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AI Governance Tips For Avoiding Securities Suits

By **Tara Jackson, Christina Russo and Arielle Flamenbaum** (July 10, 2026, 11:27 AM EDT)

Dunn v. Upstart Holdings Inc., a securities class action against an artificial intelligence-powered lending platform filed in the U.S. District Court for the Northern District of California on April 7, highlights a growing reality for public companies: Statements about AI are increasingly being scrutinized not only by regulators, but also by shareholders.

Tara Jackson

The class action alleges that Upstart overstated the accuracy of Model 22, its proprietary AI underwriting model, while that model was overreacting to macroeconomic signals, suppressing loan approvals and weighing on revenue. It is one of the latest signs that AI-related claims, once largely confined to regulatory enforcement, are now generating real litigation exposure.

Christina Russo

For public companies, AI is no longer just a technology topic. It is a disclosure and governance issue that touches securities filings, earnings calls, investor presentations and now consumer-facing representations.

The challenge is not simply whether to talk about AI, but how to do so in a way that is accurate, consistent and aligned with how the business actually operates. As with many emerging areas, the rules have not changed, but the expectations around how companies apply them have.

Arielle Flamenbaum

The Regulatory Baseline: Same Rules, New Lens

While the U.S. Securities and Exchange Commission has not adopted AI-specific disclosure rules, it appears, at least for now, comfortable relying on the existing disclosure framework. That framework, grounded in materiality and anti-fraud principles, is well understood. What is changing is how those principles are being applied.

From a practical standpoint, this means companies should disclose AI where it meaningfully affects the business; statements about AI capabilities or strategy must be accurate and supportable; and known risks, limitations or dependencies should not be omitted. In practice, most companies address AI within existing disclosure categories, including risk factors, management's discussion and analysis, and business descriptions, rather than creating stand-alone sections.

Recent SEC commentary and enforcement activity reinforce that AI-related disclosure is not a niche issue. It is being evaluated in the same way as any other statement that could influence an investor's decision-making.

While there are no AI-specific SEC disclosure rules currently in effect, there are early signs of where expectations may continue to evolve. In December 2025, the SEC's Investor Advisory Committee recommended that companies consider more structured approaches to AI-related disclosure, including defining how AI is used, describing board-level oversight and addressing the impact of AI on operations where such is material.[1]

Although these recommendations are not binding, several commissioners have expressed skepticism about AI-specific mandates, signaling that formal rulemaking in this area is unlikely in the near term. Nonetheless, the recommendations reflect a growing expectation that companies approach AI disclosure with greater clarity and consistency within the existing framework.

The Core Risk: When Messaging Doesn't Match Reality

For many public companies, the real challenge is ensuring that what is being said about AI holds up across all channels.

In practice, scrutiny often arises where there is a disconnect between narrative and execution. Examples include situations where AI is highlighted as a key differentiator while underlying capabilities are still developing, where investor-facing materials emphasize AI-driven growth without addressing dependencies or limitations, or where SEC filings lag behind how prominently AI features in earnings calls or strategy discussions.

These situations are rarely intentional. They are often the result of fast-moving internal developments outpacing disclosure processes. This dynamic is often described as AI washing, in which companies overstate or mischaracterize the role or capabilities of AI in their business.

The SEC has already brought enforcement actions in this area, underscoring that statements about AI are subject to the same anti-fraud standards as any other disclosure. Some companies may take the opposite approach, sometimes referred to as AI hushing, by underemphasizing or omitting AI-related risks or dependencies.

Both dynamics highlight the same underlying principle: Disclosure should present a balanced and accurate picture of how AI is actually used in the business.

Companies should be mindful that AI-related statements are increasingly expected to be verifiable and grounded in current capabilities, rather than forward-looking or aspirational in nature. A helpful discipline is to periodically align internal stakeholders around a simple question: Does our external messaging accurately reflect how AI is actually being used today?

Framing Disclosure Around Business Impact

AI disclosure does not always need to be technical to be effective. Investors are focused on understanding how AI affects the business, not necessarily how it is engineered. As a result, effective disclosure would typically address where AI is being used across the organization; how it contributes to strategy, efficiency or revenue generation; what risks accompany that use; and how those risks are being managed.

This approach keeps disclosure grounded in what matters most, while avoiding both overly generic statements and unnecessary technical detail. As is the case with other disclosures, generic or boilerplate references to AI are unlikely to be sufficient, so disclosures should be tailored to reflect how the AI is actually used and where the real exposure lies.

Third-Party AI: An Increasingly Important Consideration

As companies adopt AI, many are doing so through third-party tools and infrastructure rather than fully proprietary systems.

This is often the right business decision. However, it introduces considerations that are becoming more relevant from both a disclosure and a governance perspective, including reliance on external providers for critical functionality, limited visibility into how models operate or evolve, data usage and confidentiality considerations, and potential differences between vendor representations and actual performance.

Where third-party AI plays a meaningful role in operations or in how the company is presented to investors, it is worth evaluating whether that reliance is appropriately reflected in disclosure.

Governance: Integrating AI Into Existing Oversight Frameworks

AI does not necessarily require a separate governance framework, but it does require a thoughtful approach.

Boards are increasingly expected to understand how AI fits within the company's broader risk profile and to oversee management's approach to those risks. In practice, that means management should be able to clearly map where AI is being used; that key risks, including operational, data and vendor-related risks, should be identified; that oversight responsibilities should be clearly defined; and that boards should receive updates as use cases evolve or expand.

For most public companies, the focus should be on integration, not reinvention. AI should be incorporated into existing risk oversight structures in a way that is proportionate to its significance.

A March report from Institutional Shareholder Services suggests that governance practices in this area are still catching up in adoption.[2]

While AI is now widely embedded across operations, only about 8% of U.S. public companies analyzed currently disclose formal board oversight of AI, and even fewer have paired that oversight with a defined AI policy. At the same time, investor expectations are moving in the opposite direction, with increasing focus on board-level accountability for AI use and risk.

Proxy advisory firms and institutional investors are increasingly evaluating whether boards have directors with AI-relevant expertise and whether proxy statements address AI oversight. The result is a growing gap between adoption and governance that companies should be mindful of as they evaluate both oversight and disclosure.

Internal Use: Practical Guardrails Over Restrictions

AI is increasingly being used internally by employees, officers and directors as part of day-to-day workflows. This creates a different — but equally important — set of considerations, including ensuring that confidential or sensitive information is not shared inappropriately, validating outputs before relying on them in decision-making, understanding that AI-generated content may become part of the company's record, and evaluating whether certain uses raise privilege or confidentiality concerns.

Rather than limiting use, many companies are finding it more effective to implement clear and practical guidelines that enable responsible adoption while managing risk.

Enforcement and Litigation: Established Standards, New Context

Regulators and plaintiffs are focusing more closely on AI-related disclosures, but the underlying legal theories remain familiar. Recent enforcement actions have addressed statements that overstate AI capabilities or readiness, omissions relating to reliance on third-party tools or known limitations, and inconsistencies between public messaging and internal reality.

The SEC's enforcement focus on AI washing began in March 2024 with settled charges against investment advisers Delphia (USA) Inc. and Global Predictions Inc. for false claims about their use of AI, resulting in penalties of $225,000 and $175,000, respectively. And in January 2025, the SEC filed charges against Presto Automation Inc., widely regarded as the first AI-washing case against a public company, for misleading statements about its AI-powered drive-through technology.

Enforcement has continued under the current administration, with the SEC's Cyber and Emerging Technologies Unit identifying AI washing as an immediate enforcement priority. In April 2025, the SEC and the U.S. Department of Justice filed parallel actions against the founder of Nate Inc., a privately held startup, for raising over $40 million through false claims that his company's app used proprietary AI when transactions were actually processed manually.

These cases signal that enforcement will continue to target both outright misrepresentations and more nuanced overstatements about AI capabilities, and that enforcement risk extends to private companies as well as public issuers.

Beyond SEC enforcement, companies should also be aware of emerging private securities litigation risk. Shareholder plaintiffs are beginning to bring claims alleging AI-related misstatements, and the combination of regulatory scrutiny and class action exposure underscores the importance of ensuring AI disclosures are accurate and defensible.

For example, while the allegations in the Upstart class action remain unproven, the case illustrates how an AI-centered growth narrative can become the basis for securities fraud claims when the gap between what a company says about its AI and what that AI actually delivers becomes a material issue for investors.

The lesson is straightforward: If AI is central to how you present your business to the market, the accuracy and consistency of those representations carry real legal risk.

A Practical Path Forward

For public companies, the path forward does not require a complete overhaul. More often, it requires alignment.

A practical approach may include taking inventory of how AI is used across the business; comparing that usage to how AI is described in public communications; refining disclosures to better reflect actual practices and risks; ensuring consistency across SEC filings, earnings calls and investor materials; revisiting insurance coverage, including director and officer, technology errors and omissions, and cyberinsurance, and contractual allocation with AI vendors and channels; confirming that governance structures are keeping pace with adoption; and reviewing how peer companies describe their use of AI to benchmark against evolving disclosure practices.

The companies that navigate this landscape most effectively will be those that maintain a narrative that is clear, credible and sustainable over time. As recent SEC settlements and enforcement actions make clear, the cost of getting AI messaging wrong is no longer theoretical, and public companies would be well served to pressure test their AI disclosures, align internal practices with external messaging and ensure their oversight frameworks keep pace with the technology itself.

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[1] https://www.sec.gov/files/approved-artificial-intelligence-disclosure-recommendation-120425.pdf.

[2] https://insights.issgovernance.com/posts/mind-the-governance-gap-the-state-of-board-oversight-and-ai-policy-in-u-s-companies/.