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# HRO Alert

## The Sarbanes-Oxley Act of 2002

### FINAL RULES REGARDING CERTIFICATION

Pursuant to a Congressional mandate in the recently enacted Sarbanes-Oxley Act of 2002 (the "SO Act"), on Thursday, August 29, 2002, the SEC adopted final rules relating to the certifications required in annual and quarterly reports of public companies. In addition, the SEC adopted rules relating to the establishment and maintenance of internal controls for information collection and disclosure purposes. Specifically, the new rules require the following:

- Specific certifications by the principal executive officer(s) and principal financial officer(s) in annual and quarterly reports filed on Forms 10-K, 10-KSB, 10-Q, and 10-QSB and comparable foreign issuer Forms 20-F and 40-F; and
- Establishment and maintenance of internal procedures sufficient to provide reasonable assurance that the company is able to collect, process and disclose information required to be disclosed in a company's periodic and current reports filed under the Securities Exchange Act of 1934, as amended (the "Exchange Act").

These rules apply to all issuers that file Exchange Act reports, including small business issuers and foreign private issuers. The SEC noted that Section 302 of the SO Act applies to all public issuers and does not distinguish foreign private issuers or small business issuers from any other type of company.

### Certification

Under the newly adopted rules, the principal executive officer or officers and the principal financial officer or officers, or persons performing similar functions, must now certify in each annual or quarterly report, as well as in each amendment to these reports, that:

- the officer has reviewed the report;
- 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;
- 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;
- the signing officers—
  - are responsible for establishing and maintaining disclosure controls for the company;
  - have designed such disclosure controls to ensure that material relating to the company and its consolidated subsidiaries is made known to such officers, particularly during the period in which the periodic reports are being prepared;

- have evaluated the effectiveness of the company's disclosure controls as of a date within 90 days prior to the filing date of the report; and
- have presented in the report their conclusions about the effectiveness of the company's disclosure controls based on their evaluation as of that date;
- the signing officers have disclosed to the company's auditors and the audit committee of the board of directors (or persons fulfilling the equivalent function)—
  - all significant deficiencies in the design or operation of internal controls which could adversely affect the company's ability to record, process, summarize and report financial data and have identified for the company's auditors any material weaknesses in internal controls; and
  - any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal controls; and
- the signing officers have indicated in the report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls following the date of their evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

The SEC emphasized that the certification goes beyond compliance with generally accepted accounting principles to a broader "standard of overall material accuracy and completeness." In adopting these rules, the SEC stated its view that "a 'fair presentation' of an issuer's financial condition, results of operations and cash flows encompasses the selection of appropriate accounting policies, proper application of appropriate accounting policies, disclosure of financial information that is informative and reasonably reflects the underlying transactions and events and the inclusion of any additional disclosure necessary to provide investors with a materially accurate and complete picture of an issuer's financial condition, results of operation and cash flows."

The new rules refer to both "disclosure controls," a new term, and "internal controls," a preexisting concept under Section 13(b) of the Exchange Act. Disclosure controls broadly include procedures to collect, process and disclose the information required in a company's Exchange Act reports. Internal controls more narrowly encompass company procedures regarding financial reporting.

Accordingly, all public companies must include the above certifications of their principal executive officer(s) and principal financial officer(s) in all future annual and quarterly reports, including all amendments to these reports. Current reports on Form 8-K, proxy statements and information statements are not subject to the certification obligation at this point in time. The certifications are required to appear immediately following the signature sections of the relevant reports. The relevant officers must sign the certifications personally; they may not be signed under a power of attorney. To assist your company in meeting this certification requirement, we have attached the required form of certification to this alert. **Changes to the form of certification are not permitted**, even if seemingly immaterial.

Please note that the certification rule described above is separate from and in addition to the certification obligation under Section 906 of the SO Act, which requires the principal executive officer and principal financial officer to certify, subject to criminal fines and imprisonment, that the each periodic report containing financial statements filed with the SEC "fully complies" with certain requirements of the Exchange Act. Now, when a public company files its periodic reports, each report must contain both of these certifications.

### **Disclosure Controls**

Although not explicitly required under the SO Act, the SEC also adopted rules that require public companies to establish disclosure controls relating to the preparation of periodic and current reports. These rules require each public company to maintain controls and procedures designed to ensure that information required to be disclosed in the company's Exchange Act reports is recorded, processed, summarized and reported in a timely manner. This includes ensuring that information potentially within a company's disclosure obligations is accumulated and communicated to company management, including the principal executive officer(s) and principal financial officer(s), as appropriate to enable them to make timely decisions on whether to disclose the information. The controls should cover current reports and definitive proxy and information statements, even though these documents are not subject to certification. In addition to the creation and maintenance of such disclosure controls, the principal executive officer(s) and principal financial officer(s) must make certifications about the disclosure controls as set forth above.

The SEC did not mandate any form that the disclosure controls or the required evaluation of those controls must take. Instead, the rules allow each company to design a program that is consistent with its business and management practices. The SEC recommended, however, that companies create a committee with responsibility to consider the materiality of information and determining disclosure obligations on a timely basis. Furthermore, the controls should be designed to ensure timely collection and evaluation of information potentially subject to disclosure under the various rules applicable to periodic reports (such as Regulations S-X and S-K).

In theory the concept of such internal controls seems simple and the need for their existence obvious. However, the practical fact remains that public companies must now develop such internal controls with little or no guidance from the SEC. Please feel free to contact us to discuss different methods for implementing such a program.

### **How HRO Can Help**

In the months that follow, we anticipate a significant degree of discussion relating to the rules discussed in this Alert and other aspects of the SO Act. If you would like to discuss any of these issues and how they will impact your company and its practices, we encourage you to contact any of the persons listed in this Alert. Moreover, in the next few weeks you will be receiving an invitation to attend a free seminar relating to the SO Act and resulting securities law changes.

**CERTIFICATIONS\***

I, \_\_\_\_\_, certify that:

1. I have reviewed this [annual] [quarterly] report on Form [10-K] [10-Q] of \_\_\_\_\_;
2. Based on my knowledge, this [annual] [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 [annual] [quarterly] report;
3. Based on my knowledge, the financial statements, and other financial information included in this [annual] [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 [annual] [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 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] [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 [annual] [quarterly] report (the "Evaluation Date"); and
  - c) presented in this [annual] [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 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

6. The registrant's other certifying officers and I have indicated in this [annual] [quarterly] 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: \_\_\_\_\_

\_\_\_\_\_  
Name:

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.