KIRKLAND & ELLIS Alert

Corporate Practice Group **July 2002**

PRACTICES VARY REGARDING DUE DILIGENCE UNDERTAKEN TO SUPPORT PERSONAL CERTIFICATIONS OF SEC REPORTS; SEC ISSUES FURTHER GUIDANCE ON FORMAT FOR CERTIFICATIONS

As we reported in an earlier Alert, on June 27, 2002, the SEC issued an order directing that the CEOs and CFOs of over 900 public companies file sworn statements certifying the completeness and accuracy of their companies' most recent Annual Reports on Form 10-K and all subsequent 10-Qs, 8-Ks and proxy statements. For most companies, this statement will be due on or before August 14, 2002.

Practices Vary Regarding Due Diligence

The SEC has given no guidance concerning what, if any, due diligence should be undertaken in connection with these certifications, which are to be based on the CEO/CFO's "best knowledge." (In the SEC's June 17, 2002 release regarding prospective certification requirements, the SEC staff did suggest that the formation of a disclosure committee may be helpful.)

During the past several weeks, one thing has become clear: there is no "one size fits all" solution. The procedures being followed are as varied as the companies following them.

Some of the procedures we've seen include:

- Forming a disclosure committee along the lines suggested in the SEC's June 17 release;
- Obtaining "roll up" certifications from individuals within the organization responsible for providing the raw back-up data for the SEC reports--sometimes down to the individual plant level;
- Obtaining certifications only from those individuals responsible for preparing the SEC report itself;
- Using internal and/or external resources to perform extensive due diligence to ascertain the accuracy of the facts reported; and
- Relying on the adequacy of the company's existing internal SEC reporting system without obtaining internal certifications or performing extensive additional due diligence.

With regard to the last approach, it is our impression that the SEC believes that, ideally, all public companies would be able to do exactly that. The certification requirement, after all, does not impose a higher standard on companies than that required under existing law--the difference, of course, being that the individual CEOs and CFOs must certify that their company's statements meet the current standard.

With respect to internal "roll up" certifications, some companies have attempted to provide comfort to those employees providing certifications by promising not to take legal action against them absent fraud or other wrongdoing. Others, in an understandable effort to hold the certifier's feet to the fire, have not.

We note that the most rigorous internal certification processes bear some resemblance to due diligence procedures commonly followed in the U.K., Australia and New Zealand, where companies assign one or more individuals responsibility for certifying the accuracy of a section, or even a sentence, of a disclosure document. This practice has been followed in these jurisdictions for many years, and may merit further examination in connection with future certifications.

SEC Issues Guidance Regarding Certification Format

On July 25, 2002, the SEC issued an additional set of Frequently Asked Questions regarding its June 27 order, the text of which is attached. Among these questions was whether companies could modify the form of sworn statement to meet their particular circumstances. The SEC response was that any change to the wording, or any attempt to qualify the wording in a cover letter, will be treated as though the officer was unable to make an unqualified statement and will be identified as such on the SEC website.

On June 29, 2002, the SEC issued a statement indicating that, until publicly disclosed, the sworn statements and any qualifying material should be handled in the same manner as all other material non-public information, i.e., not selectively disclosed in violation of Regulation FD. In addition, the statement indicates that "…in light of the almost certain materiality of the information and the Companies' need to avoid possible misuse of such information…" companies should file an Item 5 Current Report on Form 8-K (or furnish an Item 9 Form 8-K) when the statements are completed and signed, post the statements on their websites and "…take whatever additional steps that they otherwise consider appropriate to ensure broad dissemination of the statements."

Sarbanes-Oxley Act of 2002

President Bush has now signed the Sarbarnes-Oxley Act of 2002 into law. We will be releasing an alert on that subject shortly. We note that the new law prospectively requires CEO and CFO certifications from all public companies, much like the retrospective certifications required for certain large public companies under the June 27 order.

We also note that Section 906 of the Sarbanes-Oxley Act requires a certification, not qualified by knowledge, in each periodic report containing financial statements, that such statement "…fully complies with the requirements of [the Exchange Act] and that information contained in the periodic report fairly presents, in all material respects, the financial condition and results of operations of the issuer." Knowing or willful false certifications are subject to criminal penalties. Section 906 appears to be in effect as of the date President Bush signed the bill into law. **As a result, it appears that, as it now stands, CEOs and CFOs of all public companies must make the Section 906 certification in connection with their upcoming 10-Qs, due for most companies on August 14, 2002.**

Questions

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