

**SEPTEMBER 28, 2021**

For more information,
contact:

Dixie Johnson
+1 202 626 8984
djohnson@kslaw.com

Amanda Sonneborn
+1 312 764 6940
asonneborn@kslaw.com

Keith Townsend
+1 404 572 3517
ktownsend@kslaw.com

King & Spalding

Washington, D.C.
1700 Pennsylvania Avenue,
NW
Washington, D.C. 20006-
4707
Tel: +1 202 737 0500

SEC Enforcement of Human Capital Disclosures: The First Fingerprints

INTRODUCTION

In a September 21, 2021 press release, Activision Blizzard confirmed that the SEC Enforcement Division issued a subpoena “to the Company and several current and former employees and executives regarding disclosures on employment matters and related issues.” This subpoena is part of an SEC investigation into Activision Blizzard’s human capital disclosures. Activision Blizzard stated that “The Company is confident in its prior disclosures and is cooperating with the SEC’s investigation.” These statements were part of a broader description in the press release of how the company “continues to work with regulators to resolve and address workplace issues.”¹

Activision Blizzard’s revelation about the SEC investigation came shortly after The Washington Post,² The Wall Street Journal³ and others (the “news reports”) reported on September 20, 2021, that the company is under federal and state investigation for its workplace practices, including allegations of sexual misconduct and workplace discrimination. Those and other articles detail a loud drumbeat of legal and personnel actions.⁴

Although this appears to be the first company to announce SEC Enforcement review of its human capital disclosures, it will not be the last. New disclosure rules, an aggressive Commission, and Enforcement Staff members who are focused on ESG generally, and human capital issues (the “Social” in “Environmental, Social, and Governance”) specifically, form the perfect environment for additional human capital investigations. Companies should consider now how to ensure that their disclosures will hold up well under close inspection, because the scrutiny is here.

WHY THE SEC’S ENFORCEMENT DIVISION IS INVESTIGATING HUMAN CAPITAL ISSUES

At first blush, it may seem odd that the SEC is investigating alleged workplace discrimination and misconduct, especially given the other



federal and state agencies that typically regulate these issues. But the Enforcement Division's actions should not be a surprise.

On August 26, 2020, under former Chairman Jay Clayton, the SEC revised its Regulation S-K disclosure requirements, including by revising Item 101(c) to "include, as a disclosure topic, a description of the registrant's human capital resources to the extent such disclosures would be material to an understanding of the registrant's business".⁵ Those rules became effective November 9, 2020. Companies then filed their first human capital disclosures in 2021. This initiative continued under current Chairman Gary Gensler, as he loudly broadcasted his view that investors care about human capital issues and therefore the issues may be material under the federal securities laws.⁶

Further narrowing the focus on human capital, the SEC Division of Corporation Finance also started to release information about its reviews of public company filings regarding ESG issues.⁷ Our firm's Global Human Capital and SEC Enforcement working group has been monitoring related events for some time, and now we're seeing the full picture emerge.

WHAT ENFORCEMENT IS ASKING FOR, AND WHY

In its Form 10-K for the year ending December 31, 2020 (filed February 23, 2021), Activision included more than a full page of disclosures under the heading Human Capital, with statements including, "We remain committed to building and sustaining a culture of belonging, built on equitable processes and systems, where everyone thrives" and:

We are party to routine claims, suits, investigations, audits, and other proceedings arising in the ordinary course of business, including with respect to intellectual property, competition and antitrust matters, regulatory matters, tax matters, privacy matters, labor and employment matters, compliance matters, unclaimed property matters, liability and personal injury claims, product damage claims, collection matters, and/or commercial claims. In the opinion of management, after consultation with legal counsel, such routine claims and lawsuits are not significant and we do not expect them to have a material adverse effect on our business, financial condition, results of operations, or liquidity.

During the SEC Enforcement investigation, these and other public statements by the company and its executives will be tested against internal statements they made to each other in real time. The public statements also will be evaluated against the impact on the market from subsequent disclosures of government and civil lawsuits.

In fact, the Wall Street Journal reported that the SEC already has requested documents "including minutes from Activision board meetings since 2019, personnel files of six former employees and separation agreements the company has reached this year with staffers," as well as asking for "communications [longtime Chief Executive Bobby Kotick had] with other senior executives regarding complaints of sexual harassment or discrimination by Activision employees or contractors."

If accurately reported, these requests would be consistent, in our experience, with situations in which the SEC's Enforcement Division investigates whether a company's public statements accurately reflected what was going on in the company at the time the disclosures were made. That's a traditional disclosure analysis. The requests also would be consistent with the intrusive nature of SEC investigations when it is necessary to understand personal activities to evaluate whether a securities law violation has occurred, such as in insider trading investigations. Personal lives become part of the federal record.



WHY ACTIVISION BLIZZARD DISCLOSED THE SEC INVESTIGATION

In most companies, the mere existence of an SEC investigation is generally not a required disclosure event. No line item expressly requires “real time” disclosure of an SEC investigation, so companies typically evaluate whether the investigation is required to be disclosed as material to their operations in the context of their periodic reports.⁸ Factors considered in a materiality analysis may include how fundamental the investigation could be to the operations of the company, and whether the expenses arising from responding to the inquiry are expected to be material to the Company’s results of operations. Even taking these factors into consideration, often companies determine that disclosure is not required.

Although this may seem odd to some, SEC investigations can be initiated based solely on “official curiosity,” and the SEC is constantly confirming in its public statements and private correspondence that the existence of an investigation does not mean that the SEC or its staff has formulated any views as to whether any conduct has violated the law.⁹ No “claim” is asserted at the outset of an SEC investigation – rather, a “claim” is asserted only at the end of some investigations (or in urgent situations like when the SEC seeks a temporary restraining order, for example). Many SEC investigations are closed without action against any entities or individuals.¹⁰ These and other factors are considered when determining whether disclosure is required in a specific instance.

Even when not required to do so, sometimes companies voluntarily disclose the existence of an SEC investigation. This often occurs if rumors are starting to appear in the marketplace, which may have been the catalyst here.¹¹

TAKE-AWAYS

All public companies should consider whether existing circumstances are appropriately considered when finalizing SEC filings. Here are some additional topics we are discussing with our clients now.

1. Ensure coordination and communication between Human Resources and those responsible for disclosures. Legal and financial departments, as well as senior and operational executives, are accustomed to the quarterly disclosure process, and due to recent events, Information Technology professionals also are often consulted before disclosures are finalized. Human Resources professionals must now be in this loop for more than compensation disclosures.
2. Monitor this Activision Blizzard situation and make sure company disclosures will pass muster upon review, because review is coming, one way or the other.
3. In a world where the SEC has now awarded more than \$1 Billion to whistleblowers,¹² and when whistleblowers often are represented by employment counsel who know the rules and the levers to pull, companies should double down on how they follow up on whistleblower claims and ensure that they address the claims carefully and accurately.
4. Finally, consider issues related to confidentiality and defamation when assessing what to disclose. This becomes complex, of course, and must be handled thoughtfully.



ABOUT KING & SPALDING

Celebrating more than 130 years of service, King & Spalding is an international law firm that represents a broad array of clients, including half of the Fortune Global 100, with 1,200 lawyers in 22 offices in the United States, Europe, the Middle East and Asia. The firm has handled matters in over 160 countries on six continents and is consistently recognized for the results it obtains, uncompromising commitment to quality, and dedication to understanding the business and culture of its clients.

This alert provides a general summary of recent legal developments. It is not intended to be and should not be relied upon as legal advice. In some jurisdictions, this may be considered "Attorney Advertising." View our [Privacy Notice](#).

ABU DHABI	CHARLOTTE	FRANKFURT	LOS ANGELES	RIYADH	TOKYO
ATLANTA	CHICAGO	GENEVA	NEW YORK	SAN FRANCISCO	WASHINGTON, D.C.
AUSTIN	DENVER	HOUSTON	NORTHERN VIRGINIA	SILICON VALLEY	
BRUSSELS	DUBAI	LONDON	PARIS	SINGAPORE	

¹ <https://investor.activision.com/news-releases/news-release-details/activision-blizzard-provides-update-workplace-initiatives>

² Shannon Liao, SEC Investigating Game Publisher Activision Blizzard Over Sexual Harassment, Discrimination Allegations, The Washington Post (September 20, 2021).

³ Kirsten Grind and Sarah E. Needleman, SEC Is Investigating Activision Blizzard Over Workplace Practices, Disclosures, The Wall Street Journal (September 20, 2021).

⁴ For example, the Wall Street Journal reported that the California Department of Fair Employment and Housing (DFEH) sued the company in July 2021, following a three-year investigation regarding its workplace practices, alleging that the company had a "frat boy culture." After executives responded publicly, Activision Blizzard employees organized a walk-out on July 28 in protest against what they said was an "abhorrent and insulting response." In early August 2021, the company confirmed that its president and a human resources department executive had left the company. A purported securities class action lawsuit was filed in August, claiming that material information was withheld from investors. And then in September, the Communications Workers of America (CWA) and certain Activision Blizzard employees filed an unfair labor practices lawsuit accusing the company of "worker intimidation and union busting".

⁵ Modernization of Regulation S-K Items 101, 103, and 105, 17 CFR 229, 239, and 240 (Release Nos. 33-10825; 34-89670; File No. S7-11-19).

⁶ See, e.g. Gary Gensler Tweet (August 18, 2021, 11:56 AM) ("Investors want to better understand one of the most critical assets of a company: its people. I've asked staff to propose recommendations for the Commission's consideration on human capital disclosure."); Gary Gensler, Prepared Remarks at London City Week (June 23, 2021) (describing his request to the staff and noting, with respect to human capital disclosure, "This builds on past agency work and could include a number of metrics, such as workforce turnover, skills and development training, compensation, benefits, workforce demographics including diversity, and health and safety. Disclosure helps companies raise money. It helps the efficient allocation of capital across markets. And it helps investors place their money in the companies that fit their investing needs."

⁷ See, e.g., Sample Letter to Companies Regarding Climate Change Disclosures (available at <https://www.sec.gov/corpfin/sample-letter-climate-change-disclosures>).

⁸ Item 103 of Regulation S-K requires a description of material pending legal proceedings as well as proceedings known to be contemplated by governmental authorities. Item 303 of Regulation S-K requires that a company describe (in its Management's Discussion and Analysis) certain types of "trends and uncertainties" as well as items that may affect its liquidity. In addition, Financial Accounting Standards Board Accounting Codification Topic 450 ASC 450 required disclosure of loss contingencies (generally defined as an existing condition, situation or set of circumstances involving uncertainty as to possible loss to an entity that will ultimately be resolved when one or more future events occur or fail to occur). These standards all apply to periodic reports on Form 10-K and Form 10-Q. There is no similar requirement for "real time" reporting on a current report on Form 8-K.

⁹ The typical form letter that accompanies an SEC subpoena states, "This investigation is a non-public, fact-finding inquiry. We are trying to determine whether there have been any violations of the federal securities laws. The investigation and the subpoena do not mean that we have concluded that you or anyone else has violated the law. Also, the investigation does not mean that we have a negative opinion of any person, entity, or security."

¹⁰ This statistic is not publicly reported, but it is consistent with our experience. The information also can be inferred from the SEC Enforcement Division's annual report. See, e.g. 2020 Annual Report Division of Enforcement (published November 2, 2020 and available at <https://www.sec.gov/files/enforcement-annual-report-2020.pdf>) (23,650 Tips, Complaints and Referrals received in fiscal 2020, and 1,181 new inquiries and investigations opened in fiscal 2020, while 715 enforcement actions were brought, mostly related to activities launched in prior years).

¹¹ When rumors or press reports regarding an SEC investigation are circulating, companies sometimes decide to make disclosure regarding the investigation to avoid Regulation FD concerns. Those disclosures allow executives and investor relations professionals to point to the company's public disclosures and avoid awkward interactions with investors and analysts where they otherwise may not be able to comment on the rumors. Even if a company does not believe an investigation is material, disclosure of its existence may also be important to cleanse any concern regarding whether any insiders may have material non-public information before buying or selling company securities.

¹² SEC Surpasses \$1 Billion in Awards to Whistleblowers with Two Awards Totalling \$114 million, press release (September 15, 2021, available at <https://www.sec.gov/news/press-release/2021-177>).