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# Client Alert

January 31, 2003

## INTELLECTUAL PROPERTY

### Disclosure Controls and Procedures

On July 30, 2002, Congress passed the Sarbanes-Oxley Act of 2002 (the "Act"), which has been described as the most significant change in securities and disclosure regulation since the Securities Exchange Act of 1934 (the "Exchange Act"). Among the many areas of concern for companies seeking to ensure compliance with the Act is the **mandatory requirement** that processes be established by which public companies collect, marshal and prepare information about their business, including intellectual property information,<sup>1</sup> for inclusion in disclosure documents submitted to the Securities and Exchange Commission (SEC). Under the Act, company officers are required to personally certify not only to the *establishment* but also to the *effectiveness* of these disclosure controls and procedures.

Private companies that may either be contemplating a public offering or a merger with an already public company subject to the Act, should also ensure that these processes are in place since compliance will be a significant issue in any pre-offering or pre-merger due diligence.<sup>2</sup>

#### What Is Required and Why

In response to the directives of Section 302 of the Act, the SEC issued final rules on August 29, 2002,<sup>3</sup> requiring each principal executive officer and principal financial officer of a public company to certify personally, in each quarterly and annual report, that, among other things:

- based on the officers' knowledge, the report **does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements in the report not misleading;**
- the officers themselves **are responsible for establishing and maintaining "disclosure controls and procedures"** (as defined below) for the issuer;
- the officers have **designed the disclosure controls and procedures** to ensure that necessary material information to be included in SEC filings is made known to the officers; and
- the officers have **evaluated the effectiveness of the issuer's disclosure controls and procedures** within 90 days before the filing of the report.

<sup>1</sup> Intellectual property means copyright, patent, trademark and trade secret protection.

<sup>2</sup> Please see Mintz Levin's Client Advisory entitled "How Does the New Corporate Governance Regime Affect Private Issuers?," available on Mintz Levin's web site at <http://www.mintz.com/images/dyn/publications/secadv120302.pdf>, for more information about the effect of the Act on private company issuers.

<sup>3</sup> For more information about these rules generally, please see Mintz Levin's Client Advisory entitled "Further Guidance on Certification of Periodic Reports," available on Mintz Levin's web site at <http://www.mintz.com/images/dyn/publications/SECAdvisory91202.pdf>.

In order to be able to make the required certifications to the SEC as described above without qualification, all issuers must be able to satisfy themselves that their procedures with respect to disclosure of all material areas of their businesses are well-designed and properly functioning. This process is particularly challenging for issuers having significant intellectual property assets, given the complexities of monitoring and describing the required information with respect to an intellectual property portfolio.

### What are “Disclosure Controls and Procedures”?

The phrase “disclosure controls and procedures” is a new concept under the SEC’s disclosure rules, and is defined as:

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....[and] 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.<sup>4</sup>

The new certification requirements make clear that (i) all issuers must now take greater care in the preparation and implementation of their controls and procedures, and (ii) each issuer’s chief financial and chief executive officer must personally ensure, prior to the submission of each report, that the disclosure controls and procedures, as

designed, are adequate. For many companies, this may require a level of unprecedented personal involvement by the CEO and CFO in the process of preparation of SEC disclosure documents. At the very least, any officer required to make such certification will want to have written documentation supporting the certification in the event the disclosure or non-disclosure is challenged.

### What Disclosure Is Required About Intellectual Property Matters?

Reporting companies are required to describe several aspects of their intellectual property portfolios in their annual and quarterly reports to the SEC. Detailed disclosure regarding a company’s patents, trademarks, copyrights, and trade secrets is required in the *Business* section of an annual report.<sup>5</sup> Other areas of an annual report in which intellectual property disclosure appears are the *Risk Factors* section, if there are important elements of risk relating to the use and protection of the company’s intellectual property assets, and the *Legal Matters* section, if the company is engaged in any material litigation with respect to its intellectual property portfolio. In addition, each of these areas may need to be updated in a company’s quarterly reports to the SEC if material developments or changes have occurred in the required disclosure since the filing of the annual report. It is customary for a company to report in both its Form 10-Qs and Form 10-Ks (a) that the company protects its intellectual property rights, (b) the number of its patents, trademarks, and/or copyrights (and/or the existence of company trade secrets) and the importance of all intellectual property assets to the company’s business, and (c) any

third-party intellectual property barriers to the company’s ability to conduct its business.

As a result of the new certification requirements of Section 302 of the Act, each company filing reports to the SEC, in order for its principal executive and principal financial officers to be able to make the required certifications, must implement procedures to ensure that all necessary disclosure regarding its intellectual property assets is gathered, processed, and updated in a timely manner. Further, these procedures have to be adequate so that the certifying officers can satisfy themselves that all of the disclosure regarding their intellectual property matters is complete and accurate.<sup>6</sup>

### Mintz Levin Can Help You Comply with the New Certification Rules

Mintz Levin has developed a program to help ensure that principal executive and financial officers are able to make the required certifications to the SEC with respect to the disclosure regarding their companies’ intellectual property. This program enables a company to evaluate the effectiveness of its procedures for protecting intellectual property, for tracking the number and status of intellectual property rights, and for monitoring third-party intellectual property rights that might impact on the company’s ability to conduct its business.

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*If your company would like to learn more about Mintz Levin’s capabilities in helping with this critical aspect of corporate compliance, please contact Ivor Elrifi, Co-Chair of Mintz Levin’s Intellectual Property Section, at [ielrifi@mintz.com](mailto:ielrifi@mintz.com) or 617-542-6000.*

<sup>4</sup> New Exchange Act Rules 13a-14(c) and 15d-14(c).

<sup>5</sup> This assumes that at least one intellectual property right is an “important” asset to the Company.

<sup>6</sup> Moreover, having in place well-documented procedures and policies with respect to the status and handling of intellectual property and trade secret information serves the additional purpose of bolstering protection of the company’s intellectual property rights against third parties, especially when the company seeks to enforce its intellectual property and trade secret rights under contract or common law, and is required to demonstrate that it has taken all necessary and appropriate steps to a Court or an arbitrator.