Communicating Electronically with Stock Plan Participants

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The widespread availability of email and Internet access in the workplace provides companies with new ways of fulfilling their duties to deliver documents to employees who participate in stock option and employee stock purchase plans. But new ways of doing things inevitably present traps for the unwary. To avoid these traps, companies should be mindful of the SEC's guidance regarding electronic delivery of employee benefit plan materials.

The federal securities laws require certain information to be provided to stock plan participants, including a plan prospectus and copies of all reports and proxy statements distributed to stockholders. The federal securities laws do not, however, prescribe the medium that must be used to provide this information. As a result, the SEC's view is that information distributed through electronic means (including email, company intranet or the Internet) can satisfy the delivery requirements under federal securities laws *if* the electronic communication results in the delivery of substantially equivalent information as plan participants would have received had the information been delivered in paper format.

To meet this test, companies must focus on whether the electronic communication:

- provides reasonable assurance that delivery to the intended recipient has actually occurred;
- provides timely and adequate notice to the intended recipient that the information is available; and
- can be accessed by the recipient in a way that is not burdensome and that provides an opportunity to retain a permanent record of the information.

Reasonable Assurance of Delivery

Companies using electronic distribution must have a reasonable basis for believing the selected method of distribution has actually resulted in delivery. This requirement is typically satisfied by obtaining an informed consent, in which the recipient agrees to accept delivery of documents in a specified electronic format, or by obtaining evidence that the intended recipient actually received the information. Evidence of actual receipt includes an electronic return receipt or other electronic confirmation that the information has been accessed, downloaded or printed.

In the employee context, the SEC's interpretation of the assurance of delivery requirement is more favorable to companies. The SEC allows companies to presume that an employee who has access to email and is expected to routinely access email as part of his or her job duties will access documents that are distributed via email, unless the employee specifically requests delivery of paper copy. For employees who do not regularly log-on to receive email themselves, the company could set up alternative arrangements, such as sending an email to an assistant or co-worker who then delivers it to the employee.

For employees who do not have access to email and for whom alternative arrangements to receive email messages are not practical, the employee's express and informed consent to electronic distribution is required before the company can use electronic communications to satisfy its delivery requirements. Consent may be obtained through written or electronic means or by telephone, so long as the consent is obtained in a manner that assures its authenticity and a record of the consent is retained. For a consent to be "informed" it must indicate: (1) the specific types of electronic media that may be used; (2) any costs that employees might incur in accessing the electronic information (for example, telephone charges if they dial in from their own personal computers at home over phone lines); (3) that the consent applies to all documents the company is required to deliver; (4) that the consent will be effective until it is revoked by the recipient; and (5) that the employee has the right to revoke consent at any time. Moreover, the SEC's guidance suggests that conditioning an employee's participation in a program on the employee providing consent is not permitted.

Notice of Availability

Even though an employee has consented (or may be presumed to have consented, as described above) to receive documents electronically, the employee must still be provided with notice that the documents are available. This notice needs to be delivered directly to each recipient. Without more, posting a notice on a company intranet, a company bulletin board or in a company newsletter is insufficient to alert a recipient to the online availability of a disclosure document.

For example, each person receiving an option under a stock incentive plan must receive, among other things, a plan prospectus. If the plan prospectus is provided as an attachment to an email, the delivery itself would provide sufficient notice of the availability of the document. In addition, for employees who use email in the ordinary course of performing their duties as employees, it is sufficient to send an email that merely announces the availability of the document and provides information about how to access it. On the other hand, if an employee has expressly consented to delivery of all future documents only by email, then a company cannot satisfy its delivery obligations by emailing the employee a notice that the plan prospectus is available on a company intranet. In contrast, if the employee had expressly consented to delivery by email or intranet access, an email notifying the recipient that the prospectus is available and where on the company's intranet the plan prospectus has been posted would be sufficient.

Access to Required Information

The form of electronic communication used can not be so burdensome that it interferes with the recipient's ability to effectively access the information being provided. Initially, this raised concerns about the ability to use portable document format, or PDF, documents. However, the SEC has indicated that it will allow companies, subject to certain conditions, to disseminate PDF documents and similar documents that cannot be accessed without special software (as opposed to hypertext markup language, or HTML, documents, which can be viewed through standard Internet browsers, without additional software). Companies delivering PDF format documents are required to inform recipients of the requirements necessary to download PDF format documents and to provide recipients, at no cost, with any necessary software and technical assistance to do so.

In addition, recipients must have the opportunity to retain the provided information, for example, by downloading it, or have ongoing access to the information that is the equivalent of personal retention.

In all cases, employees must have the right to receive information in paper format, even if they have previously consented (or may be presumed to have consented) to electronic delivery. In order to satisfy this obligation, and as a precaution in case system failure, computer incompatibility or other technical problems interfere with access, the SEC requires that companies be able to provide paper versions of all documents delivered by electronic means.

Best Practices

The increased efficiency of distributing required stock plan documents to employees electronically represents the main reason why companies should consider electronic delivery. Based on the SEC's guidance and our experience, we recommend that companies adhere to the following procedures if they wish to utilize electronic delivery of documents:

- Companies should be able to verify receipt of electronic documents by individuals. If employees use a company's email system in the ordinary course of business and are expected to routinely log-on to their email to receive communications, companies may generally presume that those employees have received electronic delivery of the documents. In other situations, companies should obtain the express consent of the individual to deliver the documents electronically.
- When companies are required to obtain express consent, that consent must be an informed consent, as described above.
- Companies must notify (by email or otherwise) individuals of the availability of documents. Simply posting the documents on a company's intranet, without more, is insufficient.
- The initial solicitation of employee consent to electronic delivery and each announcement of online availability of a document should prominently state that paper versions are available upon request.
- Documents should be easily accessible (for example, as email to employees that contains a hyperlink to the documents) and should remain available on the company's intranet as long as the relevant plan remains in effect.
- Plan participants should be able to download and print all electronically delivered documents.

Companies with international operations and employees should keep in mind that foreign jurisdictions have different, and often more restrictive, requirements than apply within the United States. Special care and consultation with requisite legal counsel is needed in these situations.

Finally, please refer to our March 9, 2001 Internet Alert for a discussion of Internal Revenue Service and Department of Labor guidance concerning the use of electronic communications in administering employee benefit plans. For a discussion of other SEC guidance on the use of the Internet and other electronic media, please see our May 12, 2000 Internet Alert.

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