

**SEC PROPOSES NEW RULES RELATING  
TO 8-K DISCLOSURE AND OFFICER CERTIFICATION**

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The Securities and Exchange Commission (the "SEC ") recently issued two releases with proposed rule changes on corporate disclosure.

On June 14, 2002, the SEC issued a release<sup>1</sup> that proposes new measures aimed at improving the quality of disclosure in annual reports, quarterly reports and current reports on Form 8-K and increasing investor confidence. The SEC proposes rule changes that would:

- require a company's principal executive officer and principal financial officer to certify that, to their knowledge, the information in the company's quarterly and annual reports is true in all important respects and that the reports contain all information about the company of which they are aware that they believe is important to a reasonable investor; and
- require a company to:
  - maintain procedures to provide reasonable assurance that the company is able to collect, process and disclose the information required in the company's quarterly reports, annual reports and current reports on Form 8-K;
  - review and evaluate these procedures on an annual basis; and
  - include certification by the company's principal executive officer and principal financial officer in the company's annual report that such officers have reviewed the result of the company's evaluation of the procedures.

The release states that the proposal is consistent with President Bush's objective to make corporate leaders more accountable to the investing public and to bolster investor confidence in the securities market.

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<sup>1</sup> SEC Release No. 34-46079 (June 14, 2002, modified June 18, 2002).

On June 17, 2002 the SEC issued a second release<sup>2</sup> aimed at providing investors with better and faster disclosure of important corporate events. The proposed rules would:

- add 11 new items that would be required to be included in a company's current report on Form 8-K;
- move two disclosure items currently required to be included in companies' annual and quarterly reports to Form 8-K;
- amend several of the existing Form 8-K disclosure items;
- shorten the filing deadline for Form 8-K to two business days after a triggering event (the current deadline is five business days or 15 calendar days depending on the event); and
- create a new safe harbor for certain violations of the Form 8-K filing requirements and grant an automatic two business day extension of the filing deadline to companies providing proper notice on Form 12b-25 of an inability to timely file a particular Form 8-K.

The rules in each release are subject to public comment on or before 60 days after publication of the release in the Federal Register. The SEC may, after the applicable comment period, adopt the proposed rules or adopt modified rules or make additional proposals based on the comments received.

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**MEASURES TO IMPROVE THE  
QUALITY OF DISCLOSURE**

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**CERTIFICATION OF DISCLOSURE IN QUARTERLY AND ANNUAL REPORTS**

Under the proposed rules outlined in the first release a company's principal executive officer and principal financial officer each would have to certify in the company's annual report that:

- he or she has read the report;

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<sup>2</sup> SEC Release Nos. 33-8106; 34-46084 (June 17, 2002, modified June 18, 2002).

- to his or her knowledge, the information in the report is true in all important respects as of the end of the period covered by the report; and
- the report contains all information about the company of which he or she is aware that he or she believes is important to a reasonable investor as of the end of the period covered by the report.<sup>3</sup>

The certification would also include a statement that information is “important to a reasonable investor” if:

- there is a substantial likelihood that a reasonable investor would view the information as significantly altering the total mix of information in the report; and
- the report would be misleading to a reasonable investor if the information was omitted from the report.<sup>4</sup>

The certification is limited to the knowledge of the principal executive officer and principal financial officer and to their belief as to whether information would be important to a reasonable investor. These officers would not, as a result of the certification requirement, have to separately inquire as to information not known to them. Officers should however, where appropriate, make other inquiries including inquiries regarding disclosure they do not understand or as to the materiality of information known to them.

Officers who provided false certification could be subject to both SEC and private actions for violations of the Securities Exchange Act of 1934 (the “Exchange Act”). The SEC does not believe the proposed certification would “change the underlying liability standard as to materiality or create an unacceptable risk of increased liability” for the certifying officers. These officers are already subject to potential liability as signatories<sup>5</sup> of quarterly and annual reports

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<sup>3</sup> The certification in a quarterly report would be similar but would take account of the narrower disclosure required for such reports.

<sup>4</sup> It is the SEC’s intent that the certification’s standard of materiality follows current case law and does not establish a new standard of materiality.

<sup>5</sup> The proposed certification would not change the current signature requirements for quarterly and annual reports. Form 10-Qs must be signed by an authorized representative of the company and by the principal financial officer or principal accounting officer. A company may or may not choose to have its principal executive officer sign as the duly authorized representative. Form 10-Ks must be signed by the company’s principal executive officer, principal financial officer, its controller or principal accounting officer and by at least the majority of the board of directors.

and can be liable under general antifraud standards. The SEC believes the certification requirement would cause the company's principal executive officer and principal financial officer to participate more actively in the preparation of the quarterly and annual reports and to review such reports more carefully.

#### **INTERNAL CONTROLS AND PROCEDURES**

In order to ensure that companies subject to the reporting requirements of the Exchange Act maintain adequate procedures for gathering, analyzing and disclosing information required to be included in their annual reports, quarterly reports and periodic reports, the SEC has proposed that such companies be required to:

- maintain sufficient procedures to provide reasonable assurances that the company is able to collect, process and disclose, within the time periods specified in the SEC's rules and forms, the information required to be disclosed in the annual reports, quarterly reports and periodic reports; and
- prior to the filing of its annual report,
  - conduct an evaluation of the effectiveness of these procedures; and
  - ensure that the results of such evaluation are reviewed by the company's principal executive officer, principal financial officer and board of directors.

The release does not require any particular procedures for conducting the evaluation. The SEC does, however, recommend that a company create a committee with responsibility for considering the materiality of information and determining disclosure obligations on a timely basis. The committee would report to senior management, including the principal executive officer and principal financial officer. Additionally, the SEC states that it would be beneficial if the company's board of directors also participates in the review of the evaluation of procedures.

The proposed rule was designed to ensure that a company is capable of producing accurate disclosure. According to the release, a company that failed to maintain adequate procedures, review them and comply with the rule could be subject to SEC action for violating the Exchange Act even where the failure did not cause flawed disclosure.

#### **CERTIFICATION AS TO REVIEW OF EVALUATION OF REPORTING PROCEDURES IN ANNUAL REPORTS**

The proposed rules would require a company's principal executive officer and principal financial officer to certify in the company's annual report that they have reviewed the results of their company's evaluation of the procedures maintained by the company to collect, process

and disclose the information required in the company's annual report, quarterly report and current reports on Form 8-K.

#### **APPLICATION TO SMALL ENTITIES AND FOREIGN REGISTRANTS**

The proposed rules in the first release described above would apply to companies of all sizes, including small business issuers. While the SEC believes the proposed rules would impose a significant burden on small companies, comments have been requested on whether small business issuers should be excluded from the rules.

The proposed rules would not apply to foreign private issuers subject to the reporting requirements of the Exchange Act. However, in the release the SEC requests comments on whether the proposed rules should apply to foreign registrants.

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#### **PROPOSED FORM 8-K CHANGES**

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The second release proposes to add 11 new items to the list of events that would require a company to file a current report on Form 8-K. The SEC believes each of these events are presumptively of such importance to investors that prompt disclosure is necessary and that more prompt disclosure of significant events would reduce the opportunities for deception and manipulation that stem from delayed disclosure. The proposal is consistent with the Exchange Act's purpose of establishing a system of continuing disclosure for companies that issue securities to the public.

The following is a list of the new disclosure items the SEC proposes to add to Form 8-K:

- Entry into a material agreement or material amendment to a material agreement not made in the ordinary course of business;
  - includes letters of intent and other non-binding agreements
- Termination of a material agreement not made in the ordinary course of business;
- Termination or reduction of a business relationship with a customer that constitutes a specified amount of the company's revenues;
  - disclosure is triggered when the termination or reduction equals 10% or more of the company's consolidated revenues during its most recent fiscal year
- Creation of a direct or contingent financial obligation that is material to the company;

- includes disclosure of registered sales of debt securities, private placements and bank loans and contingent obligations such as guarantees or keepwells
- Events triggering a direct or contingent financial obligation that is material to the company, including any default or acceleration of an obligation;
  - this item would replace the requirement to report defaults upon senior securities in Form 10-Q
- Exit activities including material write-offs and restructuring charges;
- Any material charge or impairment to one or more of a company's assets, including an impairment of securities or goodwill;
- A change in a rating agency decision, issuance or a credit watch, change in a company outlook or refusal to assign a credit rating after the company requested one;
  - only applies if the rating agency notifies the company of its intended action and the company has provided information (other than annual and quarterly reports) to the rating agency
- Movement of the company's securities from one exchange or quotation system to another, delisting of the company's securities from an exchange or quotation system, or a notice that a company does not comply with a listing standard;
- Conclusion by the company or notice from its independent accountant that security holders no longer should rely on the company's previously issued financial statements or a related audit report; and
- Any material limitation, restriction or prohibition on acquiring, disposing or converting participants' holdings, including the beginning and end of lock-outs periods, regarding the company's employee benefit, retirement and stock ownership plans;
  - filing is not triggered by temporary trading restrictions on senior officers and directors due to the possession of material non-public information.

The SEC also proposes to move the following two items from other Exchange Act reports to Form 8-K:

- Unregistered sales of equity securities by the company; and
- Material modifications to rights of holders of the company's securities.

Finally, the SEC proposes to expand the current Form 8-K item that requires disclosure about the resignation of a director . Currently disclosure is required only if a director departs as a result of a disagreement, provides a letter to the company describing the disagreement and requests the company disclose the matter publicly. Under the proposal, disclosure would be triggered if a director:

- resigns or chooses not to stand for reelection because of a disagreement with the company known to an executive officer on any matter relating to the company's operations, policies or practices; or
- is removed for cause from the board of directors.

Under these circumstances, if the director provides the company with any written correspondence concerning the resignation or removal, the company would have to summarize it and file copies of such correspondence as an exhibit to the Form 8-K. The company would also be required to provide the director with a copy of the Form 8-K no later than the business day following its filing with the SEC. The director would need to provide the company with a letter addressed to the SEC stating whether he or she agrees with the disclosure and if not, stating the respects in which he or she disagrees. The director's letter would need to be filed with SEC as an exhibit by amendment to the Form 8-K.

Disclosure would also be required for:

- the resignation or removal of a director for any reason other than as a result of a disagreement or for cause;
- the appointment of certain key officers;<sup>6</sup>
- resignation or termination of certain key officers from their current position (including reassignment to another position); and
- election of a new director, except by vote of security holders at an annual meeting.

The proposal also would combine the current Form 8-K item regarding a change in a company's fiscal year with a new requirement to disclose any material amendment to a company's articles of incorporation or bylaws not disclosed in a proxy statement or information statement filed by the company.

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<sup>6</sup> A company's principal executive officer, president, principal financial officer, principal accounting officer or principal operating officer (or anyone serving in an equivalent position).

In an effort to improve disclosure, many of the proposed new Form 8-K items would require companies to provide management's analysis of the expected effect of the event on the company. The release encourages companies to provide quantitative information whenever possible.

The SEC recognizes that some events might fall under more than one item in Form 8-K. In those circumstances, a company only needs to file only one report but must list all relevant item numbers.

The SEC expects the proposed changes to Form 8-K, if adopted, would become effective 60 days after adoption of the final rule. The amendments would not apply to events that occurred prior to the effectiveness of the rule change.

#### **APPLICATION OF PROPOSED FORM 8-K CHANGES TO FOREIGN PRIVATE ISSUERS**

Foreign private issuers that are subject to the periodic reporting requirements under the Exchange Act furnish reports on Form 6-K. The information that must be furnished under Form 6-K is that information which is material with respect to an issuer and its subsidiaries. The form contains a list of matters that may be considered material. The list generally tracks the subject matters contained in Forms 10-Q and 8-K prior to the proposal. The SEC is not proposing amending Form 6-K to require disclosure of specific items.

#### **SHORTENED FILING DEADLINE FOR FORM 8-K**

With the advent of the EDGAR electronic filing system companies can file their documents with the SEC within significantly shorter timeframes. Accordingly, the proposed amendments would require companies to file current reports on Form 8-K within two business days of a triggering event.<sup>7</sup>

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<sup>7</sup> The two business day amendment would not affect the filing deadline for disclosures under Regulation FD, voluntary disclosures or the proposed deadline under the recently proposed new Item 10 of Form 8-K (reports on Form 8-K related to transactions in a company's securities by its officers and directors).



## LATE FILING

The proposed rules provide a safe harbor for companies that fail to file a required Form 8-K within the deadline. Under the safe harbor a company would not be liable under Section 13(a) or 15(d)<sup>8</sup> of the Exchange Act if:

- on the date the Form 8-K was due, the company maintained sufficient procedures to provide reasonable assurance the company is able to collect, process and disclose, within the specified period, the information required to be disclosed by Form 8-K (see the above discussion regarding internal controls and procedures);
- no officer, employee or agent of the company knew, or was reckless in not knowing, that a report on Form 8-K was required to be filed; and
- once an executive officer of the company became aware of its failure to file, the company promptly (and not later than two business days after becoming aware of the failure) filed a Form 8-K containing the required information and stating the date when the report should have been filed.

A company that fails to file a Form 8-K in a timely manner would be precluded from using short form registration statements even if it fell within the safe harbor. However, the release proposes amending Rule 12b-25 and Form 12b-25 to allow a company not to lose its eligibility to use short form registration statements if the company:

- files a Form 12b-25 (Notification of Late Filing)<sup>9</sup> within one business day after the Form 8-K is due; and
- files the Form 8-K within two business days after the original due date.

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If you have any questions concerning the releases, please contact Risë Norman (rnorman@stblaw.com), Vincent Pagano (vpagano@stblaw.com), John Tehan (jtehan@stblaw.com) or Jessica Gross (jgross@stblaw.com) of our firm at (212) 455-2000.

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<sup>8</sup> The safe harbor would not affect the obligation to disclose information on Form 8-K for purposes of determining liability under Section 10 and Rule 10b-5 of the Exchange Act and Sections 11, 12 and 17 of the Securities Act.

<sup>9</sup> The company must represent in the Form 12b-25 that the Form 8-K could not be filed in a timely manner without unreasonable effort or expense.

