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News Leak Probe May Chill Media's Use Of Federal Data

By **Erin Coe**

Law360, San Diego (January 29, 2013, 11:29 PM ET) -- A recent investigation into whether Dow Jones & Co. and other media companies facilitated insider trading by prematurely releasing market-sensitive government information points to aggressive use of insider trading laws by prosecutors, a development experts say could chill lawful use of such data by news organizations and firms.

Federal law enforcement officials were looking into whether Dow Jones, Bloomberg LP, Thomson Reuters Corp. and other companies had used high-speed transmission systems to give traders access to economic information a split second before the official release time, a source familiar with the investigation confirmed. They decided not to pursue any criminal charges related to the probe, first reported by The Wall Street Journal on Monday.

Authorities had opened the investigation after noticing trends that indicated some traders had obtained the data a little before the official release time, but didn't bring charges because they were not able to connect the trading patterns to specific activities by the media firms, the source confirmed. Officials plan to close the investigation over the next month, the source said.

The FBI and the U.S. Securities and Exchange Commission scrutinized several agencies that release economic data, including the Commerce, Labor, Energy, Agriculture and Treasury departments and the Federal Reserve, according to the source. These agencies have so-called data lockup rooms, facilities where economic information, such as federal job data, is first made available to news reporters and later officially released to the public. Under the lockup system, an agency controls a switch for all media communications lines, and reporters are blocked from releasing the information until the agency lifts the embargo.

Insider trading generally involves an insider's disclosure of information that is unavailable to the market. But once media companies disseminate the economic information they get from the government, it enters the market and can no longer be considered insider information, according to Miller & Chevalier Chtd. member Barry Pollack.

“Putting aside the grave First Amendment concerns of investigating media companies for publishing truthful information, the investigation is stretching insider trading laws far beyond where they were ever intended to go,” he said. “As much as it wants to, the government can’t control the dissemination of all information. The fact that the media publishes a nanosecond before the official release time is competition, not insider trading.”

Insider trading liability requires that a party traded on the basis of nonpublic information. It would be troubling if the government were to treat the information made available to members of the media as nonpublic if they disseminated it slightly before the official release time, according to Bass Berry & Sims PLC member Eli Richardson.

“It would be pushing the bounds of nonpublic information too far,” he said.

The investigation could make media companies and businesses that use the economic data more gun-shy about how they handle the information, according to experts.

“Even though the government is closing the investigation, it could have a chilling effect on media companies,” Pollack said. “It could cause them to be concerned that if they publish legitimate market information an instant before a competitor, they could be accused of somehow facilitating insider trading.”

The probe could also have a chilling effect on businesses whose stock trades are based on access to rapidly developing economic information released by media companies, Richardson said.

“This kind of investigation might cause some businesses to be overly cautious of their trading activities for fear the government is going to say after the fact that the information is not public,” he said.

Additionally, it could spur calls to regulate the premature release of economic data, experts say.

“Investor confidence in the market is dependent on material information being evenly available, and the market itself needs to correct any imbalance such practices may create,” Morgan Lewis & Bockius LLP partner George Terwilliger III said. “But I hope that we would recognize that overregulation is ... costly and stifles growth.”

But potential reforms could face resistance from news organizations, according to Pollack.

“I think there could be pushback, primarily from media companies that are concerned about the government trying to tell them when and how they can publish truthful and accurate information,” he said. “That is something the First Amendment is supposed to preclude.”

News of the investigation comes after Netflix Inc. disclosed in December that the SEC was threatening to bring a civil fraud action against the company and CEO Reed Hastings over his July Facebook post revealing that Netflix members had watched more than 1 billion hours that month. The company’s stock price jumped shortly thereafter.

“We have a seemingly endless stream of new technologies and new factual scenarios that could raise insider-trading issues in the SEC’s mind,” Richardson said. “But what we have that is not new are the essential elements that define the crime of insider trading. I would hope that the SEC always keeps these elements firmly in mind when confronted with new circumstances that someone may wish to deem ‘insider trading.’”

The government should continue to be cautious about handling economic information, but it needs to understand that it loses control of that information once the data is released, according to Pollack.

“With modern media and technology, it’s unrealistic for the government to think it can exercise control of the information once it’s released,” he said.

As part of the investigation, authorities also looked into whether smaller news outlets with access to the economic information might have served as extensions of trading firms, according to the WSJ. Besides examining each media firm as a whole, they also investigated whether any employees or contractors had violated any rules, according to the publication.

Investigators last summer asked Bloomberg to hand over one of its computers at the Department of Commerce, and Bloomberg complied with the request, according to the report.

Ty Trippet, a Bloomberg spokesman, said the company had discovered a flaw in the Department of Commerce's lockup system during a testing period sponsored by the agency.

"We alerted Commerce to this flaw when we saw it had potential to be exploited by others to beat their embargo during an actual lockup," he said. "We suggested solutions to secure their system, and they thanked us for alerting them to the issue."

Dow Jones spokeswoman Paula Keve said the company had not been contacted by the government regarding a criminal investigation.

"Dow Jones always endeavors to follow all lockup procedures and rules and would never sanction any intentional violation," she said. "Over the course of handling thousands of embargoes during the past several years, Dow Jones is not aware of violating an embargo on any major piece of economic data."

Barb Burg, a Thomson Reuters spokeswoman, said the company was unaware of any investigation or request for any of its equipment to be turned over for examination.

--Editing by Kat Laskowski and Elizabeth Bowen.

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