



**FENWICK & WEST LLP**

*CORPORATE & SECURITIES LAW UPDATE*

## **New Rules Requiring Additional Certifications by CEO and CFO Under Section 302 of Sarbanes-Oxley Act Are In Effect**

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## **New Rules Requiring Additional Certifications by CEO and CFO Under Section 302 of Sarbanes-Oxley Act Are In Effect**

On August 29, 2002, the SEC issued final rules requiring CEO and CFO certifications of annual and quarterly reports. These rules were mandated by Section 302 of the Sarbanes-Oxley Act of 2002 and are effective immediately. The complete text of these rules can be found at:

<http://www.sec.gov/rules/final/33-8124.htm>

The SEC also adopted final rules requiring accelerated filing and website posting of Forms 10-K and 10-Q and requiring accelerated filing of Forms 4. Our update on accelerated filings of Forms 10-K and 10-Q will be available shortly after those rules are promulgated. Our update summarizing the new rules for two-day Form 4 reporting is available at:

[http://www.fenwick.com/pub/corp\\_pubs/SEC\\_Proposes\\_New\\_Rules/SEC\\_8\\_29\\_02.htm](http://www.fenwick.com/pub/corp_pubs/SEC_Proposes_New_Rules/SEC_8_29_02.htm)

### **Who is required to make this certification?**

The principal executive officer and the principal financial officer of every public company are required to make this new certification. If a company has co-CEOs, both would certify. The certification must be made personally and may not be made pursuant to a power of attorney. Each certifying officer should file a separate certification.

The Section 302 certification requirements apply to each company filing periodic reports under Section 13(a) or 15(d) of the Securities Exchange Act of 1934, including foreign private issuers and small business issuers.

### **What reports must be accompanied by a Section 302 certification?**

A Section 302 certification must be included in each annual or quarterly report filed or submitted under either Section 13(a) or Section 15(d) of the Exchange Act. Therefore, these certifications must be included with each Form 10-K and Form 10-Q, Form 10-KSB and Form 10-QSB, and each Form 20-F and 40-F. Certifications must also be included with each amendment to such a form. Certifications are required for filings with the SEC on or after August 29, 2002, as discussed in more detail below.

The SEC is considering whether to extend the Section 302 certification requirement to proxy statements as well. Form 8-K and Form 6-K filings do not require a certification.

This certification is in addition to other required certifications, discussed below.

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**What is the required content of the certification?**

The CEO and CFO each must certify that:

1. The officer reviewed the report being filed;
2. Based on the officer's knowledge, the report does not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by the report;
3. Based on the officer's knowledge, the financial statements, and other financial information included in the report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in the report;
4. The officer and the company's other certifying officers are responsible for establishing and maintaining "disclosure controls and procedures" for the company and have:
  - a. Designed those disclosure controls and procedures to ensure that material information is made known to them, particularly during the period in which the periodic report is being prepared;
  - b. Evaluated the effectiveness of the issuer's disclosure controls and procedures within 90 days before the date the report is filed; and
  - c. Presented in the filed report their conclusions about the effectiveness of the disclosure controls and procedures based on the required evaluation;
5. The officer and the other certifying officers disclosed to the issuer's auditors and audit committee:
  - a. All significant deficiencies in the design or operation of "internal controls" which could adversely affect the issuer's ability to record, process, summarize and report financial data and have identified for the issuer's auditors any material weaknesses in internal controls; and
  - b. Any fraud, whether or not material, involving management personnel or other employees who have a significant role in the company's internal controls; and
6. The officer and the other certifying officers indicated in the filed report whether there were significant changes in internal controls or related areas subsequent to the date of the officers' evaluation of the company's disclosure controls and procedures, including any corrective actions with regard to significant deficiencies and material weaknesses.

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**How do these rules relate to other certifications that the CEO and CFO make?**

CEOs and CFOs will still be required to make the so-called “Section 906 certifications” under the Sarbanes-Oxley Act with each periodic report under the Exchange Act that contains financial statements. Please refer to our earlier update on this subject, at [http://www.fenwick.com/pub/corp\\_pubs/SEC\\_Proposes\\_New\\_Rules/SEC\\_8\\_2\\_02.htm](http://www.fenwick.com/pub/corp_pubs/SEC_Proposes_New_Rules/SEC_8_2_02.htm).

Any of the approximately 1,000 large domestic public companies that were ordered by the SEC on June 27, 2002 to provide CEO and CFO certifications of their past filings are still be required to do so by the due date for those certifications specified by the SEC, if they have not done so already.

**Is it possible to vary the language of the certification at all?**

No. The certification must be made exactly as required for a specific form. For your reference, the texts of the required [Form 10-Q certification](#) and [Form 10-K certification](#) are attached to this update.

**How is the certification filed?**

The certifications must be included in the report when it is filed with the SEC, immediately after the signature page. Issuers should retain an original copy of the signed certification with the original signed copy of the filed report.

**What is covered by the “fair presentation” certification?**

The SEC has indicated that a “fair presentation” of a company’s financial condition, results of operations and cash flows covers all of the financial information disclosed in a report, viewed in its entirety. Therefore, it relates to the company’s financial statements (balance sheets, statements of operations, statements of cash flows), the notes to financial statements, MD&A disclosure and other financial information contained in the filed report. “Fair presentation” means more than compliance with GAAP. In the SEC’s view, it means that appropriate accounting policies have been selected and properly applied, and the financial information disclosed in the report is informative and reflects transactions and events that are necessary to provide a materially complete picture of the company’s financial condition, results of operations and cash flows.

**What are “internal controls”?**

A company’s “internal controls” are the procedures it uses to manage its financial reporting and assets. They are part of the disclosure controls and procedures discussed below. Each public company is required to make and keep books, records and accounts reflecting its transactions. It must maintain a system of internal accounting controls that provide reasonable assurance that:

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- Transactions are executed in accordance with management authorization;
  - Transactions are recorded as necessary to maintain accountability for assets and permit preparation of financial statements in accordance with generally accepted accounting principles;
  - Only authorized access to assets is permitted; and
  - Actual assets are periodically reviewed and appropriate action is taken to account for any differences.

As described by the AICPA, internal controls are a process designed to provide reasonable assurance about the achievement of reliable financial reporting, effective and efficient operations and compliance with applicable laws and regulations.

**What are “disclosure controls and procedures”?**

“Disclosure controls and procedures” is a new term that is intended to capture the concept of procedures required to gather, analyze and disclose all information required to be disclosed in a company’s Exchange Act reports. It includes the concept of “internal controls”, which is described above, but is broader. Disclosure controls and procedures is defined to mean the issuer’s controls and other procedures ensuring that the information required to be disclosed in the issuer’s Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms. They include controls and procedures designed to ensure that relevant information is accumulated and communicated to management, including its CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

Disclosure controls and procedures must include procedures designed to ensure full and timely disclosure in current reports (such as Forms 8-K and 6-K), as well as definitive proxy and information statements, even though Section 302 certifications are not currently required to accompany these reports. These procedures must ensure timely collection and evaluation of information potentially subject to disclosure under the requirements of Regulation S-X, Regulation S-K or S-B and Forms 20-F and 40-F. The procedures should capture information that is relevant to an assessment of the need to disclose developments and risks that pertain to the company’s businesses. They also should cover information that must be evaluated to ensure that the report is not misleading.

The SEC does not require companies to adopt specific disclosure controls and procedures. It expects each issuer to develop processes that are appropriate for its own business and internal management. We have set forth below some procedures that companies may want to consider.

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**Do these rules require companies to put new systems in place?**

Under the new rules, issuers are specifically required to establish and maintain an overall system of disclosure controls and procedures that is adequate to meet their Exchange Act reporting obligations. Some system of disclosure procedures exists at most companies already, as each public company should have in place internal controls for financial reporting purposes as well as some sort of procedures that are designed to collect and digest non-financial information for periodic reports.

In order to facilitate the new CEO and CFO certifications, public company disclosure systems will likely become more formal and more complex. In addition, the new Section 302 certification rules require CEOs and CFOs to take actions that most companies did not include as part of their procedures before now. Therefore, public companies and their CEOs and CFOs will need to evaluate and revise their current disclosure procedures in light of the new requirements.

As part of the evaluation of the company's disclosure controls and procedures, companies will want to make sure that the following procedures are included:

- The CEO and CFO must supervise an evaluation of the effectiveness of the design and operation of the company's disclosure controls and procedures within 90 days prior to the filing of each Form 10-K and Form 10-Q;
- Each Form 10-K and Form 10-Q (or equivalent report) must include the CEO's and CFO's conclusions about the effectiveness of those disclosure controls and procedures, based on the periodic evaluation;
- Each Form 10-K and 10-Q (or equivalent report) must include disclosure by the CEO and CFO of any significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of their most recent evaluation of the company's disclosure controls and procedures; and
- The CEO and CFO must inform the Board's audit committee and the company's independent auditors of any fraud involving management or finance or internal audit personnel, as well as deficiencies or material weaknesses in internal controls.

Other changes in disclosure controls and procedures will vary from company to company, depending on their circumstances. Companies should work with their counsel and auditors to determine what other changes should be made to their disclosure controls and procedures. We have set forth below some procedures to consider.

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**What must CEOs and CFOs do in connection with their certifications and the underlying disclosures?**

CEOs and CFOs making the required Section 302 certifications must, at a minimum, do the following:

- Review drafts of the Form 10-K or Form 10-Q with management personnel responsible for preparing it;
- Review the disclosure requirements applicable to the report being filed; and
- Review the company's disclosure controls and procedures to make certain that they are adequate to ensure that required information comes to their attention.

These executives may also participate in a wide variety of other processes associated with preparation of the filed report, some of which are discussed below.

**What should companies do to assist their CEOs and CFOs with the required certifications?**

Each company should devise backup procedures as part of its disclosure controls and procedures that are appropriate for its management and business. Most companies will establish a "disclosure committee", as described below, which will serve as a clearinghouse for information processing and disclosure compliance – it will be a key element of the company's disclosure controls and procedures. Many companies will undertake some combination of the following procedures, and others, to ensure that their disclosure obligations are satisfied and to provide the CEO and CFO with assurances about the company's disclosure processes:

- Discussions with independent auditors about their review of financial information included in the report;
- Discussions with internal audit personnel about their activities in the past quarter;
- Discussions among the members of the disclosure committee (and others) about the nature of the disclosure issues that arose in the course of the most recent quarter;
- Review of recent management letters from the company's independent auditors, and management responses;
- Review of communications from employees and others that comment on the company's accounting or business;
- Analysis of recent analyst or press commentary on the company's accounting practices or business;
- Requesting backup certificates from responsible subordinate officers;
- Considering the overall quality of disclosures about the company contained in the

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filed report, particularly the completeness of MD&A and the clarity of the disclosure to non-expert readers;

- Documenting the process used to review the filed report;
- Soliciting the views of the company's audit committee, internal auditors, independent auditors and legal counsel about the adequacy of these procedures and the company's other disclosure controls and procedures.

#### **What is a "disclosure committee"?**

The disclosure committee is a general name for a new kind of committee – a management committee responsible for supervising the process of a company's compliance with securities law disclosure requirements. As discussed above, the committee will likely serve as a clearinghouse for information processing and disclosure compliance. Among its duties will be establishing procedures that will enable it to collect information about the company, assess that information in light of applicable disclosure requirements, and make accurate and complete disclosures on a timely basis. For example, one or more members of this committee should be informed promptly about material contracts, major customer or vendor developments, executive officer changes, and acquisitions or dispositions, to ensure that any required disclosures are made in timely fashion.

The SEC has recommended that all public companies organize a committee of this sort, consisting of the company's principal accounting officer, its general counsel or other senior legal staff with disclosure responsibilities, the principal risk management officer, the chief investor relations officer, and other appropriate personnel such as representatives of significant business units. It should work closely with external counsel and auditors as needed. The committee should meet as often as necessary to help the company comply with its disclosure requirements. The disclosure committee should report to the senior management of the company, including the CEO and CFO.

#### **When are these new rules effective?**

The certifications regarding officer review of the report, no material misstatement or omission, and fair presentation of the financial condition, results of operations and cash flows of the company (set forth in paragraphs 1, 2 and 3 of the sample certification) must be made in reports filed on or after August 29, 2002. The certifications regarding disclosure controls and internal controls (set forth in paragraphs 4, 5 and 6) must be made for reports with respect to periods ending after August 29, 2002.

For example, a company with a fiscal year ended June 30, 2002 is required to file a Form 10-K by September 30, 2002. The Section 302 officer certification for that report is not required to contain the certifications about disclosure controls and procedures and internal controls. That company's Form 10-Q for the quarter ending September 30, 2002 will be required to contain all of the certifications.



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**What if I have more questions?**

Should you have any questions about these new requirements, please feel free to contact any member of your Fenwick & West team. You may also contact Horace Nash ([hnash@fenwick.com](mailto:hnash@fenwick.com)), Eileen Robinett ([erobinett@fenwick.com](mailto:erobinett@fenwick.com)), Dan Winnike ([dwinnike@fenwick.com](mailto:dwinnike@fenwick.com)) and Rob Freedman ([rfreedman@fenwick.com](mailto:rfreedman@fenwick.com)), each of whom contributed to the preparation of this update.

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## Form 10-Q Certification

I, [identify the certifying individual], certify that:

1. I have reviewed this quarterly report on Form 10-Q of [identify registrant];
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

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6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses

Date:

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[Signature]

[Title]

\* Provide a separate certification for each principal executive officer and principal financial officer of the registrant. See Rules 13a-14 and 15d-14. The required certification must be in the exact form set forth above.

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## Form 10-K Certification

I, [identify the certifying individual], certify that:

1. I have reviewed this annual report on Form 10-K of [identify registrant];
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
  - a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and
  - c) Presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

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6. The registrant's other certifying officers and I have indicated in this annual report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date:

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[Signature]

[Title]

\* Provide a separate certification for each principal executive officer and principal financial officer of the registrant. See Rules 13a-14 and 15d-14. The required certification must be in the exact form set forth above.