

Practice Update

SEC Enforcement Brings Covid-related Disclosure Case

December 10, 2020

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Last week the Securities and Exchange Commission (SEC) filed its first case related to misleading COVID-19 disclosures. In a settled administrative order, the SEC found that disclosures in two press releases by [The Cheesecake Factory Incorporated](#) violated Section 13(a) of the Exchange Act and Rules 13a-11 and 12b-20 thereunder. Without admitting the findings in the order, the company agreed to pay a \$125,000 penalty and to cease-and-desist from further violations.

The SEC found that a number of Form 8-Ks filed by the Company were materially misleading. Specifically, the SEC found that the SEC's March 23 and April 3 disclosures failed to disclose: (1) a March 18, 2020 letter from the company to its restaurants' landlords stating that it was not going to pay its rent for April 2020; (2) that the Company was losing \$6 million in cash per week; (3) that it had only approximately 16 weeks of cash remaining even after drawing down its \$90 million revolving credit facility; and (4) that it was excluding expenses attributable to corporate operations from its claim of sustainability.

While this is the first enforcement action against a public company based on disclosures about the financial effects of the pandemic, there are two interesting observations from the SEC's action:

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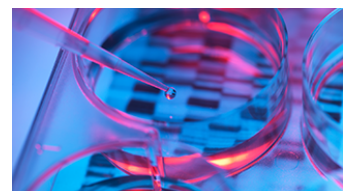
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- The SEC's order focuses on two press releases included as exhibits in Form 8-Ks that are deemed to be "furnished," and not "filed," under the Exchange Act. Specifically, one was filed under Item 7.01 and the other under Item 2.02. While "furnishing" reports violations generally may result in lower liability exposure because of the lack of a private cause of action under Section 13, it does not mean that the SEC cannot take enforcement action.
- The language at issue in the two Form 8-Ks was "sustainably," as in "operating sustainably." The concept of sustainability is generally thought to encompass the concept of over the long- or longer term; therefore, it is not clear what was materially misleading. However, it is important to note that the company remains in business and its stock price is near a 52 week high.

In addition to the observations, there are a few lessons to be learned from the enforcement action:

- The use of the word "sustainably" without further qualification or explanation can put an issuer at risk of an enforcement action. What is sustainably meant to reflect? Over what period of time?
- Where the subject matter involves the impact of Covid, the SEC's order demonstrates that it may be willing - in the context of Covid-related disclosures - to take action even if the disclosure is vague or unclear. This enforcement action raises the question of whether Covid-related disclosures are attracting greater scrutiny than other corporate disclosures in the current climate.
- Why did the SEC bring this action? It appears that the SEC brought this action to underscore the importance of carefully drafted Covid-related disclosures with respect to the impact of Covid on results of operations, financial condition, and liquidity, and to signal its willingness to take action if issuers' Covid-related disclosures are not carefully drafted. The SEC brought this action as a statement case.

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