

Tesla likely to face SEC investigation following scammer Musk tweets amid debate of market manipulation



- Tesla CEO Elon Musk's tweets about securing funding to take the company private will likely prompt an investigation by federal securities regulators.
- The Wall Street Journal reported that the Securities and Exchange Commission has already "made inquiries."
- Musk risks both civil and possible criminal penalties if he doesn't actually have funding lined up, securities lawyers say.

Robert Ferris | Dawn Kopecki

 Engineer and tech entrepreneur Elon Musk.

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Engineer and tech entrepreneur Elon Musk.

Elon Musk's lawyers are probably pouring over rule 14e-8 of the Securities Exchange Act of 1934 right about now.

That regulation is the one the [Tesla](#) CEO may or may not have violated when he sent the markets into a frenzy and halted trading in Tesla's shares after nonchalantly tweeting Tuesday that he was thinking about taking the electric car company private and had "funding secured," securities lawyers say.

Whether it was an impulse tweet or not, it's likely that the [Securities and Exchange Commission](#) has already opened an investigation and is looking for documentation to back up Musk's comments, former SEC enforcement lawyers say.

The [Wall Street Journal](#) reported Wednesday that the SEC has, in fact, "made inquiries" to find out whether his claim was true, citing people familiar with the matter.

 [SEC has made inquiries on Musk's Tweet from Tuesday: Dow Jones](#)

SEC has made inquiries on Musk's Tuesday tweet: Dow Jones

4 Hours Ago | 00:51

"I can't imagine that the enforcement division hasn't opened a file, that they are not calling his counsel or him and saying 'we would like whatever papers you have about this, if you have written anything down, if you have talked to lenders, if you have materials about that we would like to see them,'" said Tom Gorman, a former senior enforcement attorney with the SEC and a partner at Dorsey & Whitney in Washington, D.C. "And right after we have finished seeing all that stuff, we would like to talk to you."

Investors aren't so convinced that Musk has actually secured funding. If not, that would spell big trouble for both Musk and his company.

"There is skepticism as to where this money comes from. It doesn't make sense," Efraim Levy, an analyst at CFRA, told CNBC. "The reason it is trading at a discount is because of uncertainty as to whether the deal will come to fruition. If it doesn't come through, the stock is going to crater."

The SEC's rule 14e-8 basically prohibits publicly traded companies from announcing plans to buy or sell securities if executives don't intend to follow through, don't have the means to complete the deal or are flat out trying to manipulate the stock price.

§ 240.14e-8 Prohibited conduct in connection with pre-commencement communications.

It is a fraudulent, deceptive or manipulative act or practice within the meaning of section 14(e) of the Act (15 U.S.C. 78n) for any person to publicly announce that the person (or a party on whose behalf the person is acting) plans to make a tender offer that has not yet been commenced, if the person:

(a) Is making the announcement of a potential tender offer without the intention to commence the offer within a reasonable time and complete the offer;

(b) Intends, directly or indirectly, for the announcement to manipulate the market price of the stock of the bidder or subject company; or

(c) Does not have the reasonable belief that the person will have the means to purchase securities to complete the offer.

"He is claiming there is a specific source of the funding so that had better be true. He has also claimed there is a specific amount available for funding. That has to be true. Otherwise, even if it's not manipulation it would be fraud, so he's got two potential areas of difficulty right there," former SEC Chairman Harvey Pitt told CNBC.

Tesla [still hasn't said](#) where it's getting the more than \$71 billion it would cost to take the company private. Wall Street bankers also don't know, suggesting Musk has secured financing elsewhere. But that seems implausible given the size of the deal, which would require multiple banks, and cult-like interest in Musk and Tesla, dealmakers and analysts say.

"News of the deal would have leaked had Tesla already held discussions to secure funding," UBS analyst Colin Langan wrote in a research note Tuesday.

Musk's first tweet at 12:48 p.m. — "Am considering taking Tesla private at \$420. Funding secured" — started a trading frenzy that drove shares to an intraday high of \$387.49 — \$45.47 above Monday's closing price. That comes to \$7.72 billion with its 169.8 million shares outstanding, more than enough to squeeze short sellers who bet the price would fall.

Musk's frequent complaints about "relentless attacks from short sellers" have raised questions about whether or not he was intentionally trying to drive the shares higher, which would meet the definition of market manipulation and carry possible criminal penalties, securities lawyers say.

The comments also might [ease some financial pressure](#) on the carmaker by moving an important convertible bond above its conversion price. If Tesla's shares are above \$359.87 when the debt matures Dec. 1, the bondholders can decide to convert the debt into stock rather than triggering a cash payout of \$920 million when the debt is due come March.

Moody's specifically cited that bond issuance and the company's cash burn rate as reasons for downgrading Tesla's credit rating in March.

Tesla's skeptics have called into question the state of the company's financial position. It lost nearly \$2 billion last year, and so far this year it burned through about \$1.8 billion in cash after capital investments through two quarters. The company had \$2.2 billion in cash at the end of the June quarter.

"If his comments were issued for the purpose of moving the price of the stock, that could be manipulation. It could also be securities fraud," Pitt, now CEO of consulting firm Kalorama Partners, told CNBC's ["Squawk Box."](#) "The use of the specific price for a potential going private transaction is highly unprecedented. And therefore raises significant questions about what his intent was."

If Musk's statements weren't true, he runs the risk of paying damages to investors who lost money on his tweets as well as criminal prosecution, Pitt said.

Peter Henning, a law professor at Wayne State University, called it "backwards corporate governance."

"You don't announce a price and then negotiate. There are a lot steps left in this," he said. "There is a whole process they have to go through or they are going to get the daylights sued out of them."

Investors, meanwhile, are still confused.

Tesla's stock price is a good gauge of how much investors believe Musk. In general, if investors are confident in a deal, shares will rise close to whatever offering price is announced, which would be \$420 in this case.

"However, if investors think there's a 50/50 chance the deal will go through, the price will walk up halfway, between \$340 and \$420, which would be \$380," Yale University finance professor Jacob Thomas told CNBC. "Given a post-tweet price of \$380, roughly speaking, investors think the probability is about 50 percent."

As investors confidence fluctuates, so does the price, rising toward \$420 the more convinced they are or back to \$340 if they are skeptical, he said.

Tesla's stock fell 2.4 percent Wednesday to close at \$370.34 a share.

— *CNBC's Berkeley Lovelace, Tae Kim, Alex Sherman and Hugh Son contributed to this article.*