeting, Kogan said that the coming

year would be tough for Schering and earnings would be “terrible.” In response to inquiries at the meeting, Schering later issued a press release which in part provided earnings guidance that was materially below analysts’ estimates and the company’s own earlier guidance.

Regulation FD and the Settlement

Reg FD prohibits public companies from selectively disclosing material, nonpublic information to certain persons outside the company, including institutional investors, securities analysts, and other securities professionals. When disclosure is made “intentionally” simultaneous disclosure to the public must occur. When disclosure is made “unintentionally” disclosure must be made “promptly” (as soon as reasonably practicable but in no event after the later of 24 hours or the commencement of the next day’s trading on the principal exchange on which the company's stock is listed). The rule governs the disclosure of material information whether that information is communicated expressly or through indirect or implied communication.

The SEC asserted that Schering violated Reg FD and the Exchange Act, and Kogan caused such violations, by providing guidance that included material, nonpublic information and earnings during private meetings with institutional investors and analysts and by failing to make a public disclosure of the information as required by Reg FD. Kogan’s statements, general expressions of concern, tone and demeanor during private meetings were selective disclosure and the result was a significant sell off of Schering stock.

The Result

The result is a strong reminder of the obligation a company has to comply with Reg FD and the Exchange Act. By this action, the SEC has indicated that it will not tolerate selective disclosure. The company and its officers may be held accountable.

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The information in this Alert is intended for general information purposes only and should not be considered legal advice or opinion on any specific facts or circumstances. You are urged to contact a professional advisor concerning any specific question you may have relating to your own situation.

If you would like additional information about this case or to discuss Reg FD or any of the matters presented in this Alert you may contact:

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