SIMPSON THACHER

# DISCLOSURE CONTROLS AND PROCEDURES

JOHN D. LOBRANO, JOHN G. FINLEY, ARTHUR D. ROBINSON,
RAYMOND, W. WAGNER AND ALEXIA DELICARI
SIMPSON THACHER & BARTLETT LLP

OCTOBER 21, 2002

## SIGNIFICANCE OF DISCLOSURE CONTROLS AND PROCEDURES

In recent months, U.S. securities law and regulation has changed significantly as a result of the enactment of the Sarbanes-Oxley Act of 2002 and issuance or modification of a host of Securities and Exchange Commission rules that, taken together, are intended to improve the quality of corporate disclosure and accelerate the flow of public information to investors.[1] Among the new rules issued are rules contemplated by Section 302 of the Sarbanes-Oxley Act which require senior officer certifications and the establishment of "disclosure controls and procedures" by issuers that file annual and quarterly periodic reports under the Securities Exchange Act of 1934. These new rules place considerable emphasis on the concept "disclosure controls and procedures" as part of the reforms intended to address the abusive corporate practices evidenced by Enron and other companies.[2]

---

1 This memorandum supplements our memorandum dated September 6, 2002 entitled *"SEC Adopts New CEO/CFO Certification Rules Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002,"* as well as our memoranda more generally regarding the Sarbanes-Oxley Act dated July 31, 2002 entitled *"Sarbanes-Oxley Act of 2002: CEO/CFO Certifications, Corporate Responsibility and Accounting Reform;"* August 8, 2002 entitled *"Sarbanes-Oxley Act of 2002: Supplemental Memorandum No. 1;"* and August 9, 2002 entitled *"Sarbanes-Oxley Act of 2002 Supplemental Memorandum No. 3 – Registered Investment Companies."* These memoranda are available upon request or at our website: *www.simpsonthacher.com.*

2 Registered investment companies that file reports under the Exchange Act must similarly comply with the Section 302 certification requirements and must maintain disclosure controls and procedures. See section entitled *"Registered Investment Companies"* in this memorandum. However, due to the unique structure and operations of investment companies, the design and operation of disclosure controls and procedures will necessarily be somewhat different from what is described in this memorandum. Please contact your relationship partner regarding the application of disclosure controls and procedures to registered investment companies.

New Rules 13a-14 and 15d-14 under the Exchange Act require principal executive officers and principal financial officers of reporting companies (other than asset backed issuers) to certify in each periodic report filed on Forms 10-K, 10-KSB, 10-Q, 10-QSB, 20-F or 40-F relating to a fiscal period ended after August 29, 2002, among other things, that those officers:

- are responsible for establishing and maintaining disclosure controls and procedures for their companies;
- have designed such disclosure controls and procedures to ensure that material information relating to their companies, including their consolidated subsidiaries, is made known to them by others within those entities;
- have evaluated the effectiveness of such controls and procedures within 90 days prior to the filing of the applicable report; and
- have presented in the applicable report the conclusions of their evaluation.

In addition, new Rules 13a-15 and 15d-15 under the Exchange Act require reporting companies (other than asset backed issuers) to maintain disclosure controls and procedures and evaluate the effectiveness of their design and operation within 90 days prior to the filing of each annual and quarterly report as to which certifications must be made pursuant to Rule 13a-14 or 15d-14.[3]

These new rules, in combination with other SEC initiatives such as the phased shortening of the deadlines for filing by certain reporting companies of Exchange Act reports and real time disclosures by reporting companies as contemplated by the Sarbanes-Oxley Act, are imposing significant new obligations on reporting companies.[4] These obligations will make it essential that reporting companies reassess their disclosure controls to ensure that, in conformity with

---

[3] Rules 13a-15 and 15d-15 also require that disclosure controls and procedures be designed to ensure full and timely disclosure in other reports filed under the Exchange Act, including current reports and definitive proxy and information statements, even though the certification requirements of Rules 13a-14 and 15d-14 do not apply to those disclosure documents.

Pursuant to Section 302 of the Sarbanes-Oxley Act and new Rules 13a-15 and 15d-15, the SEC has also amended Form 10-K by adding a new Item 14 and Form 10-Q by adding a new Item 4. These amendments incorporate new Section 307 of Regulation S-K requiring disclosure of the conclusions of CEO's and CFO's about the effectiveness of reporting companies' disclosure controls and procedures based on their evaluation as of a date within 90 days of the filing date and disclosure about significant changes in internal controls. The SEC also amended Forms 10-KSB and 10-QSB and Forms 20-F and 40-F in a similar manner.

[4] The accelerated filing deadlines apply only to reporting companies that file annual reports on Form 10-K and quarterly reports on Form 10-Q with a public float of at least $75 million, have been a reporting company for at least 12 months and have previously filed at least one annual report; the new rules do not apply to foreign governments, foreign private issuers, registered investment companies and small business issuers.

the new rules, they have effective mechanisms for the timely collection, analysis and dissemination of material information.

## DEFINITION OF DISCLOSURE CONTROLS AND PROCEDURES

Rules 13a-14 and 15d-14 under the Exchange Act define "disclosure controls and procedures" to mean:

> "controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the [Exchange] Act is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the [Exchange] Act is accumulated and communicated to the issuer's management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure."

In essence, disclosure controls and procedures are intended to implement and make systematic a process by which information relating to a reporting company is identified, assembled and presented to responsible parties on a timely basis for an analysis of whether public disclosure in an Exchange Act filing is required or desirable.

The SEC release[5] adopting Rules 13a-14 and 13a-15 and 15d-14 and 15d-15 (the "Adopting Release") emphasizes that disclosure controls and procedures are broader than the pre-existing concept of internal controls, which relate to a company's financial reporting and control of its assets. In contrast to internal controls, disclosure controls and procedures relate to financial *and* non-financial information. Most internal controls are a subset of disclosure controls and procedures, and the characteristics that make for good internal controls – segregation of duties and strong monitoring functions – will also be an integral part of effective disclosure controls and procedures. Indeed, internal controls are a good model to use in the development of effective disclosure controls and procedures because both relate to the design and implementation of information management systems intended to yield reliable information in a timely fashion. In effect, by imposing a requirement that reporting companies implement effective disclosure controls and procedures, the SEC has extended the concept of internal

[5] SEC Release Nos. 33-8124 and 34-46427 (August 28, 2002).

controls, which lie at the heart of the effective processing of a large quantity of financial information, to non-financial information as well.

## THE BASIC PRINCIPLES OF INTERNAL CONTROLS

The basic principles of internal controls, which are set forth in the Committee of Sponsoring Organizations of the Treadway Commission's report *Internal Controls – Integrated Framework* (the "COSO Report"), provide a framework for building effective disclosure controls and procedures. Such principles consist of:

- ***control environment***, which defines the tone and way of operation of the organization and comprises the integrity, ethical values and competence of the people in the organization, the manner in which management assigns authority and responsibility, the way in which it organizes its human resources and the attention and direction provided by the board of directors and audit committee;

- ***risk assessment***, which is the identification and analysis of relevant risks to the achievement of specified objectives and forms a basis for determining how the risks should be managed;

- ***control activities***, which are the policies and procedures put in place to ensure management's directives are carried out; these policies and procedures permeate the entire organization;

- ***information and communication***, which are systems capturing and communicating relevant information in a timely manner and allow information to flow through an organization; and

- ***monitoring***, which is intended to ensure that internal controls are performing as intended; it can be accomplished through ongoing monitoring and separate evaluations by management.

Disclosure controls and procedures will necessarily be tailored to the circumstances of a particular company including the scope and nature of its activities. While precise disclosure controls and procedures appropriate for a particular company must be addressed on an *ad hoc* basis, we believe that including certain general processes in a set of disclosure controls and procedures should enable a company's disclosure controls and procedures to satisfy the requirements of Rules 13a-15 and 15a-15. In addition, these processes provide a basis for CEO's and CFO's to file the Section 302 certifications required by Rules 13a-14 and 15a-14. We recommend, in establishing disclosure controls and procedures, a company incorporate in one form or another the following elements:

- a corporate culture that emphasizes good disclosure (reflects the principle of control environment);
- a disclosure committee (reflects the principle of control activities);
- internal reviews of business areas that need to be monitored for disclosure issues (reflects the principle of risk assessment);
- a process for drafting disclosure (reflects the principle of information and communication); and
- an evaluation process (reflects the principle of monitoring).

## ESTABLISHMENT OF DISCLOSURE CONTROLS AND PROCEDURES

The SEC has acknowledged that there is no "one-size-fits-all" approach to establishing effective disclosure controls and procedures and has not prescribed any specific disclosure controls and procedures. Rather, the SEC expects "each issuer to develop a process that is consistent with its business and internal management and supervisory practices." We recommend that companies begin by documenting, evaluating and building upon their existing practices for compiling and assessing information for their Exchange Act reports. Although Rule 13a-15 and Rule 15a-15 require disclosure controls and procedures to be maintained only for Exchange Act reports, we recommend that companies design their disclosure controls and procedures to apply also to registration statements filed under the Securities Act of 1933 and private offering memoranda.[6] We further recommend that companies consult with counsel to determine the extent to which a company's disclosure controls and procedures should be extended to other forms of communication to shareholders and the investment community.

A company's existing process for preparing Exchange Act reports would most likely already comprise a form of disclosure controls and procedures, although these current controls and procedures may be informal and require reconsideration and revision in light of the new requirements. Documentation of a company's current process will better enable it to evaluate areas where the process can be improved. Before revising a company's disclosure process, the company should assess the risks and challenges that the company faces. By analyzing the "risk factors" for its business, whether financial, regulatory, technological or competitive, a company

[6] In the context of shelf take-downs by certain seasoned issuers, following abbreviated disclosure controls and procedures may be appropriate. For example, the entire disclosure committee may not need to approve the disclosure in a prospectus supplement. Rather, approval of that disclosure by a subgroup of the disclosure committee may be sufficient.

can more effectively design its disclosure controls and procedures to allocate appropriate resources to areas where information management is most critical.

We provide below a list of actions that reporting companies may wish to consider in improving their disclosure controls and procedures. Companies should consider the suggested actions below in light of their particular businesses and management and operating practices. Some companies may have more improvements to consider than others. Some companies, for example, may only be able to evaluate information at specified intervals, such as at month or quarter-end. Other companies may already have the ability to evaluate business information on a weekly, or even daily, basis. Some companies may have informal systems that provide frequent information but need to be upgraded to assure reliability.

Each company should decide what set of disclosure controls and procedures is most suitable for it, recognizing that disclosure in the future will need to be made on a more comprehensive and accelerated basis. As a result, disclosure controls and procedures should be scalable – that is, capable of meeting the company's requirements as the company grows and disclosure requirements change. We recommend that each company formalize and document, at least in a general way, the disclosure controls and procedures that it adopts. In addition to providing a record that such processes exist, this documentation will create a base line that can be instrumental in performing the requisite periodic evaluation of the company's disclosure controls and procedures.

**1. ESTABLISHING A CORPORATE CULTURE EMPHASIZING GOOD DISCLOSURE.**

***Role of Senior Management.*** Corporate culture should emphasize the importance of good disclosure, an effective disclosure process and the company's code of ethics. The tone at the top of an organization is an essential element in establishing a corporate culture conducive to effective disclosure controls and procedures. Senior management, including the CEO and CFO, may promote the principles of good disclosure through oversight of and involvement in the company's disclosure controls and procedures, as well as through attitude and behavior acknowledging the importance of complete, accurate and timely disclosure.[7]

**2. CREATING A DISCLOSURE COMMITTEE.**

***SEC Recommendation.*** The SEC has recommended that reporting companies create a disclosure committee to consider the materiality of information and determine disclosure

---

[7] See the COSO Report: "The chief executive is ultimately responsible and should assume 'ownership' of the system. More than any other individual, the chief executive sets the 'tone at the top' that affects the integrity and ethics and other factors of a positive control environment. In a large company, the chief executive fulfills this duty by providing leadership and direction to senior managers and reviewing the way they're controlling the business… [I]n a cascading responsibility, a manager is effectively a chief executive of his or her sphere of responsibility."

obligations on a timely basis. The SEC contemplates that the disclosure committee would report to senior management, including the CEO and CFO. We believe that disclosure committees already exist informally in most reporting companies.

***Purpose.*** The disclosure committee should be responsible for assisting the CEO and CFO in designing, establishing, maintaining, reviewing and evaluating the company's disclosure controls and procedures for which the CEO and CFO bear the express responsibility. The disclosure committee should evaluate all disclosure issues and discuss important disclosure issues with senior management, including the CEO and CFO. In addition, the disclosure committee should be responsible for preparing, or assisting in the preparation of, the disclosure that will be publicly filed or distributed. We recommend that the disclosure committee adopt a charter, a form of which is attached as Appendix A. We recommend that disclosure committee charters be prepared with sufficient specificity to ensure that the committee's responsibilities are clearly delineated but not be so detailed as to be prejudicial in the context of a disclosure lawsuit.

***Members.*** The members of the disclosure committee should have the necessary qualifications and experience, access to information and stature within the company to allow them to identify and evaluate disclosure issues. The Adopting Release indicates that the disclosure committee could include the principal accounting officer or controller, the general counsel and/or other senior in-house lawyer responsible for SEC disclosure matters, the principal risk management officer, the chief investor relations officer and any other officers or employees that a company deems appropriate. The disclosure committee should also include the principal draftspersons of the company's Exchange Act filings so that such persons are fully informed of all corporate developments. To be effective, however, we believe that a disclosure committee should not be unduly large. Members of the disclosure committee should receive training in SEC reporting and disclosure practices and be updated regularly on changes to relevant accounting policies and disclosure requirements.

Some filings, particularly some filings on Form 8-K, may require immediate action or may include sensitive information. For these disclosure documents, companies may decide to have either the CEO or CFO, or a subgroup of committee members, including at least one attorney with expertise in SEC rules and regulations with respect to disclosure and at least one certified public accountant with expertise in accounting and SEC financial reporting, to act in lieu of the whole committee.

***Chairperson and Coordinator.*** A member of senior management should be appointed chairperson of the disclosure committee. The chairperson should be designated by the CEO and/or CFO. In addition, a member of the disclosure committee should act as the coordinator of the activities of the disclosure committee and disclosure controls and procedures. The coordinator would be responsible for ensuring that the disclosure controls and procedures are properly followed on a timely basis. The coordinator should be a lawyer or a senior member of the finance department. The coordinator needs to be familiar with all SEC disclosure

requirements, i.e. financial and non-financial, and able to dedicate the necessary time to accomplish his or her responsibilities.

**3. CONDUCTING INTERNAL REVIEWS.**

***Process.*** The process by which disclosure issues are identified and communicated to the disclosure committee will vary from company to company, based on a company's business and management and operating practices. One approach could involve the conduct of internal reviews by the disclosure committee on a regular basis. In conducting such a review, the disclosure committee could consider taking the following steps:

- *Identification of Sensitive Areas of the Business*. Identify the areas of the company's business that need to be monitored for disclosure issues. Consideration should be given as to whether this identification process should be done in consultation with the audit committee so that the committee's concerns may be addressed as part of the normal disclosure process. Sensitive areas could include particular business units or locations, litigation, insurance and risk management, regulatory matters, off-balance sheet arrangements, reserves, R&D and intellectual property.

- *Identification of Key Individuals.* Identify individuals within each sensitive area of the company's business, such as heads and chief financial officers of business units and officers responsible for particular business functions, who will best be able to identify potential disclosure issues within their areas.

- *Creation of Communication Channels.* Make such individuals responsible for communicating all potential disclosure issues to the disclosure committee at, for example, regularly scheduled meetings of the disclosure committee. Companies that use an internal review process in connection with the preparation of their budgets may want to use that process as a model.

- *Determination of Subject Disclosures.* Determine which disclosure documents, other than reports filed under the Exchange Act, registration statements filed under the Securities Act and private offering memoranda, are the responsibility of the disclosure committee. These documents could include communications to the investment community, including reports and letters to shareholders, earnings and guidance releases (if not filed), presentations to analyst conferences and the like. Each company will make that determination based on its business, size and other factors.

- *Evaluation of Disclosure Issues*. Evaluate potential disclosure issues. In doing so, the disclosure committee may choose to talk to officers or employees within the company that have requisite knowledge regarding the issues, as well as to the outside auditors and outside counsel, as applicable. The disclosure committee

should discuss the outcome of the evaluation with the particular individuals that communicated the relevant issues to the disclosure committee. These individuals and the disclosure committee should be in agreement with respect to whether or not an issue that has been identified needs to be disclosed.

- *Interview of Audit Firm*. Interview the audit firm to determine the effectiveness of the company's internal control system. Statement on Auditing Standards ("SAS") No. 61, *Communication with Audit Committees*, as amended by SAS No. 90, *Audit Committee Communications*, would be a useful roadmap to the disclosure committee in conducting the interview. The head of internal audit, if not a committee member, should also be interviewed, and the committee members should familiarize themselves with recent management letters delivered to the audit committee by the auditors or the contents of any other presentations to the audit committee relating to internal controls.

- *Discussion with CEO and CFO*. Discuss important disclosure issues with the CEO and CFO. It may be advisable for the CEO and CFO to participate in committee meetings at which important issues are discussed.

- *Discussion with the Audit Committee*. The CEO and the CFO, together with the chairperson of the disclosure committee, should discuss important disclosure issues with the audit committee.

***Financial Information.*** The disclosure committee's duties will extend to the entirety of the company's disclosure, including financial information, i.e., financial statements and accompanying footnotes, the MD&A (including critical accounting policies, off-balance sheet arrangements, related party transactions, trend disclosure and disclosure of known uncertainties), summary and selected financial information and pro forma earnings information. The disclosure committee should be made aware of all assumptions and judgments (whether relating to accounting, business, industry, litigation or other areas) that underlie the financial information and could raise disclosure issues.

The disclosure committee's task goes beyond assessing whether the financial statements and accompanying footnotes have been presented in accordance with GAAP. Rather, the disclosure committee should assess whether or not the financial information "fairly presents" in all material respects the financial condition, results of operations and cash flows of the company as of and for the periods presented. This language is used in the Section 302 certifications and, according to the SEC, means that the financial information disclosed in a report, viewed in its entirety, meets a standard of overall material accuracy and completeness that is broader than

financial reporting requirements under GAAP. In the SEC's view, a "fair presentation" of a company's financial condition, results of operations and cash flows encompasses:

- the selection and proper application of appropriate accounting policies;
- the 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 the company's financial condition, results of operations and cash flows.

Obviously, some members of the disclosure committee, such as those members with accounting expertise, will be more familiar with the financial information. Although the "non-financial" members of the disclosure committee are not required to be experts in accounting matters, the "non-financial" members should understand and participate in the evaluation of disclosure issues relating to financial information. To a certain extent, the audit committee's review of public disclosure and the review by the disclosure committee will overlap. As a timing matter, the disclosure committee will begin reviewing the public disclosure at an earlier stage than the audit committee, which will ordinarily begin its review with more advanced drafts.

**4. ESTABLISHING A PROCESS FOR DRAFTING AND REVIEWING THE DISCLOSURE.**

***General.*** The disclosure committee should be responsible for designing and implementing the process of drafting the disclosure to be included in the applicable SEC filings or other public documents. Each reporting company should develop a process that is best suited to its particular practices and needs. As an initial matter, we recommend that disclosure committees review and familiarize themselves with the company's existing disclosure, as well as the public disclosure of competitors and any analyst reports concerning the company and key competitors. This knowledge will create a historical perspective on disclosure matters and a benchmark to judge the adequacy of the company's disclosure. We outline a sample process below.

- *Development of Timetable and Responsibility Schedules*. The first step in any process should be the development of a timetable that would identify deadlines for the preparation of the company's 10-K, 20-F or 40-F, 10-Q's or 6-K's, proxy statement, annual report and any other disclosures that the company may choose to subject to the disclosure controls and procedures, such as earnings press releases and any other regular press releases bearing on financial or operational

performance.[8] The company should then schedule meetings of the board of directors and the audit committee to facilitate the review of the relevant documents by the board of directors and the audit committee prior to their filing. Once the timetable is established, responsibility schedules should be developed in a sufficient level of detail to allow one or more individuals on the disclosure committee to review progress against the schedule. The preparation and monitoring of the disclosure schedule could be assigned to the disclosure coordinator.

- *Assignment of Drafting Responsibilities.* Responsibility for drafting key sections of the public disclosure should be delegated to members of the disclosure committee or other personnel who are suitably skilled and experienced, including, at least in the case of registration statements and private offering memoranda, outside counsel. While existing disclosure may be a sensible place to begin, past disclosure should be reviewed with a critical eye and the impetus of the recent regulatory actions should be used to update and reformulate disclosure as necessary. The individuals drafting the disclosure should be familiar with the SEC's "plain English" requirements.

- *Scheduling Drafting Sessions.* In the case of larger companies or companies with a number of business segments, the disclosure coordinator should consider scheduling drafting sessions dedicated to specific portions of an Exchange Act report, as necessary. These drafting sessions would be attended by officers, employees and, particularly in the case of offering documents, outside advisers including outside counsel and outside auditors, whose input is necessary or desirable in drafting the disclosure document. There would be at least one drafting session for each portion of each document, generally at a time in the process to allow review of draft disclosure – that is, not too early in the process – and to permit substantive revisions or additions in response to comments – that is, not too late in the process.

- *Internal Review of Draft Disclosure.* Once drafted, the disclosure should be reviewed by the disclosure committee members. In the case of larger companies or companies with a number of business segments, the disclosure may then need to be distributed to experts within the organization for their review. Officers in charge of business units or functions, such as litigation, tax, environmental, regulatory etc., would be assigned the tasks of reviewing the relevant sections of

---

[8] Timetables and responsibility schedules in the context of securities offerings should continue to be prepared in consultation with the underwriters and their counsel, with it now being appropriate to give additional consideration to the role of the disclosure committee in the process of preparing and reviewing the offering document.

the public disclosure and providing detailed comments. The individuals charged with responsibility for various sections of the public disclosure would also be the key individuals in the organization who were interviewed as part of the internal review process. Appendix B sets forth sample instructions for reviewers.

- *External Review of Draft Disclosure*. Once comments are received and a new draft produced, the revised disclosure may then be distributed to the outside auditors, outside counsel and, if applicable, any other experts for review and comment.

- *Back-up Certifications*. When officers and/or employees "sign off" on the disclosure that they have responsibility for reviewing, the disclosure committee may consider obtaining back-up certifications from these individuals. Such certification may take several forms. Attached to this memorandum as Appendix C-1 is a form of certification that could be used where the reviewer has the experience, information and responsibilities to certify as to the company's financial and non-financial information on a consolidated basis. Alternatively, where certifications are sought from individuals such as heads, or principal financial officers, of business units who may be unable to certify as to the company's financial and non-financial information on a consolidated basis in light of their more limited experience, information or responsibilities, a company may consider obtaining certifications in the form attached to this memorandum as Appendix C-2.

- *Review by CEO and CFO*. The disclosure committee should determine when it is appropriate to circulate the draft disclosure to the CEO and CFO for their review and comments.

- *Review by Audit Committee*. The audit committee, if required, would typically review the draft periodic reports and other financial disclosure after the CEO and CFO commented.[9]

---

[9] Under the proposed rules of the New York Stock Exchange, the audit committee is required to discuss, prior to filing with the SEC, the annual audited financial statements and quarterly financial statements, including the MD&A, with management and the company's independent auditor. However, the audit committee's responsibility to discuss earnings releases and earnings guidance may be done generally (type of information and presentation) and need not be done in advance of issuance. See our memorandum dated August 23, 2002 entitled *"NYSE Board of Directors Approves New Corporate Governance Disclosure Standards."* This memorandum is available upon request or at our website: *www.simpsonthacher.com*.

We understand that the NASDAQ Stock Market's proposed rules do not currently contain such a requirement. While the SEC has indicated that it intends to harmonize the NYSE and NASDAQ proposals on corporate governance, the result of this intended harmonization is unclear.

***MD&A.*** The MD&A is one of the most important sections of a periodic report. The SEC has regularly affirmed the importance of the MD&A, urging public companies to use particular care in the preparation of the MD&A and other financial disclosures. In January 2002, for example, the SEC stated that:

> "MD&A requirements are intended to provide in one section of a filing material historical *and* prospective textual disclosure enabling investors and other users to assess the financial condition and results of operations of the registrant, with particular emphasis on the registrant's prospects for the future."[10]

Indeed, in this post-Enron era, the MD&A has been a principal focus of the SEC's disclosure initiatives to increase the transparency and understandability of financial reporting. The individuals responsible for drafting the MD&A should, therefore, not only have the requisite accounting and financial background, but also have a thorough understanding of the SEC disclosure requirements applicable to the MD&A, including with respect to critical accounting policies, off-balance sheet arrangements, related party transactions, liquidity, trend disclosure and disclosure of known uncertainties. The process of drafting the MD&A should not merely involve marking up last year's or last quarter's MD&A.[11] Rather, the individuals drafting the MD&A should take a fresh look at the MD&A and draft it in a way that satisfies the three objectives set forth by the SEC:

- provide a narrative explanation of the company's financial statements that enables investors to see the company through the eyes of management;

- improve overall financial disclosure and provide the context within which financial statements should be analyzed; and

- provide information about the quality of, and potential variability of, the company's earnings and cash flow, so that investors can ascertain the likelihood that past performance is indicative of future performance.[12]

---

[10] SEC Release Nos. 33-8056 and 34-45321 (January 22, 2002).

[11] See speech by Robert K. Herdman, entitled *"Critical Accounting and Critical Disclosures,"* January 24, 2002, before the Financial Executives International – San Diego Chapter: "I'd like to challenge each of you to capitalize on the flexibility in the [MD&A] rules and avoid discussions that are boilerplate and simply translate the financial statements from numbers into words. I also want to put you on notice that investors and the SEC staff alike can be expected to challenge MD&A discussions that are unclear, boilerplate and missing or misleading… We at the SEC have given you a lot to think about and I'll pass along some good advice I heard yesterday. That is, this year's MD&A ought not just be a mark-up of last year's. Start with a clean sheet of paper!"

[12] SEC Release Nos. 33-8098 and 34-45907 (May 10, 2002).

Although one or two individuals are typically delegated the responsibility of preparing the initial draft of the MD&A, all members of the disclosure committee should participate in a detailed review of the MD&A, including disclosure of critical accounting policies, off-balance sheet arrangements, related party transactions, presentations on trends reflected in the accompanying financial statements and known uncertainties. With the breadth of experience and authority that the disclosure committee should possess, particularly after conducting the internal review process, the likelihood that the MD&A will be prepared from a "critical perspective" will be significantly enhanced.

***Risk Factors and Forward-Looking Statements.*** The risk factors and forward-looking statements may also be critical components of annual reports and other SEC filings. The review of any such sections should be at least quarterly. In light of the importance of any such disclosure, it may be advisable to delegate such responsibility to one or more senior officers with a good understanding of the risks relating to the company's business. Such senior officer or officers would be advised to monitor the risk factor disclosure of competitors, customers and suppliers and discuss with the disclosure committee any material changes in such disclosure. In addition, these officers would be asked to review research reports of analysts that follow the company and its competitors and discuss with the disclosure committee any potential disclosure issues that may be raised as a result. Companies also should conform the forward-looking statement sections of their filings to their revised risk factor disclosure. Forward-looking statements must be accompanied by "meaningful cautionary statements" if the safe harbor for forward-looking statements under the Private Securities Litigation Reform Act is to be available.

***Documentation***. We recommend that companies consider delegating to the disclosure coordinator the task of documenting the actual work done in connection with disclosure documents and, in particular, periodic reports. This record would document what was done, when it was done and who was involved. This documentation might be similar to board minutes and like board minutes would not be unnecessarily detailed. Such documentation would provide a permanent record of compliance with the disclosure controls and procedures and would assist in the required quarterly evaluation process. Care must be taken to ensure that these minutes are not prejudicial in the context of a disclosure lawsuit.

**5. ESTABLISHING AN EVALUATION PROCESS.**

The SEC, at an open meeting on October 16, 2002, agreed to propose rules under Section 404 of the Sarbanes-Oxley Act requiring that annual reports contain (1) internal control reports stating the responsibility of management for the establishment and maintenance of an adequate internal control structure and procedures for financial reporting and (2) an assessment of the internal control structure and procedures for financial reporting. This assessment must be attested by a reporting company's outside auditors. The proposed new rules have not yet become publicly available and will be discussed in a future memorandum. Pending consideration of these new proposed rules, we would recommend that the evaluation process in

relation to the establishment of disclosure controls and procedures should include an evaluation of any material change in circumstances relating to disclosure controls and procedures since the last evaluation, including a review of any deficiencies in disclosure controls and procedures identified by internal personnel, the outside auditors or the audit committee. In conducting each evaluation, we also suggest that the disclosure committee review, in particular, the impact on the company's disclosure controls and procedures of any significant changes to the business, such as:

- installation of new information systems;
- material acquisitions or dispositions;
- changes in lines of business;
- geographic expansion; and
- changes in personnel involved in the disclosure controls and procedures.

In addition, the disclosure committee should discuss internal controls with the outside auditors.

**6. PREPARING FOR "REAL-TIME" DISCLOSURE.**

Enhanced disclosure controls and procedures should help assure that the disclosure committee is advised promptly of the occurrence of any events or transactions that need to be reported on Form 8-K in order to be able to prepare and timely file such reports. The importance of establishing disclosure controls and procedures which will assure the prompt dissemination of important developments to the disclosure committee will be heightened by the movement to more real time disclosure as contemplated by Section 409 of the Sarbanes-Oxley Act and as proposed by the SEC prior to the enactment of the Sarbanes-Oxley Act. The SEC has proposed significant amendments to Form 8-K[13] which would, if adopted, add eleven new items to the list of events that are required to be reported, including:

- entry into a material agreement or material amendment to a material agreement not made in the ordinary course of business;
- termination of a material agreement not made in the ordinary course of business;

[13] See our memorandum dated June 27, 2002 entitled *"SEC Proposes New Rules Relating to 8-K Disclosure and Officer Certification."* This memorandum is available upon request or at our website: *www.simpsonthacher.com*.

- termination or reduction of a business relationship with a customer that constitutes a specified amount of the company's revenues;

- creation of a direct or contingent financial obligation that is material to the company;

- events triggering a direct or contingent financial obligation that is material to the company, including any default or acceleration of an obligation;

- 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 of a credit watch, change in a company outlook or refusal to assign a credit rating after the company requested one;

- 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-out periods, regarding the company's employee benefit, retirement and stock ownership plans.

In addition, the proposed amendments would require a Form 8-K to be filed within two business days of the occurrence of the event requiring the report.

The SEC received significant comments on the proposed amendments during the public comment period, which ended on August 26, 2002. Most of the comments focused on the two-business day filing requirement and the subjective nature of some of the new triggering events that use a materiality standard such as entry into and termination of material contracts. We recommend that companies circulate to the appropriate people the currently proposed list of reportable events (while noting that these events may not currently be required to be reported on Form 8-K). When amendments are adopted in final form, companies should circulate a revised list of reportable events, together with the revised instructions for Form 8-K. To the extent the deadlines are shortened and/or events based on a materiality standard are included

in the final amendments, companies are advised to design a process that will bring to the attention of the disclosure committee the *possible* occurrence of triggering events. If the SEC decides to retain the proposed two-day filing deadline in the final rules, many companies will probably decide that they require a process to identify *possible* triggering events *even if* the standard used for the event is an objective one.

The proposed amendments to Form 8-K provide for a limited safe harbor for companies that fail to file a current report in a timely manner if, among other things, these companies maintained sufficient procedures to provide reasonable assurances that the companies were able to collect, process and disclose, within the specified time periods, the information required to be disclosed by Form 8-K. The proposed amendments contemplate that companies that qualify for the safe harbor would not be liable for violation of Section 13(a) or 15(d) of the Exchange Act, although companies may still be liable under Section 10 and Rule 10b-5 of the Exchange Act and Sections 11, 12 and 17 of the Securities Act. In addition, the safe harbor would not apply to a company's eligibility to use short-form registration statements.

**7. DETERMINING THE ROLE OF OUTSIDE AUDITORS.**

Companies may consider engaging their outside auditors to prepare an "agreed-upon procedures letter" with respect to each periodic report. An agreed-upon procedures letter is a process similar to a comfort letter in the case of a securities offering and applies to financial information that is not included in the financial statements which the outside auditors audit on an annual basis and review on a quarterly basis. In addition, companies may consider engaging their outside auditors to provide an examination report or a review report regarding the MD&A in accordance with Statement on Standards for Attestation Engagements ("SSAE") No. 10. The examination report would state that, in the auditor's opinion, the MD&A includes in all material respects the required elements of the rules and regulations adopted by the SEC. The review report would state that, based on the auditors' review, nothing came to the auditors' attention that caused them to believe that the company's presentation of the MD&A did not include, in all material respects, the required elements of the rules and regulations adopted by the SEC. At the present time, SSAE No. 10 examination and review reports are not standard practice and many accounting firms have historically been reluctant to furnish them. However, the new SEC requirements may lead more companies to consider seeking this additional comfort.

**8. DETERMINING THE ROLE OF OUTSIDE COUNSEL.**

Each company will determine the extent of the involvement of their outside counsel as part of their disclosure controls and procedures in the context of Exchange Act filings; outside counsel should continue to have a prominent role in the context of the preparation of registration statements and private offering memoranda. Some companies will opt for limited or no involvement by outside counsel in connection with their Exchange Act filings, while others will ask outside counsel to review such filings. As a middle course, some companies may

engage outside counsel to review specified sections of annual and quarterly reports, such as the litigation and regulatory matters sections, or to assist with the resolution of specific disclosure issues. At a minimum, companies should consider involving outside counsel in discussions of significant disclosure issues. Outside counsel may offer valuable experience and knowledge in evaluating disclosure issues, as well as offer insights gained from the experience of participating in other companies' disclosure processes. Companies may also wish to involve outside counsel in the review of Exchange Act reports, and in particular sensitive disclosure areas, to decrease the likelihood that the same disclosure will have to be materially revised by outside counsel in the context of a securities offering to comply with applicable SEC rules. The value of participation of outside counsel will be enhanced to the extent such counsel participates early on in the review process relating to the filing.[14]

## REGISTERED INVESTMENT COMPANIES

Registered investment companies satisfy their Exchange Act reporting requirements by filing Form N-SAR. Accordingly, the Section 302 certification and the additional certifications relating to disclosure controls and procedures are currently required to be filed with Form N-SAR. If proposed Rule 30a-2 is adopted by the SEC, these certifications will additionally be required to be filed with new Form N-CSR which will include a copy of the investment company's annual or semi-annual shareholder report.

Registered investment companies, unlike operating companies, generally outsource the production of their SEC reports, including Forms N-SAR, and the data compilation connected therewith. Therefore, in order for a fund's principal executive officer and principal financial officer to make the certifications regarding Form N-SAR required by Section 302 of the Sarbanes-Oxley Act, certifying officers will have to undertake a review not only of the report and the fund's disclosure controls and procedures, but of the disclosure controls and procedures of the relevant service providers as well. At a minimum, this will require fund management to:

- familiarize itself with the current processes by which service providers collect, process and report fund-related information;
- review previous N-SARs as well as any auditor internal control reports to identify weaknesses in existing procedures;
- discuss current procedures with the service providers; and

[14] See speech by Robert K. Herdman, *supra* note 8: "Invite your attorneys into the discussion; they undoubtedly help you with MD&A when you are raising capital, and they can be of great assistance in your annual report as well."

- cause the service providers to make any necessary adjustments to existing disclosure controls and procedures to ensure that material information is made known to the certifying officers.

A fund should not continue to delegate the preparation of fund reports to a service provider unless management determines that the entity has adequate controls and procedures in place to allow the fund's principal executive officer and principal financial officer to make the required certifications.

## FAILURE TO MAINTAIN DISCLOSURE CONTROLS AND PROCEDURES

The SEC has indicated that a company that fails to maintain adequate disclosure controls and procedures could be subject to SEC enforcement action for violating Section 13(a) or 15(d) of the Exchange Act, even if such failure does not lead to flawed disclosure. In addition, a failure in disclosure could lead to liability in private litigation against a certifying CEO or CFO under Section 10(b) and Rule 10b-5 under the Exchange Act and liability for the reporting company under Sections 11 and 12(a)(2) of the Securities Act of 1933, in the event that a quarterly or annual report is incorporated by reference into a registration statement. By comparison, Section 906 of the Sarbanes-Oxley Act imposes criminal penalties for false certifications. [15]

Maintenance of effective disclosure controls and procedures is therefore necessary to comply with the provisions of the Sarbanes-Oxley Act and the new SEC rules and to protect the signing officers from liability. Naturally, no system of disclosure controls and procedures can be perfect. However, in the event of failure of a company's disclosure controls and procedures, the company is more likely to receive more lenient treatment from the SEC if it maintained effective disclosure controls and procedures prior to such failure than if it did not.[16]

---

[15] Section 906 requires the CEO and CFO of an issuer to certify in each periodic report that contains financial statements filed with the SEC pursuant to Section 13(a) or 15(d) of the Exchange Act that:

- the report fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act, as applicable; and
- information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the issuer.

[16] See speech by Commissioner Cynthia A. Glassman, entitled *"Sarbanes-Oxley and the Idea of 'Good' Governance,"* September 27, 2002, before the American Society of Corporate Secretaries: "Obviously, no system of controls can prevent all misconduct; however, if a company can demonstrate that it has satisfied its obligation to implement good procedures, then in my eyes it has a significantly better chance of

* * *

Please contact your relationship partner if we can be of assistance regarding these important developments. The names and office locations of all of our partners, as well as additional memoranda regarding recent corporate governance developments, can be obtained from our website, www.simpsonthacher.com.

SIMPSON THACHER & BARTLETT LLP

---

receiving leniency… In short, if you are looking for leniency you had better be able to show that you cared about preventing corporate misconduct before you discover that it occurred."

**Appendix A**

## DISCLOSURE COMMITTEE CHARTER

*Some disclosure committee charters may extend to any information disclosed to shareholders and the investment community while others may be limited to Exchange Act reports. We recommend that, at a minimum, the Disclosure Controls and Procedures extend to Exchange Act reports, registration statements and private offering memoranda, although abbreviated Disclosure Controls and Procedures may be appropriate in the context of shelf take-downs by certain seasoned issuers. Companies should consult with counsel to determine the extent to which a company's Disclosure Controls and Procedures should be extended to other forms of communication to shareholders and the investment community.*

This Disclosure Committee Charter (the "Charter") has been adopted by the Chief Executive Officer and the Chief Financial Officer (the "Senior Officers") of [insert name of company] (the "Company") and ratified by the Audit Committee of the Company's Board of Directors (the "Audit Committee").

### PURPOSE

Subject to the guidance and supervision of the Senior Officers, the Disclosure Committee (the "Committee") shall:

A. Design, establish and maintain controls and other procedures (the "Disclosure Controls and Procedures") to ensure that:

1. information required to be disclosed in the reports and statements filed by the Company pursuant to the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, summarized and reported in conformity with, and within the time periods specified by, the Exchange Act and the rules and forms of the Securities and Exchange Commission (the "SEC");

2. information required to be disclosed in registration statements and prospectuses filed by the Company pursuant to the Securities Act of 1933, as amended (the "Securities Act"), is recorded, processed, summarized and disclosed in conformity with the Securities Act and the rules and forms of the SEC;

3. information included in the documents identified in clauses A.1 and A.2 and in private offering memoranda (collectively, "Disclosure Documents") is recorded, processed, summarized and disclosed so that:

(a) Disclosure Documents do not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made

therein, in light of the circumstances under which such statements were made, not misleading; and

(b) any financial statements and other financial information included in Disclosure Documents 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 therein; and

4. all information to be included in any Disclosure Document is communicated to the Company's management, including, without limitation, the Senior Officers, as appropriate to allow timely decisions regarding required disclosure.

B. Evaluate the effectiveness of the Disclosure Controls and Procedures on a regular basis, but in no event later than as of a date within 90 days prior to the filing date of any [Annual Report on Form 10-K and each Quarterly Report on Form 10-Q] [Annual Report on Form 20-F] [Annual Report on Form 40-F] and, in each case, communicate to the Company's management, including, without limitation, the Senior Officers:

1. the Committee's conclusions regarding the effectiveness of the Disclosure Controls and Procedures;

2. all significant deficiencies in the design or operation of the Disclosure Controls and Procedures which could adversely affect the Company's ability to record, process, summarize and report information identified in clauses A.1 through A.3 above;

3. any fraud, whether or not material, that involves management or other employees who have a significant role in the Disclosure Controls and Procedures, including, without limitation, internal controls; and

4. any significant changes in the Disclosure Controls and Procedures, including, without limitation, internal controls, or in other factors that could significantly affect the Disclosure Controls and Procedures, including, without limitation, internal controls, subsequent to the date of the Committee's most recent evaluation, including, without limitation, any corrective actions with regard to significant deficiencies and material weaknesses.

C. Design, establish and maintain a process pursuant to which the Committee shall be responsible for preparing and approving the disclosure included in the Disclosure Documents.[1]

---

[1] In the event that companies determine not to subject certain information to be communicated to shareholders and the investment community to the Disclosure Controls and Procedures, companies should consider including that information within the scope of this clause C.

D. Maintain written records of the Disclosure Controls and Procedures followed in connection with the preparation and approval of Disclosure Documents.

E. Undertake any other responsibilities delegated to it from time to time by any Senior Officer to assist that Senior Officer in fulfilling his or her responsibility for oversight of compliance with the Disclosure Controls and Procedures.

In discharging its duties, the Committee shall have access to all Company books, records, facilities and personnel, as well as the Company's outside auditors and outside counsel.

**COMPOSITION AND QUALIFICATIONS**

The Committee shall consist of officers or employees of the Company appointed from time to time by the Senior Officers; *provided*, *however*, that at least one member of the Committee shall be an attorney with expertise in SEC rules and regulations with respect to disclosure and at least one member of the Committee shall be a certified public accountant with expertise in accounting and SEC financial reporting. Notwithstanding the foregoing, the Senior Officers at their option may from time to time assume any or all of the responsibilities of the Committee set forth in this Charter or may appoint two or more members (who among themselves shall have the expertise described in the proviso in the preceding sentence) to approve Disclosure Documents when time or other circumstances do not permit the full Committee to meet, all in order to ensure compliance with the objectives stated in clause A. above.

The members of the Committee may be removed by any Senior Officer or by a majority vote of the Audit Committee or the Company's Board of Directors.

One member of the Committee shall be appointed by a Senior Officer as Chairperson. The Chairperson shall be responsible for scheduling and presiding over the Committee's meetings, preparing agendas for such meetings and supervising the work of the Committee.

The Committee shall meet regularly and shall meet with the Senior Officers, the Audit Committee and the Company's outside auditors and outside counsel, in each case as necessary, appropriate or desirable to discharge the responsibilities set forth in this Charter. The Committee may invite to its meetings any director, member of management and such other persons as it deems appropriate in order to carry out its responsibilities.

No member of the Committee shall receive compensation for serving on the Committee.

## ANNUAL PERFORMANCE EVALUATION

The Committee shall perform a review and evaluation, at least annually, of the performance of the Committee and its members, including by reviewing compliance of the Committee with this Charter. In addition, the Committee shall review and reassess, at least annually, the adequacy of this Charter and recommend to the Senior Officers any improvements to this Charter that the Committee considers necessary or valuable. The Committee shall conduct such evaluations and reviews in such manner as it deems appropriate.

**Appendix B**

## INSTRUCTIONS TO REVIEWERS

Please find enclosed a draft disclosure document relating to the Company. We encourage you to read this document in its entirety. The portions of such document that you are particularly responsible for reviewing have been highlighted for your convenience. [If applicable: We have enclosed a copy of the SEC rules that set forth the information that needs to be disclosed in the sections of the enclosed document you are requested to review.] After completing your review but in any event not later than [date], please contact [insert name of member of Disclosure Committee] and inform [him/her] as to whether or not:

1. the information you are required to review contains any untrue statement of a material fact or omits to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading and, if yes, identify such untrue statement(s) or omission(s);

2. [if applicable: such information complies with the enclosed SEC rules and, if not, in what respects such information needs to be modified in order to comply with such SEC rules; and]

3. [if applicable: the enclosed financial statements (including footnote and schedule disclosure) and other financial information 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 and, if not, in what respects such financial statements (including footnote and schedule disclosure) and other financial information need to be modified in order to 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.]

With respect to clause (1) above, "material" means information that is important to an investor in deciding whether or not to buy, hold or sell securities of the Company. However, you are not required to evaluate materiality as to the Company as a whole. Rather, you are requested to evaluate materiality as to your particular business unit, segment or geographic region, as applicable. The Disclosure Committee will then evaluate the materiality of any disclosure issue you raise as to the Company as a whole. A member of the Disclosure Committee will then contact you to inform you of the results of the Disclosure Committee's evaluation.

[If applicable: With respect to (3) above, "fairly present" is not limited to the financial statements and other financial information having been presented in accordance with GAAP.

Rather, the term "fairly present" encompasses the selection of appropriate accounting policies, the appropriate 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 the Company's financial condition, results of operations and cash flows.]

Please note that you will be required to sign the enclosed form of certification with respect to the final version of the portions of the enclosed disclosure document that you are responsible for reviewing.

Please be advised that any material defects in the Company's disclosure could result in civil and/or criminal liability for the Company and its officers and directors. It is, therefore, critically important that you conduct your review in a diligent manner.

Please feel free to contact [insert name of member of Disclosure Committee] with respect to any questions you may have in conducting your review.

THE DISCLOSURE COMMITTEE

**Appendix C-1**

## CERTIFICATION OF OFFICERS AND/OR EMPLOYEES

The undersigned, being [insert title of officer or employee] of [insert name of company] (the "Company"), hereby certifies that:

1. I have reviewed the enclosed disclosure; and

2. I have complied in all material respects with the provisions set forth in "Instructions to Reviewers" with respect to the enclosed disclosure; and

3. I have disclosed to Company's Disclosure Committee each incident of fraud that I am aware of, whether or not material, that occurred in [identify region, business segment or unit, as applicable] and involves any employee or agent of the Company.

[If applicable: The undersigned acknowledges that the Company's Chief Executive Officer and Chief Financial Officer will rely on this certification in connection with their certification of the enclosed disclosure pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and the SEC rules and regulations promulgated thereunder.]

IN WITNESS WHEREOF, I have signed this certification on this ____ day of [insert month], 20__.

_______________________________

[INSERT NAME OF INDIVIDUAL]

**Appendix C-2**

## CERTIFICATION OF OFFICERS AND/OR EMPLOYEES

The undersigned, being [insert title of officer or employee] of [insert name of company] (the "Company"), hereby certifies that:

1. To my knowledge, the enclosed financial statements for which I am responsible [fairly present][1] in all material respects the financial condition, results of operations and cash flows of the Company's [insert name of business unit] (the "Unit") as of, and for, the periods presented in those financial statements;

2. The statements made by me to the Company's Disclosure Committee during the [meeting/telephone conference] held on [insert date] are true and correct in all material respects and do 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;

3. I have disclosed to the Company's Disclosure Committee any and all material developments, whether positive or negative, relating to the Unit; and

4. I have disclosed to the Company's Disclosure Committee each incident of fraud that I am aware of, whether or not material, that occurred in the Unit and involves any employee or agent of the Company.

With respect to clauses (1) through (4) above, I have evaluated materiality as to the Unit.

---

[1] This certification would not be applicable in circumstances where the financial information is so summary as to not admit a "fairly present" standard. In that case, the standard to be used should be determined based on the kind of financial statements available and their level of detail. As an example, an alternative certification could be as follows:

> "To my knowledge, the enclosed financial statements of the Unit for which I am responsible are true and correct in all material respects and have been prepared in accordance with GAAP in all material respects. I have fully and accurately communicated to the Company's Disclosure Committee any risks, contingencies, transactions, arrangements, trends, uncertainties or other similar or related information of which I am aware that could affect the financial condition, results of operations or cash flows of the Unit in any material respect and which are not expressly identified in the enclosed financial statements."

With respect to (1) above, “fairly present” is not limited to the financial statements and other financial information having been presented in accordance with GAAP. Rather, the term “fairly present” encompasses the selection of appropriate accounting policies, the appropriate 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 the Unit’s financial condition, results of operations and cash flows.

[If applicable: The undersigned acknowledges that the Company’s Chief Executive Officer and Chief Financial Officer (together, the “Certifying Officers”) will rely on this certification in connection with their certification of the Company’s periodic reports pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and related SEC rules and regulations promulgated under the Securities Exchange Act of 1934, as amended. The undersigned also acknowledges that the Company’s [identify the individuals that will prepare and review the disclosure on a consolidated basis] will rely on this certification in connection with their related certification to the Certifying Officers of the Company’s periodic reports.]

IN WITNESS WHEREOF, I have signed this certification on this ____ day of [insert month], 20__.

_________________________________

[INSERT NAME OF INDIVIDUAL]