Impact of Social Media on the Securities Market

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The ever-evolving digital space has contributed to the enormous flow of data available on the internet today. The spread of social media platforms such as Twitter, Facebook and Instagram has contributed immensely to the volume of readily available information and opinions. The impact of social media platforms on political discourse, social issues and matters of national security has been well publicized. The recent controversies ranging such as the U.S. Presidential elections, Mark Zuckerberg's testimony to the U.S. Congress, the global #MeToo moveme~nt, issues surrounding the publication of documents on WikiLeaks and unfortunate incidents surrounding the spread of "fake news" on Whatsapp in India are well-known.

In the context of the securities market, the impact of social media has become increasingly relevant because thoughts expressed on social media platforms increasingly influence stock market behaviour. Be it episodic, the influence exerted by even a single tweet show cases the impact of social media platforms today - in that they have percolated much beyond private zones of 'tech-affection' and have moved into the larger realm of the manner in which businesses function.

Securities regulators such the U.S. Securities and Exchange Commission ("S.E.C.") and the Securities and Exchange Board of India ("SEBI") are facing the challenge of maintaining the integrity of the stock markets in the face of social media platforms which provide an unregulated source of data and opinions. The objective of this article is to identify causal links between social media and the way stock markets have reacted to it, in order to assess the growing impact of messages sent via social networks on the larger market sentiment. This article will not indulge in text mining algorithms used to identify patterns of messages over the social network and their causal links with the whole market; but based on a contextual reading of some of the recent news-making events, it seeks to find the causality between a social media sentiment and the price of specific stock titles in order to understand

and illustrate the far-reaching impact of the social media space. This article also analyzes some of the other regulatory issues that stock markets may have to grapple with in the coming times, in the context of insider trading and publishing of price sensitive information, demonstrating the effect of social media in more ways than purely cyber security centric - in ways that can very much affect already established regimes of securities laws.

A case that perfectly fits the point being made above is that of Elon Musk and his recent entertaining tryst with Twitter. The case involves a series of tweets by Elon Musk, founder and Chief Executive Officer of Tesla, Inc. ("Tesla"), on August 7, 2018, regarding taking Tesla (a listed company in the U.S.) private.[1] Musk's statements, made via Twitter, indicated that he sought to take Tesla private at a purchase price that reflected a substantial premium over Tesla's stock's then-current share price, that funding for this transaction had been secured, and that the only contingency was a shareholder vote.[2] In truth, Musk had not even discussed or finalized key deal terms, including price, with any potential funding source.[3] To quote, on August 7, 2018 at around 12:48 PM EDT, Musk tweeted to a Twitter following of over 22 million, "*Am considering taking Tesla private at $420. Funding secured.*"[4] Over the next three hours, Musk made several other materially false and misleading prospective statements via Twitter in relation to taking Tesla private with the support of shareholders and investors.[5] As a result of the hue and cry over his tweets, NASDAQ halted trading in Tesla shares for one and a half hours.[6] After NASDAQ lifted the trading halt, Tesla's stock price continued to rise, closing at $379.57, up over 6% from the time Musk first tweeted about taking Tesla private earlier in the day and up 10.98% from the previous day.[7]

In the complaint filed by the S.E.C. against Elon Musk on September 27, 2018, S.E.C. alleged that Musk knew or perhaps was reckless in not knowing that each of his tweets amounted to false and/or misleading statements because he did not have an adequate basis in fact for his assertions, and neither had he satisfied several additional contingencies when he declared that the only thing remaining between the finalization of Tesla going private was a shareholder vote.[8] Funnily enough, according to Musk, he had calculated the $420 price per share based on a 20% premium to Tesla's then market

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1 *United States Securities and Exchange Commission* v. *Elon Musk*, (2018) Unites States District Court, Southern District of New York, Civil Action No. 1:18-cv-8865 [1].
2 *Ibid* 1.
3 *Ibid.*
4 *Elon Musk*, *supra* note 1, 2.
5 *Ibid.*
6 *Ibid.*, 40, 46.
7 *Ibid.*, 4, 6.
8 *Ibid.*, 3, 68.

price because he thought 20% was a "*standard premium*" in going-private transactions.[9] But in fact, as the S.E.C. concluded, the $420 was rounded up from the actual $419 price per share because he had recently learned about the number's significance in marijuana culture and thought his girlfriend "*would find it funny, which admittedly is not a great reason to pick a price*."[10]

In assessing the market chaos andharm caused to Tesla investors by Musk's impulsive tweets, the S.E.C. noted that immediately prior to Musk's August 7 statements via Twitter, Tesla's stock was trading at $356.67.[11] Musk's first tweet about taking Tesla private set off a trading frenzy and the trading volume and price of Tesla shares immediately spiked.[12] By the end of August 7, after Musk's tweets and a post on Tesla's blog, the stock closed at $379.57, up 6.42% from just prior to the first tweet.[13] By the close of market trading on August 13, after Musk and Tesla disclosed more information about the details underlying Musk's "funding secured" statement, Tesla's stock price had declined to around pre-tweet trading levels. Moreover, by the close of trading on August 27, the first trading day after Musk announced that he was abandoning his proposal to take Tesla private, Tesla's stock had dropped to$319.44.[14] Thus, in S.E.C.'s opinion, investors who purchased Tesla stock in the period after the false and misleading statements but before accurate information was made known to the market, were harmed.[15]

On September 29, 2018, S.E.C. issued a press release indicating that Elon Muskhad agreed to settle the securities fraud charge brought by the S.E.C. against him. The settlements will result in comprehensive corporate governance and other reforms at Tesla with the appointment of two new independent directors, including Musk's removal as Chairman of the Tesla board, and the putting in place of additional controls and procedures to oversee Musk's communication and financial penalties amounting to $20 million each on Musk and Tesla, and another $40 million to the harmed investors, under a court approved process.[16]

What makes Musk-gateintriguing is that it involves one of the most prolific entrepreneurs of the 21st century, having founded PayPal, Tesla, Space X

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9 *Ibid.*, 24.
10 *Ibid.*
11 *Ibid.*, 75.
12 *Ibid.*
13 *Ibid.*
14 *Ibid.*, 76.
15 *Ibid.*, 77.
16 "Elon Musk Settles SEC Fraud Charges; Tesla Charged with and Resolves Securities Law Charge" (2018) <https://www.sec.gov/news/press-release/2018-226> accessed 10 December 2018.

and The Boring Company, a sophisticated businessman and investor whose social media commentary was a clear violation of securities law in the United States. While this was possibly a relatively easy investigation for the S.E.C., it does highlight the challenge securities regulators face globally in ensuring that no false or misleading statements are disseminated on social media.

Depicting the blurred lines between social media profiles and market consequences, Musk's example comes as an eye opener in a day and age where social networking profiles are used heavily by companies and organizations to muster investor interest and support. In the absence of much clarity on what can be or is permitted on one's social media profile to keep investors informed, it is perhaps safer to err on the side of caution when operating social media platforms especially on behalf of businesses and in capacities of CEOs and the like, on topics that concern investors and business forecasts.

In another instance of a tweet causing some ripples in stock prices, Snap Inc. (the company that owns and operates Snapchat) was at the receiving end when American reality television personality and model Kylie Jenner, who also wields extraordinary influence with a Twitter following of over 25 million, expressed disinterest in using Snapchat by tweeting, "*Sooo does anyone else not open Snapchat anymore? Or is it just me... ugh this is so sad*." The tweet was on February 22, 2018 (Thursday) and a brief review of publicly available historical data of stock prices for Snapchat on the NYSE shows that from a closing price of $18.64 per share on February 21, Snapchat closed at $17.51 per share on February 22, i.e., down by 6%. From a look at the previous week's trading prices for Snapchat, it appears that in the week leading up to February 22, the stock prices for Snapchat were on an upturn from Monday and the week before that, until the dip on Thursday, February 22. While Jenner did follow up with a Tweet declaring "*still love you tho snap ... my first love*" - with social media, much like an arrow from a bow, once let loose, the damage may have already been done.

While these are episodic correlations between one-off instances over social media and stock prices, the logic is the same - what one says over the internet is disseminated in a fashion that has all-pervading results, especially in the context of a market susceptible to volatilities like the securities market.

In a dangerously unsettling reality, in addition to Twitter, another popular social networking application with a much wider reach in terms of instant messaging has presented starkly real problems for the stock market, even closer to home. Indian-listed shares of Infibeam fell by approximately 71% on September 28, 2018, from ₹ 200.35 on the closing of September 27 to ₹ 58.45 on the closing of September 28. The Economic Times noted that this was the steepest single-day fall after Satyam Computers Services, which plunged 83% on January 7, 2009, after the accounting scam broke out.[17] What caused this plunge were WhatsApp messages, allegedly attributable to brokerage firm Equirus, raising questions about Infibeam's accounting practices.[18] With Infibeam being only one such example in recent times, the volatility of stock prices relating to social media makes one wonder how and where to draw the line, from a regulatory perspective, for information dissemination on a platform that otherwise knows no bounds.

In another curious case in India, the effect of a blog article expressing surprise at the success of Manpasand Beverages Limited (or Manpasand, a company that sells juices and drinks under the Mango Sip and Fruits Up brand) brings to light what sometimes even an opinion expressed on an online blog can result in, in the context of stock prices and the securities market. In a blog post titled "*The curious case of Manpasand Beverages*" written on December 6, 2016, Amit Mantri (former Vice President at Hornbill Capital, Mumbai, with eight years of experience across private equity and public markets) analyzed the success of Manpasand in achieving high sale volumes, in comparison with its competitors, such as Parle Agro, Coca Cola, Pepsi Cola.[19] Mantri in his blog expressed disbelief in accepting the simple success of Manpasand in attaining a higher market share than brands like Parle Agro (which sells drinks under the brand of Frooti), which being 30 years old, had a much larger advertising budget and distribution network. Mantri questioned governance aspects of the company and the low compensation of a supposedly high performing management, and concluded that something was amiss.[20] While the impact of the blog was not immediate (Manpasand's stock price corrected more than 7% in the days after the blog was published), what precipitated a freefall in the stock price was the sudden resignation of Manpasand's auditorsin late May 2018, days before the final audit for the company was to be finalized. Given the unease created by Mantri's online blog, the market assumed that something was amiss. In its resignation letter, Deloitte stated that "significant information" requested by it from the company's management at various points in time was not provided. The

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17 Rajesh Mascarenhas, "How a WhatsApp Note Triggered Crash in Infibeam Avenues" (ET Bureau, 1 October 2018) <https://economictimes.indiatimes.com/markets/stocks/news/how-a-whatsapp-note-triggers-crash-in-infibeam-avenue/articleshow/66002863.cms> accessed 10 December 2018.

18 Mascarenhas, *supra* note 17.

19 Amit Mantri, "The Curious Case of Manpasand Beverages" (2point2 capital, 6 December 2016) <https://2point2capital.com/blog/index.php/a2016/12/06/the-curious-case-of-manpasand-beverage/> accessed 10 December 2018.

20 *Ibid*; Prathamesh Mulye, "No Longer Street's Manpasand" (*Outlook Business*, 8 June 2018) <https://www.outlookbusiness.com/markets/trend/no-longer-streets-manpasand-4438> accessed 11 December 2018.

questionsraised by Mantri in his blog, coupled with Deloitte's untimely resignation, led to Manpasand's stock price plummeting by over 40% in in less than a week.

What has beenclear from the trials and tribulations of companies such as Infibeam and Manpasand is that the lack of quality information, particularly by small and mid-cap promoter-driven companies, leads to a trust deficit with investors – these companies are easy prey for short sellers waiting to pounce on information asymmetry. While the above instances demonstrate how intra-day trades have been impacted by social media, the effect of social media can also be increasingly felt in the way that SEBI is dealing with issues pertaining to insider trading and sharing of unpublished price sensitive information under the SEBI (Prohibition of Insider Trading) Regulations, 2015 (the "PIT Regulations").

On April 16, 2018, SEBI passed an order in the matter of insider trading in the scrip of Deep Industries Limited ("DIL"), establishing connection between certain persons for the purposes of the PIT Regulations, on the basis of being friends on Facebook and having liked posts of one another on Facebook. SEBI's order indicted three investors –Rupesh Savla, V-Techweb India Pvt. Ltd ("VTPIL") and Sujay Hamlai.[21] According to SEBI, DIL (a diversified oil and gas company) was awarded three contracts around July-August 2015 for hiring mobile drilling rigs from ONGC over a period of several months.[22] Considering the magnitude of the new contracts, the information relating to DIL bagging them constituted as price-sensitive information, which would affect the share price of the company, once published.[23] However, it was observed that Rupesh Savla (Managing Director and Promoter of DIL) had increased his stake in DIL to 8.62% from 8% before this information was made public.[24] SEBI found that VTPIL was owned equally by Ajay and Sujay Hamlai, and that Sujay had traded in the scrip during the investigation period.[25] Additionally, the directors of VTIPL were Facebook friends with Rupesh Savla and his wife, Sheetal. Radhika Hamlai (wife of Ajay Hamlai) was also a friend of Rupesh and Sheetal on Facebook. There were several photos posted by Sheetal Savla on Facebook that were 'liked' by Ajay

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21 SEBI order for DIL, April 16, 2018 (till note 28).

22 Order in the matter of Deep Industries Limited (Order of Whole Time Member, Securities and Exchange Board of India) (2018) (SEBI/WTM/MPB/IVD/ID–6/162/2018).

23 *Ibid.*, 11.

24 *Ibid.*, 4; K.S. Badri Narayanan, "Insider Trading: Beware of Your 'Likes' on Social Media" (*The Hindu Business Line*, 20 April 2018) <https://www.thehindubusinessline.com/markets/insider-trading-beware-of-your-likes-in-social-media/article23619826.ece> accessed 11 December 2018.

25 Order in the matter of Deep Industries Limited (Order of Whole Time Member, Securities and Exchange Board of India) (2018) (SEBI/WTM/MPB/IVD/ID–6/162/2018) (17).

Hamlai and Sujay Hamlai. Similarly, Rupesh and Sheetal Savla had 'liked' several photos posted by Ajay, Sujay and Radhika Hamlai.[26] SEBI found the evidence sufficient to establish connection between these parties and DIL Managing Director Rupesh Savla for the purpose of the PIT Regulations. SEBI held that, by virtue of this association, they were reasonably expected to have access to unpublished price sensitive information of DIL at the relevant period and, therefore, as per the PIT Regulations, Sujay Hamlai and Ajay Hamlai were connected persons and insiders with respect to DIL.[27]

While social media connections may be one out of several other factors (such as trading pattern, KYC documents, etc.) being considered in totality, SEBI seems to have based its *prima facie* finding on the Facebook association to establish connection. While this conclusion may not be inappropriate, the process of relying on Facebook connections to draw links between connected persons is divisive in a time when accepting friend requests or interacting on social media can often be a very light hearted, ill thought out, casual process. Virtual connections becoming the basis of regulatory action raises questions regarding the very authenticity of these virtual connections, not to mention the prospect of online surveillance by regulators.

In a series of other recent actions in relation to social media, in February 2018, SEBI issued directions to HDFC Bank Limited ("HDFC") in respect of the leakage of its unpublished price sensitive information ("UPSI"), relating to its financials, through WhatsApp.[28] SEBI initiated a preliminary examination in the matter of the circulation of the UPSI through WhatsApp, during which it observed that messages circulated on WhatsApp since July 21, 2017[29] closely matched the quarterly financials of HDFC for the quarter ended June 30, 2017, prior to official announcement of actual results by HDFC on July 24, 2017[30]. This could not have been possible without the leakage of information from persons who were privy to the information prior to its official announcement.[31] SEBI noted that leakage of the unpublished quarterly financial results (covered under the definition of UPSI under regulation 2(n) of the PIT Regulations), which eventually led to circulation of messages on WhatsApp, was prohibited and in contravention of the PIT Regulations, which prohibit procurement or communication of UPSI.[32]

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26 *Ibid.*, 18.
27 *Ibid.*, 25.
28 Directions in the matter of HDFC Bank Limited (Order of Whole Time Member, Securities and Exchange Board of India) (2018) (WTM/MPB/ISD/142/2018).
29 *Ibid.*, 2.
30 *Ibid.*
31 *Ibid.*, 10.
32 *Ibid.*, 11.

Whatever be our views regarding regulatory surveillance of social media interactions, there is undoubtedly a role for Indian regulators in the domain of policing corporate disclosure and protecting investor interests. The incidents involving Infibeam and Manpasand demonstrate that not only facts, but also social media banter on the functioning of a company can dramatically affect stock prices, because of the information asymmetry that exists with respect to Indian listed companies. Presently in India, a company is required to make comprehensive disclosures in the form of filing an offer document for a public issue, with relatively condensed yet still detailed offer documents required to be issued at the time of private placements, rights issues, or other offerings post listing. In contrast, there is a disparity in compliance with ongoing financial disclosure obligations by Indian listed companies. While Indian law requires annual and quarterly disclosure of financial information, including related party transactions, there is no 'prospectus style' disclosure to the market by an Indian-listed company to ensure that all material aspects of a company's governance and operations are presented to the larger pool of investors. Annual reports published by listed companies in India are essentially a narration of basic facts and audited financials. Upon listing, fragmented additional disclosures are often guided by a company's own judgment of what it considers to be material developments on an 'as and when basis'. Unavailability, lack of uniformity or subjective nature of information about a company makes such a company more susceptible to stock market volatility post listing.

Regulation 35 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("Listing Regulations") is SEBI's attempt at remedying this information gap by requiring a listed entity to submit an annual information memorandum to the stock exchange(s) as may be specified by the SEBI from time to time in order to assist investors in making informed investment decisions.[33] However, as specific requirements are yet to be notified by SEBI, there is a current lacuna in operationalizing this disclosure requirement for listed companies, particularly in the face of omnipresent and ever-growing social media and given India's promoter-controlled and family-driven corporate environment. A robust corporate governance compliance framework – truly independent directors coupled with transparent and fair public disclosure norms – is becoming increasingly important.

In fact, SEBI is not alone in its concern regarding social media influences upon the market and the public. The Telecom Regulatory Authority of India ("TRAI") issued a press note on August 10, 2017, addressing issues faced

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33 Securities and Exchange Board of India, Discussion Paper on "Annual Information Memorandum" (Reports for Public Comments, 2014).

by SEBI in enforcing its regulations, in relation to misleading unsolicited bulk SMSs by unauthorized persons, relating to investments in securities market.[34] TRAI directed service providers to ensure that SMSs relating to investment advice are only from SEBI registered investment advisers/stock brokers and that necessary arrangements be made to filter and block SMSs sent by telemarketers using bulk SMS channels containing key words relating to securities.[35] This welcome collaboration between TRAI and SEBI in addressing issues faced by the securities market on account of social media is a reminder that the securities market is very susceptible to pressures from a growing digital and social media space, and that issues arising on account of this need to be addressed far more rapidly and creatively than ever before, possibly in consultation with other regulatory authorities.

While it has long been the regulatory objective to improvethe quality and parity of information available in the Indian securities market, the new paradigm that unites multiple regulators, companies, investors and other stakeholders in India is that timely and robust corporate disclosure should temper investor sentiment, whenthe pop of a single social media post may send the stock of a company, or the entire market, crashing.

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[34] Telecom Regulatory Authority of India, "TRAI Issues Direction to Service Providers Regarding Unsolicited Bulk SMSs Relating to Investment in Securities Market" (Information Note to the Press, Press Release No. 58/2017, 2017).

[35] *Ibid.*, 3.