

# Client Alert

Latham & Watkins Corporate Department

## Giving Good Guidance: What Every Public Company Should Know

Every public company must decide whether and to what extent to give the market guidance about future operating results. Questions from the buy side will begin at the IPO road show and will likely continue on every quarterly earnings call and at investor meetings and conferences between earnings calls. The decision whether to give guidance and how much guidance to give is an intensely individual one. There is no one-size-fits-all approach in this area. The only universal truths are (1) a public company should have a policy on guidance and (2) the policy should be the subject of careful thought.

The purpose of this *Client Alert* is to provide an updated discussion of the issues that CEOs, CFOs and audit committee members should consider before formulating a guidance policy.<sup>1</sup> In Annex A, we answer some frequently asked questions about guidance and offer some practical guidelines to consider when drafting a guidance policy.

### A Review of the Basics

Public companies are not required by stock exchange rules or the SEC's rules to provide investors with projections of future operating results.<sup>2</sup> However, investors and analysts can be demanding, and many public companies elect to provide the market with guidance about their expectations for the future. The decision to give guidance can spring from a desire to share good news with investors in order to help the market get to a higher valuation for the company's stock or it can spring from a desire to correct analysts' overly optimistic earnings expectations. Whatever the motivation, the legal landscape should be carefully understood before management takes the plunge. It is possible to give guidance in a deliberate and careful way without incurring undue liability. It is also possible to make critical mistakes that can have significant economic consequences under the federal securities laws and in the financial markets.

### Primary Liability Provisions

There are a number of provisions in the federal securities laws that can create liability for forward-looking statements. In the context of a public offering, Section 11 and Section 12 of the Securities Act of 1933 impose liability on issuers, their officers and directors, and underwriters for misstatements of material fact or

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omissions of material facts necessary to make included statements not misleading. Rule 10b-5 under the Securities Exchange Act of 1934 imposes liability in a broadly similar manner, although the burden of proof on a plaintiff bringing a Rule 10b-5 claim is higher.<sup>3</sup> Rule 10b-5 applies to statements made in the context of securities offerings as well as in periodic reports and day-to-day communications with analysts and investors. Because of the potential for liability, it is prudent for those giving guidance to speak carefully, completely and deliberately.

### **Safe Harbors**

The Private Securities Litigation Reform Act of 1995 (PSLRA) enacted safe harbor provisions in both the Securities Act and the Exchange Act for forward-looking statements<sup>4</sup> that are (1) identified as such and (2) accompanied by “meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement.”<sup>5</sup> These safe harbors also provide protection where a plaintiff fails to prove that a statement was made with actual knowledge that the statement was false or misleading if made by a natural person, or was made by or with the approval of an executive officer if made by a company.<sup>6</sup> The PSLRA safe harbor provisions do not apply in the context of an IPO or to enforcement proceedings brought by the SEC.

### **Forward-Looking Statements**

The federal courts have held that forward-looking statements that are accompanied by appropriate cautionary language do not give rise to a claim for liability under the federal securities laws because the predictive statement read in context with the risk disclosure is not misleading as a matter of law. However, despite the broad protections of the PSLRA's safe harbor, boilerplate cautionary language may not be sufficient. Some courts have declined to allow the protections of the safe harbor where risk disclosures did not change over time or did not identify the risks that ultimately caused the prediction not to come to pass. Specific, robust and dynamic cautionary language is often the best defense to a review of forward-looking statements that may (especially with the benefit of hindsight) ultimately prove to be inaccurate.<sup>7</sup> As a result, public companies should routinely evaluate and tailor cautionary language for each significant forward-looking statement. Any areas of heightened risk or known uncertainties warrant fact-specific disclosures that are customized to the particular risks underlying each forward-looking statement. Well-crafted disclosure can serve as a shield against future challenges if good-faith predictions of future results do not materialize.

### **Whether to Update**

Although the PSLRA explicitly states that it does not “impose upon any person a duty to update a forward-looking statement,”<sup>8</sup> some courts have suggested that a duty to update may apply if events transpire that cause a company's prior disclosure to become materially inaccurate, even though that prior disclosure was accurate when made.<sup>9</sup> There is no requirement that a public company immediately make public all material facts that come into its possession on a real-time basis,<sup>10</sup> but where a public company's affirmative and definitive prior statement becomes clearly and materially false, it should consider issuing a clarifying, correcting or updating statement.

What does all this mean for public companies? Among other things, it means a company can answer the question “Are you in merger negotiations with XYZ, Inc.?” with a “no comment” and not be obligated to later update that statement

if it enters into merger negotiations.<sup>11</sup> However, if the answer to the first question was “This company will never enter into merger negotiations with XYZ, Inc.,” then the company may want to consider an updating disclosure if merger negotiations begin in earnest. In other words, once the decision to speak on a particular topic — expected earnings for the year, for example — is made, it may be problematic to stop talking about it in the future as the facts change.

Considering whether to update earnings guidance is particularly complicated and depends very much on the facts and circumstances at hand. The analysis should always begin with a review of what was said in the first place. As an example, let’s consider a company that issues guidance only once per year, in the first quarter, projecting earnings for the full year then in progress. In order to answer the question whether our hypothetical company needs to update its guidance every quarter as more facts become available and its expectations about the likely outcome for the full year move around, we must first ask what was said when the guidance was originally issued. Did the company specifically say that it would not be updating the full-year guidance every quarter? Did the company say it would only update guidance if a material corporate transaction occurs?

The next series of questions to consider focuses on the facts that have transpired since the original guidance was issued. Is it obvious that the original guidance no longer holds because of well-understood changes in industry trends or market conditions or an intervening acquisition or disposition? Did the original guidance include a clear explanation of the assumptions on which it was based? Is it clear that those assumptions have not come to pass? Has the Wall Street analyst community revised its estimate of full-year earnings down to a level that the company believes it can deliver?

Still other questions focus on the unique facts of the company’s circumstances. Is the company in a line of business where it is difficult to know how the year will turn out until the last bottle of New Year’s champagne has been poured? Will the company realistically be able to avoid questions from analysts about the continuing validity of its earlier guidance? All of these considerations will come into play in analyzing the legal landscape and deciding whether to confirm or update prior guidance. Also very relevant to the decision is the investor relations department’s desire to avoid unpleasant surprises among the company’s constituents. An important further complication, which we will discuss below, is whether the company is selling or purchasing its own securities.

### **Regulation FD**

Regulation FD’s prohibition on selective disclosure of material nonpublic information must also be taken into account in any discussion of whether to give or update guidance.

Regulation FD and subsequent SEC enforcement actions have effectively eliminated the historical practice of privately “walking” analysts’ earnings estimates up or down to avoid unpleasant surprises at quarter-end or year-end. Guiding analysts about future earnings is still permissible under Regulation FD, so long as the analysts and the general public learn all material information at the same time.

Updating or confirming prior guidance is treated the same way under Regulation FD — it’s all fine as long as the public gets the same material information at the same time that the analysts do. Therefore, the question “Are you still comfortable with your guidance for this year?” is right in the center of Regulation FD’s bull’s eye. When answering that question, Regulation FD considerations need to be taken into

account. An officer who provides direct or indirect guidance to an analyst regarding earnings forecasts “takes on a high degree of risk under Regulation FD.”<sup>12</sup>

## **Two Basic Questions**

Many companies will sort through the overlapping webs of safe harbors, case law and liability provisions and conclude that guidance is simply not worth the headaches. Other companies will conclude that the benefits of managing market expectations outweigh these headaches and will take the guidance plunge. The remainder of this *Client Alert* is aimed at providing some practical suggestions on how to survive as a giver of guidance.

### **How Far to Go**

The most basic decision is whether to give guidance on a quarter-by-quarter basis or on a year-by-year basis. The next question is how far forward to project results. There is no one-size-fits-all answer here. Some businesses are stable and predictable. For them, predicting earnings on a quarter-by-quarter basis may be an option. Many energy companies, for example, have presold the majority of their output multiple years into the future. A company with a predictable earnings stream is in a very different position than a company with unpredictable operating results.

Businesses with lumpy revenue streams or that experience seasonality or weather issues may not feel they can make quarterly projections prudently. A September 2012 survey performed by the National Investor Relations Institute (NIRI) found that guidance-giving companies most often communicate annual estimates only. The most common frequency for communicating those estimates is on a quarterly basis.<sup>13</sup> Even the most stable businesses typically elect not to provide earnings guidance beyond the year in progress, although some businesses will provide long-term estimates or goals for longer periods.

### **What to Say**

Directly related to the decision of how far forward to look when guiding investors is the decision of what to say about the periods in question. Guidance takes many forms, not just earnings per share for the year. Some companies will guide investor expectations by giving a range of anticipated earnings per share or simply by saying that they are “comfortable with the Wall Street analysts’ consensus” regarding earnings per share for the year. However, explicitly blessing a specific analyst’s estimate can be viewed under the case law as “adopting” it, which has the same liability considerations as issuing guidance directly. This casual approach to guidance usually does not offer an opportunity to include appropriate cautionary disclosure and should generally be avoided.

Many companies prefer to provide the market with forecasts of an Adjusted Net Income or Adjusted EBITDA metric that excludes the impact of expected (or unexpected) non-recurring, non-cash and/or unusual items. Adjusted measures of operating performance are easier to predict accurately since they are unaffected by many of the income statement items that impact earnings per share. Of course, public release of these non-GAAP financial measures will need to comply with Regulation G.<sup>14</sup>

Other companies stop their numerical guidance at the revenue line, projecting only a targeted revenue growth in percentage terms. Revenue-only guidance may be supplemented with a comment about profit margins — “We expect to see an improvement in profit margins as we do not expect anticipated revenue increases

to be accompanied by a corresponding increase in our fixed costs" — or not. Still another form of guidance involves non-financial measures — "We expect to open 25 new company-owned stores this year" or "We currently expect to complete construction of the facility in the fourth quarter of 2012."<sup>15</sup> There is no limit to the forms that guidance can take. What is appropriate for one company in one industry may be totally inappropriate for another company, even one in the same industry.

## **Guidance Guidelines**

### **Scope**

Each company's decision of what to say and how far to go needs to be made in light of the nature of its industry and the circumstances of its business. Careful thought should be given to the tradeoff that going further down the income statement presents — more precise information will please analysts in the short run but it can create sharper liability issues in the long run. Much more agility is needed to predict earnings per share successfully than to predict revenue, Adjusted Net Income, Adjusted EBITDA or another "normalized" measure of performance that is less likely to be affected by surprises on the business front or in the accounting literature. We recommend that companies only give guidance on a metric that they feel comfortable they can accurately predict.

### **Cautionary Statements**

All good guidance should be accompanied by dynamic, carefully tailored cautionary statements. These disclaimers should temper the predictions of a rosy future with a balanced discussion of what could go wrong. Risk factor disclosure should also be appropriately updated with each publication — don't just use the same old boilerplate from prior years. It is also helpful if some of the material assumptions on which the guidance is based are disclosed and if the company's risk factors tie to the achievement of those assumptions. A 10 percent increase in earnings that is premised on cutting redundant overhead costs is not the same as a 10 percent increase that is premised on a substantial increase in market share. The point of cautionary language is to explain what goes into the sausage so investors can make their own intelligent decisions about the likelihood of the projected outcome actually being realized. Good cautionary disclosure can be an effective insurance policy against future liability if the guidance turns out to be incorrect.

### **The Delivery**

It is best if guidance and the related cautionary disclosures are given in a controlled environment. The most popular forums are the year-end or quarter-end press release and the related quarterly earnings calls. The press release and the script for an earnings call are usually the subject of a greater degree of oversight than any casual encounter, and earnings calls are always Regulation FD-driven events since the public is invited to listen in and a recording is typically available on the company's website for a period of time after the call. Many companies prefer to give guidance orally on their earnings calls and do not produce a written version of their statements for the related earnings press release. For a CFO who is comfortable sticking tightly to a prepared script, this is a perfectly acceptable choice. For others, putting it down in writing in the earnings release may be a wise precaution. Regardless of the method of delivery of guidance, every company should carefully evaluate its internal processes for preparing and providing guidance.

The earnings release or call should include carefully tailored disclaimer language and the actual guidance statements should be carefully vetted and scripted. Oral forward-looking statements should be accompanied by an oral statement that cautionary disclosures are contained in a readily available written document. Similarly, statements regarding non-GAAP financial measures should identify where the required reconciliations can be found.

### **Anticipating Questions**

There are at least three good reasons to anticipate the questions about guidance that analysts are likely to ask on an earnings call. First, there are some questions the company will want to answer. If the answer has not been scripted, it may not come out with all of the nuance that is appropriate. Second, there are some questions the company will not want to answer. It helps to have worked out in advance which questions the company is prepared to answer and which questions merit only a "no comment" response. Finally, Regulation FD frowns on answering follow-up questions in private calls or meetings where the public does not have access, so what is said on the earnings call will set the boundaries of what can be discussed in private meetings between earnings calls. Answering questions that were asked on the earnings call or providing additional detail on topics that have been covered at an appropriate level of materiality on the earnings call will generally be acceptable in follow up one-on-one investor meetings. Venturing into territories that were not covered on the earnings call in subsequent private meetings can raise selective disclosure issues under Regulation FD.

### **Updating or Confirming Prior Guidance**

When management begins to doubt whether the company's actual results will be in line with prior guidance, the decision whether to make a public statement to that effect is entirely dependent on context — all facts and circumstances must be considered. As always, the analysis should start with a review of what was said in the first place. Did the company say that it would confirm annual guidance every quarter? Did the company say that it would not? Is it obvious from the facts that the prior guidance is no longer reliable (due to an important acquisition, disposition or industry development)?

If a company expects to exceed its prior guidance by a modest amount, it is probably safe to keep that information confidential and pleasantly surprise the investment community. On the other hand, if a company is reasonably sure that it will miss the mark by a material amount, intervening events or market pressures may force an out-of-sequence guidance update. Context is everything. For a company repurchasing its own shares or one involved in a going-private transaction, the fact that current guidance is materially low may be problematic. In the context of a securities offering, the opposite is true — materially high guidance is the concern. Managing expectations to maintain credibility, provide transparency and avoid unpleasant surprises is always the goal.

Below is a list of key considerations to keep in mind when giving guidance:

## **10 Rules for Giving Good Guidance**

1. Designate a limited number of company personnel to communicate with analysts and investors about future plans and prospects.
2. Adopt an appropriate guidance policy early and follow it.
3. Do not rely on boilerplate. Explain the assumptions underlying each forward-looking statement and disclose the risks that may cause anticipated results not to be realized — the cautionary statements should be tailored to fit the guidance.
4. Have prepared remarks reviewed by counsel and stick to the script.
5. Remember Regulation FD: Disclose guidance and other material information only in an FD-compliant manner.
6. Do not be afraid to say “no comment” in response to questions or to deflect uncomfortable questions by restating the company’s guidance policy.
7. Do not comment on or redistribute analysts’ reports, and only review advance copies of analysts’ reports for factual errors.
8. Remember Regulation G: Include appropriate disclosure for non-GAAP financial measures where required.
9. Continually evaluate whether changed circumstances argue in favor of an update of prior disclosures.
10. Be particularly sensitive to Rules 1 through 9 in the context of an intervening event between quarterly earnings releases and calls such as an offering of securities, share repurchase program or acquisition, or when insiders are buying or selling company securities.

## **Special Considerations**

### **Securities Offerings**

The pendency of a securities offering creates special issues for guidance-giving companies. It is rare to find written guidance in a prospectus or offering memorandum and most earnings releases are furnished on Form 8-K rather than filed and hence are not incorporated by reference into the offering document. This means that guidance is rarely part of the landscape for purposes of Section 11 of the Securities Act.<sup>16</sup> However, there remains an important question of whether the prior guidance can be considered part of the offering for Section 12 and Rule 10b-5 purposes. The answer depends on the facts and circumstances. Where the prior guidance was given only orally at an earnings call many months previously, and if no reference is made to the prior guidance in the selling process, it may be possible to argue successfully that it is not part of the liability file for Section 12 purposes.<sup>17</sup> That fact pattern could occur, for example, in a block trade context where there is no road show. However, where actual results are expected to be materially lower than the prior guidance, most companies elect to stay out of the market until they can properly adjust investor expectations by amending or updating their prior



guidance.<sup>18</sup> Even when it is possible to conclude that there is no legal duty to do so, investor relations considerations usually prevail. It is easy to see how a new investor who purchased securities at a time when the prior guidance indicated earnings per share for the year in the range of \$1.05 to \$1.10 might feel wronged if shortly after his or her purchase the company reports earnings per share of \$0.90. In the context of a securities offering, managing expectations becomes even more important. Investors who get what they expected generally don't sue issuers. Disappointed investors sometimes do.

In the event of an out-of-sequence guidance update prior to a securities offering, special consideration should be given as to whether the update constitutes an "offer" under the Securities Act.<sup>19</sup> The SEC has adopted a number of safe harbors to protect various activities that are either harmless or necessary to the proper functioning of the capital markets.

Rule 168 is a non-exclusive safe harbor from Section 5(c)'s prohibition on pre-filing offers (and from Section 2(a)(10)'s definition of prospectus) that is available only to reporting issuers with a history of making similar public disclosures. It allows a reporting issuer and certain widely traded non-reporting foreign private issuers to make continued regular release or dissemination of "factual business information" and "forward-looking information,"<sup>20</sup> but not information about an offering or information released as part of offering activities. Rule 168 is not available to underwriters.

Disclosure of Rule 168 information is permitted at any time, including before and after the filing of a registration statement, but only if:

- the issuer has previously released or disseminated Rule 168 information in the ordinary course of its business and
- the timing, manner and form in which the information is released is materially consistent with similar past disclosures.

For the information to be considered previously released in the ordinary course of business, the method of releasing or disseminating the information, and not just the content, is required to be materially consistent with prior practice.<sup>21</sup> The SEC has acknowledged that one prior release could establish a sufficient track record,<sup>22</sup> although it has also cautioned that an issuer's release of "new types of financial information or projections just before or during a registered offering will likely prevent a conclusion" that the issuer regularly releases that information.<sup>23</sup>

What should public companies do in light of the Rule 168 safe harbor? Because Rule 168 looks to track record, public companies should establish a pattern of issuing information and then stick to it. Concluding that the safe harbor for any particular situation is available is going to be easier if there is a prior record of releasing the same general information on reasonably similar timing.

### **Share Repurchase Programs**

Like pending offerings or strategic transactions, share repurchases require careful attention to guidance practices since the potential for liability under Rule 10b-5 exists equally in all of these contexts.<sup>24</sup> However, there are some important differences. Few purchasers in an offering will be disappointed if the company's guidance turns out to have been unduly conservative and earnings come in higher than projected. Shareholders who sold stock back to the company following gloomy projections, on the other hand, may feel aggrieved if subsequent actual earnings are strong. In other words, overly conservative guidance given during, or before commencing, a share repurchase program can be just as problematic as overly rosy guidance in the context of a securities offering.



The key to avoiding liability is careful forethought to the timing of the guidance and the share repurchases. For example, consider limiting share repurchases to time periods that closely follow guidance announcements. The more closely in time the repurchases follow the guidance, the less likely that intervening events have undermined the guidance. Companies with particularly active share repurchase programs may want to consider adopting and closely monitoring blackout trading windows and utilizing Rule 10b5-1 plans executed during open trading windows.

### **Insider Sales**

A decision not to update guidance may restrict the ability of executives and other insiders to sell shares of their company's stock. If the company learns facts causing management to conclude that prior guidance may no longer be accurate, both the underlying facts and management's conclusion could later be found to be material information. If insiders sell shares before the stale guidance is updated, regulators and plaintiffs could take the position that those transactions constituted improper insider trading. Accordingly, if events undermine the accuracy of earlier public guidance, it may be wise to suspend executive purchases and sales of stock in order to avoid allegations of insider trading.

### **Mergers and Acquisitions**

Companies often provide guidance about the effects of significant corporate transactions — "We expect this transaction to be accretive to our earnings next year." These statements are subject to all of the concerns in this *Client Alert* generally, including the risk of liability under Rule 10b-5 and, if there is a registration statement to be filed in connection with the transaction, Sections 11 and 12. These statements also need to be considered in the context of the incremental statutory liability imposed by the proxy and tender offer rules. Regulation M-A may require documents containing these statements to be filed with the SEC. In business-combination transactions, companies must also closely monitor public statements of their financial advisors, information agents and proxy solicitors that might be attributed to the company for purposes of compliance with Regulation FD and the other issues discussed in this *Client Alert*. Statements made in the context of merger or acquisition transactions may influence voting decisions, tender decisions and purchase and sale decisions by both the company's and the target's shareholders, which increases the number of potential claimants. The many additional variables (such as the combined results of the two companies and synergies) to be taken into account when giving guidance in these circumstances make giving guidance in the context of mergers and acquisitions particularly complex.

## **Conclusions**

### **Be Deliberate**

The decision whether and to what extent to give guidance should be made in a deliberate manner and should be the subject of careful internal control, including discussion with counsel. Each company's situation is unique — there is no one-size-fits-all solution to earnings guidance because each decision is fact-intensive. Plan ahead about how and when guidance will be given and script the statements carefully. Make sure to explain the critical assumptions underlying projected results so investors can evaluate those projections fairly.

### **Get a Policy and Stick to It**

Consistency can be very helpful, both from an investor relations perspective and from a liability perspective. Having a policy and following it can go a long way.<sup>25</sup> Companies should tell investors when guidance will be given so investors know what to expect. For example, a company should tell investors that its policy is to give guidance once a year in March concurrently with the year-end earnings release, covering expectations for the year in process. The company should then not update its guidance during the course of the year except in extraordinary circumstances, such as a securities offering or a material acquisition or disposition. This way, in between planned updates, the company can deflect investor questions by explaining that it is the company's policy not to comment on prior guidance out of cycle.

### **Be Vigilant With Respect to Updates**

A company should not simply follow its guidance policy blindly. Particularly in the context of securities offerings, sales by insiders or share repurchase programs, companies need to be alert to market expectations. Circumstances that might cause a company to want to update guidance can occur very quickly and at inopportune times, and companies need to be able to act quickly in this era of instant information flow. All of the key players should coordinate and communicate when the need arises so that informed judgments can be made as to what to say to the market and when.

### **Involve Counsel**

Viewed with hindsight, overly optimistic guidance can result in financial cost to the company and its directors and officers. Legal counsel should be part of the quality control and risk/reward evaluation process. It is not always true that the investor relations department wants more information projected and lawyers want less. In practice, giving good guidance can only be done by balancing the benefits to the company and the associated risks, and counsel can assist in this balancing act.

## Annex A

### Frequently Asked Questions

Set forth below are some frequently asked questions about how and when to give and update guidance.

*Q: A company normally issues annual guidance in its year-end earnings release and updates that guidance during subsequent quarterly earnings releases. The company no longer expects to meet its previously published guidance. Should the company revise its guidance downward ahead of the next regularly scheduled quarterly earnings release?*

A: It depends. The company should review what was said in the previously published guidance. Did the company say it would update its guidance between scheduled earnings releases? Did it say that it would not? Was it silent on the matter? Many companies have a general no-update policy, but companies sometimes do not make that clear in each earnings release. Updating previously published guidance between scheduled earnings releases is not common practice and the company should consider all facts and circumstances before updating guidance ahead of the next regularly scheduled earnings release. If a major corporate event has occurred, such as a material acquisition or disposition, it may be obvious that the previously published guidance is no longer operative, which may lessen the pressure for an early update.

*Q: What about a similar scenario, where the company is near the end of its quarter and the midpoint of its current estimates for the year in progress is not in line with previously published guidance. Should the company revise or adjust guidance downward prior to the next earnings release?*

A: The starting point of the analysis is always the same. What was said in the first instance and what does the market expect? Will the market be surprised if the company's results do not square with previously published guidance? Does the midpoint of the estimates show that the company is going to miss the bottom end of the previously announced range by a material amount? Revising or adjusting guidance downward may be an option if there is a compelling reason to provide an out-of-sequence update and the company is reasonably sure that its results will not be in line with guidance. In most cases, however, the update can wait until the next regularly scheduled earnings release. In other words, if the company's guidance policy is to give updates quarterly, then the company should follow its policy absent compelling circumstances.

*Q: The company plans to attend an annual industry conference that takes place between earnings releases. Can the company pre-release a guidance update prior to the conference?*

A: Yes, if there is a good reason to do so, after considering all facts and circumstances. Departing from a regular policy of giving guidance only on designated earnings releases should not be undertaken lightly, but may be necessary on occasion. For example, if there is a compelling need to update customers on expected future results — a situation that sometimes arises in the troubled-company context — then have at it. Absent a compelling reason to depart from established policy, follow the policy. As always, any updates need to occur in a manner that complies with Regulation FD.

*Q: The company is near the end of its quarter and some of the analysts' estimates are higher than the results the company expects to report for the quarter and even higher than the company's previously announced guidance. Can the company meet privately with the analysts to talk them down?*

A: No. This is an easy one. Regulation FD requires that when issuers disclose material information, they must make broad public disclosure of that information. Talking down an industry analyst is providing material nonpublic information to that analyst and is not allowed in any manner that does not comply with Regulation FD. Some issuers handle the rogue analyst situation by issuing a press release (or making statements on an earnings call) emphasizing the factors that the company believes will make it difficult to achieve the overly optimistic results predicted by the outlying analysts. Most companies decline to get drawn into specific public disavowals of rogue analysts' estimates.

*Q: The company issued annual guidance in its year-end earnings release in March. It's now June and the company is about to launch a public offering of its common stock. The company still expects to meet (or slightly exceed) its published guidance. Can the company put a slide in the road show deck that reiterates its annual guidance?*

A: This is tricky. The presence of the slide may imply that the company is confirming its annual guidance, which is effectively the same as publishing new guidance. That raises the question of whether the confirmation is itself material nonpublic information. Depending on the circumstances, there may be an argument that a reaffirmation of prior guidance is not material, but if any significant amount of time has passed between the original public guidance and the private reaffirmation, the private statement is likely to be considered material nonpublic information. If a guidance update or confirmation is material, then a public press release would be appropriate under Regulation FD.

However, an out-of-sequence guidance release, particularly where guidance is being increased, raises other issues in the context of an offering. An SEC Staff Compliance and Disclosure Interpretation (C&DI) of Regulation FD suggests that a company's reference to prior guidance will not necessarily be deemed to convey material nonpublic information as long as the company makes clear that (a) the prior guidance was issued as of the earlier date and (b) the company is not currently reaffirming the earlier guidance.<sup>26</sup> That C&DI could be read to support the position that a road show slide citing the earlier earnings guidance (and giving the date it was issued) is not problematic from a Regulation FD perspective. Such a slide may be an option for management teams that are able to stick tightly to the road show script and can avoid commenting on the slide in a way that would implicitly confirm the prior guidance as of the date of the road show. However, many companies elect not to venture into this tricky territory and do not comment on guidance during their road shows, except perhaps to say "We publish our annual guidance in March and it is our policy not to update guidance between earnings releases." Those companies rely on the market's understanding that it would not be appropriate to sell securities without updating outstanding guidance if the issuer felt that the prior guidance had become too high.

*Q: What if the company wants to confirm or increase its guidance immediately prior to launching an offering?*

A: This is another difficult scenario. The first question is whether the increased guidance is an offer under the Securities Act. Rule 168's safe harbor for regularly released factual business information or forward-looking information is available

for the same type of information as previously released in the ordinary course of business. Increasing guidance between earnings releases is not in most companies' ordinary playbook, but a company that has done so at least once before (perhaps outside the context of an offering) may be able to get comfortable that it has an adequate track record for an increase in guidance to fall within the safe harbor. If a company has no such track record, the proximity of the increase in guidance to the launch of the offering would be another uncomfortable fact in the analysis of whether the communication might constitute an offer. The next question is whether the new guidance will be considered to be part of the Section 12 file associated with the upcoming offering. Depending on the new guidance's proximity to the launch of the offering, it may well be. Bottom line: Confirming or increasing guidance within days of launching an offering is potentially problematic unless part of a company's regular routine or, at least, its prior experience.

*Q: The company wants to launch an offering next week but it does not expect to meet its prior guidance for the quarter in progress. Can the company revise guidance downward just before launching its offering?*

A: Yes. This is good corporate citizenship. In fact, absent unusual circumstances, we would not recommend launching an offering without correcting prior guidance that has proved overly optimistic. Updating guidance to reduce the market's expectations ordinarily would not be considered to be an offer under the Securities Act. Even if it were deemed an offer, the company's Exchange Act obligation to communicate with its investors should trump any Securities Act restrictions on offers.

*Q: Economic uncertainty has prevented the company from consistently meeting its guidance. Can the company discontinue providing guidance?*

A: Yes. A number of companies ceased to provide guidance in 2009–2010 as a result of the financial crisis. Bear in mind, however, that there may be an adverse market reaction when a company discontinues giving guidance. One likely consequence is that the spread may widen between the highest and lowest analyst estimates.

*Q: The company just announced an increase in its annual guidance and the market reacted very favorably. How long does the company need to wait before launching an offering?*

A: It depends. The first question is whether the Rule 168 safe harbor is available for the announcement. Did the increase in guidance occur in a regularly scheduled earnings release or call? If not, does the company have a track record of adjusting guidance between earning calls? These would be good facts for the Rule 168 analysis. If the Rule 168 safe harbor is not available, the more prudent course would be to hold off launching the offering for a period of time sufficiently long to break the connection between the increase in guidance and the offering. How long is that? The answer will depend on the extent of the increase in guidance, the company's post-announcement trading activity compared to historical trading patterns and all other relevant facts and circumstances. The analysis under Section 12 is the same. More time between the guidance update and the launch of the offering is better than less time.

*Q: The company just completed its fiscal quarter. Can it disclose preliminary financial data on that quarter in the offering memorandum?*

A: Yes. This is more in the nature of "Recent Developments" disclosure than true guidance and is done all the time. For some good advice on how to provide this type of information, see our *Client Alert* "Recent Developments in Recent Developments—Using Flash Numbers in Securities Offerings," available at <http://>

[www.lw.com/thoughtLeadership/4189-RecentDevelopmentsInRecentDevelopments-Using-Flash-NumbersinSecuritiesOfferings](http://www.lw.com/thoughtLeadership/4189-RecentDevelopmentsInRecentDevelopments-Using-Flash-NumbersinSecuritiesOfferings).

*Q: The company's CFO sent an email to a group of internal personnel indicating that the company will likely miss its previously announced earnings guidance. The CFO's email inadvertently included an industry analyst as an addressee. What should the company do?*

A: Time is of the essence. The company must either publicly disclose the information or obtain from the analyst an express confidentiality agreement, written or oral, within the later of 24 hours or the next trading day's opening bell. Regulation FD requires simultaneous public disclosure for any intentional disclosure of material nonpublic information and prompt public disclosure for any non-intentional disclosure that is made selectively. For this purpose, "prompt" means as soon as is reasonably practicable but in no event later than 24 hours (or before the next opening bell, if later) after a director, executive officer or investor relations official of the company learns about a non-intentional disclosure of material nonpublic information.

*Q: The company has just announced its intention to publicly offer its securities, and the company's CFO wants to discuss the planned public offering during the upcoming earnings call. The CFO will also be discussing guidance and other forward-looking information during the call. Is it OK to mention the offering?*

A: It would be best not to mention the planned offering during the earnings call. The CFO's desire to discuss a recently announced public offering during an earnings call is understandable — after all, investors are likely to be interested in the topic and it was just publicly announced. The rub is the Securities Act's broad (and broadly interpreted) definition of offer. Most companies rely on the press release to notify the market about the upcoming offering and refrain from discussing it during the earnings call other than to refer to the press release.

*Q: The company's offering of securities will affect its previously announced guidance, either through the issuance or repayment of debt that changes interest expense or the increased dilution resulting from more outstanding shares. Should the company update its guidance during the offering?*

A: The impact that the offering will have on the company's income statement and balance sheet is usually disclosed in the offering document, so most companies do not update prior guidance. Since the Rule 168 safe harbor would probably not apply, as discussed above, most companies will wait until their next regular guidance update to factor in the results of the offering.

**Endnotes**

- <sup>1</sup> This *Client Alert* is an update to the *Client Alert* we published on giving good guidance on March 2, 2007.
- <sup>2</sup> This *Client Alert* does not address the SEC's encouragement to include forward-looking information in Management's Discussion and Analysis. See, e.g., *Commission Statement about Management's Discussion and Analysis of Financial Condition and Results of Operations*, Release No. 33-8056 (Jan. 22, 2002), text at note 8 ("Disclosure is mandatory where there is a known trend or uncertainty that is reasonably likely to have a material effect on the registrant's financial condition or results of operations."). In our experience, MD&A does not typically include earnings guidance, although more and more public companies include some kind of forward-looking statements in their MD&A under a caption entitled "Outlook" or something similar.
- <sup>3</sup> Rule 10b-5 generally requires a plaintiff to demonstrate that a defendant acted with *scienter* — that is, either intent to deceive, manipulate or defraud or recklessness (beyond mere negligence).
- <sup>4</sup> These statements include, among other things, projections of revenues, income, earnings, capital expenditures, dividends, capital structure or other financial items, plans and objectives for future operations, products or services and related assumptions. See definition of "forward-looking statement" in Securities Act Section 27A(i)(1)(A) and Exchange Act Section 21E(i)(1)(A).
- <sup>5</sup> Securities Act Section 27A(c)(1)(A)(i); Exchange Act Section 21E(c)(1)(A)(i).
- <sup>6</sup> See Securities Act Section 27A(c)(1)(B) and Exchange Act Section 21E(c)(1)(B).
- <sup>7</sup> The case law underscores the importance of providing detailed, robust and regularly customized cautionary language for each significant forward-looking statement. See, e.g., *Slayton v. American Express*, 604 F.3d 758 (2d Cir. 2010) (finding that the company's forward-looking statement was not immunized by the PSLRA safe harbor's "meaningful cautionary language" prong because the cautionary language in the company's Form 10-Q was too vague to be "meaningful"). For further information on the Slayton opinion and its implication for public companies, see our *Client Alert* "Second Circuit Wades Into the PSLRA Safe Harbor — The Lessons of *Slayton v. American Express* for Forward-Looking Statements," available at <http://www.lw.com/thoughtLeadership/2nd-circuit-addresses-pslra-safe-harbor>.
- <sup>8</sup> Securities Act Section 27A(d); Exchange Act Section 21E(d).
- <sup>9</sup> A duty to update should be distinguished from a duty to correct. The duty to correct potentially applies when a statement that was believed to be correct when made turns out to have been incorrect when made.
- <sup>10</sup> The NYSE and Nasdaq rules for listed companies contain requirements for prompt disclosure of material information, but these requirements have not been understood to apply to internal projections or forecasts of future operating results.
- <sup>11</sup> See *Basic Inc. v. Levinson*, 485 U.S. 224, 239 n.17 (U.S. 1988).
- <sup>12</sup> *Selective Disclosure and Insider Trading*, Release No.33-7881 (Aug. 15, 2000), text following n.47.
- <sup>13</sup> National Investor Relations Institute "Guidance Practices and Preferences, 2012 Survey Report" (Sept. 5, 2012) [hereinafter "NIRI Guidance Survey Report"] (survey results received from approximately 360 NIRI corporate members).
- <sup>14</sup> Regulation G requires SEC-reporting companies that publicly disclose non-GAAP financial measures to provide an accompanying presentation of the most directly comparable GAAP financial measure and a reconciliation of the disclosed non-GAAP financial measure to the most directly comparable GAAP financial measure. See Regulation G, Rule 100(a). The GAAP reconciliation is only required for forward-looking financial measures "to the extent available without unreasonable efforts." *Id.* Rule 100(a)(2). For further information on Regulation G and the use of non-GAAP financial measures, see our *Client Alert* "Adjusted EBITDA Is Out of the Shadows as Staff Updates Non-GAAP Interpretations," available at <http://www.lw.com/thoughtLeadership/non-gAAP-financial-measures>.
- <sup>15</sup> Nearly half of guidance-giving companies provide non-financial guidance, such as statements about market conditions or industry information. However, the number of companies providing non-financial guidance has been decreasing over the past several years. See NIRI Guidance Survey Report.
- <sup>16</sup> Section 11 only applies to guidance if it is included (or incorporated by reference) in the prospectus for a public offering, which is highly unusual. In these rare circumstances, companies should consider the SEC requirements for projections. See Item 10(b) of Regulation S-K.



- <sup>17</sup> For a discussion of the information considered to be part of the Section 11 file and the Section 12 file for purposes of liability under the Securities Act, see our *Client Alert* “The Bought Deal Bible: A User’s Guide to Bought Deals and Block Trades,” available at <http://www.lw.com/thoughtLeadership/the-bought-deal-bible>.
- <sup>18</sup> Companies should carefully consider the consequences of providing or updating guidance in road show meetings if the information provided at the road show is not made public. In addition, companies should also consider the impact on the offering of saying “no comment” in response to questions about previous guidance.
- <sup>19</sup> Section 2(a)(3) of the Securities Act defines the term “offer” expansively to include “every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value.” Given the breadth of this language, it can be difficult to say with certainty what is or is not an offer under this definition. For a thorough review of the law and the lore surrounding “offers,” see our *Client Alert* “The Good, the Bad and the Offer: Law, Lore and FAQs,” available at <http://www.lw.com/thoughtLeadership/how-to-navigate-publicity-and-offers-of-securities>.
- <sup>20</sup> Under Rule 168, “factual business information” means: (i) factual information about the issuer, its business or financial developments, or other aspects of its business; (ii) advertisements of, or other information about, the issuer’s products or services and (iii) dividend notices. “Forward-looking information” means: (i) projections of an issuer’s revenues, income or loss, earnings or loss per share, capital expenditures, dividends, capital structure, or other financial items; (ii) statements about management’s plans and objectives for future operations, including plans or objectives relating to the products or services of the issuer; (iii) statements about the issuer’s future economic performance, including statements generally contemplated by the issuer’s MD&A and (iv) assumptions underlying or relating to the foregoing.
- <sup>21</sup> See *Securities Offering Reform*, Release No. 33-8591 (July 19, 2005) at 63 n.81.
- <sup>22</sup> *Id.* at 64.
- <sup>23</sup> *Id.*
- <sup>24</sup> Compliance with Rule 10b-18 creates a limited safe harbor for share repurchase programs. However, that safe harbor only protects issuers from liability for market manipulation under Sections 9(a)(2) and 10(b) of the Exchange Act. It does not shield against liability for materially false statements and omissions or insider trading.
- <sup>25</sup> The SEC has stated that the “existence of an appropriate policy, and the issuer’s general adherence to it, may often be relevant to determining the issuer’s intent with regard to a selective disclosure.” *Regulation FD Release*, n.90.
- <sup>26</sup> See *SEC Division of Corporation Finance*, Compliance and Disclosure Interpretations, Regulation FD, Question 101.01.

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