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# RECENT CASE HIGHLIGHTS POTENTIAL PITFALLS OF INFORMAL COMMUNICATIONS WITH ANALYSTS

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A recent court case highlights the potential pitfalls for public companies engaging in informal communications with analysts. The court found that paraphrased statements attributed to an officer in an analyst's report can be actionable (City of Warren Police & Fire Retirement System v. Prudential Financial (3rd Cir. June 13, 2023)). Although the claim was dismissed on other grounds, the decision is a reminder of the perils of unstructured or informal discussions with analysts and the need to continually review "best practices" for communicating with the street.

## BACKGROUND OF CASE

In January 2013, Prudential acquired 700,000 life insurance policies from The Hartford for $615 million and, by 2015, had fully integrated the block into its individual life segment. Following a $65 million reserve increase in mid-2018, the company made several public statements in early 2019 that disavowed any serious problems with the individual life segment. In March 2019, in a meeting with analysts, a senior officer assured that there were no systemic issues with underwriting or mortality assumptions in the segment.

In July 2019, Prudential announced a $208 million increase in its individual life reserves and an expected reduction in quarterly earnings of $25 million for the foreseeable future. After that news, its stock price dropped 12% over the next two days. The plaintiff filed a putative class action alleging securities fraud under Sections 10(b) and 20(a) of the Securities Exchange Act. The Third Circuit affirmed the dismissal by the trial court of three of the claims but reversed on one set of claims that it found contained sufficiently particularized and plausible allegations of falsity.

The plaintiff had alleged that the officer's statement in March 2019 that there were no "systemic issues" with the company's underwriting practices or mortality assumptions was false and misleading. The district court dismissed the claim because the statement was not a direct quotation but instead was paraphrased in an analyst's report and therefore not "made" by the officer. The Third Circuit rejected that reasoning, concluding that the statement was actionable because the statement was clearly attributable to the officer and "the context of the statement indicates that he exercised control over its content and the decision to communicate it to [the analyst].” However, it dismissed the claim for failing to plausibly allege the falsity of the statement.

With respect to a different claim involving a statement by CFO, however, the court remanded the case to the district court to consider the adequacy of the allegations of loss causation and scienter.

Eight weeks before the announcement of the increase in reserves, the CFO had stated that recent mortality experience was within the “normal” range of volatility or, at worst, only “slightly negative.” However, according to the complaint, and based on a confidential former employee, the company was then already considering a significant increase in reserves due to negative mortality experience.

## RECOMMENDED PRACTICES WHEN DEALING WITH ANALYSTS

In order to minimize risks, companies should consider the following steps:

- Monitor internal operating reports, analyses and board reports; seek to maintain consistency between public disclosures and internal documents; seek to minimize the possibility of hindsight mischaracterization of internal documents.

- Review analyst, investment banker and other third-party reports to assess whether the market understands the risks associated with the company's business.
  - When appropriate, provide supplemental disclosure in an FD-compliant manner, to the extent it may contain material non-public information (MNPI).

- Use and follow scripts; avoid informal comments. Remember that third parties are likely to publish transcripts.
  - Except during an FD-compliant webcast, avoid providing any MNPI to analysts.
  - Debrief after presentations or one-on-one meetings to consider whether any inadvertent disclosures of MNPI may have occurred and/or whether FD remedial steps might be advisable.
    - In case of any close calls, consider documenting any determinations of immateriality to memorialize the company’s good faith judgments, taking into account consultations with counsel.

- Care should be exercised in dealing with analysts to avoid entanglement or inadvertently disclosing MNPI.
  - Consider having an FD-trained official accompany officers meeting with analysts to monitor and assist with debriefings and, when advisable, devising FD remedial steps.
  - Consider maintaining logs of contacts or phone calls and contemporaneously documenting the substance of any one-on-one discussions.
  - Avoid commenting on analyst reports or earnings models, except for corrections of factual misstatements consistent with publicly available historical or factual information or to correct mathematical errors.
    - Maintain a written record of comments, and include a disclaimer approved by legal counsel but recognize that it may not provide complete protection, depending on the facts and circumstances.
    - No other feedback or guidance on analyst reports or earnings models, including as to analyst forecasts or projections, should be communicated.
  - Avoid commenting on or confirming earnings expectations, except during an approved short window following, and consistent with, prior broadly noticed and disseminated guidance, such as during an earnings call, and after consultation with legal counsel.

- Avoid distributing third party materials, such as analyst reports or media articles, posting them on websites or maintaining hyperlinks to third-party sites.
  - At a minimum, if distributed, use appropriate disclaimers of responsibility, approved by legal counsel, but recognize that they may not provide complete protection, depending on the facts and circumstances.
  - If materials are distributed, do not selectively distribute only the favorable materials.
  - To the extent materials that are implicitly endorsed contain MNPI (e.g., projections), consideration should be given to risks of selective disclosure.

- Utilize the safe harbor in connection with any oral or written forward-looking statements.
  - Update the safe harbor whenever used. Do not let it become “boilerplate.”
  - Include whenever slides or transcripts are “republished,” such as on a website.

- Exercise care when making forward-looking disclosures; consider any potential duty to update.
  - Specifically state that statements will not be updated or revised in the future.

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- Securities & Corporate Governance

## MEET THE TEAM


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