WILMERHALE

SEC Charges CEO and CFO for Internal Control Reporting Violations

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Last month the SEC initiated administrative proceedings charging the CEO and former CFO of a Florida-based computer equipment company with making misrepresentations about the company's internal control over financial reporting (ICFR). The SEC alleges that in 2008 and the first quarter of 2009, the executives were aware of deficiencies in and circumvention of internal controls relating to inventory and the resulting falsification of the company's books and records. They also allegedly participated in actions to accelerate recognition of revenue in order to increase the borrowing base under a credit facility. The SEC charged that, as a result, the executives' management representation letters to the company's external auditor falsely stated that they had disclosed all significant deficiencies in ICFR, in violation of Rule 13b2-2(b) under the Exchange Act. The SEC also charged that the executives signed a Form 10-K containing a management report on ICFR that falsely stated that the CEO had participated in assessing the effectiveness of the company's ICFR, when he had not done so, and had signed false management certifications contained in SEC periodic reports. The CFO settled the charges, but the CEO did not.

While the case turns on its particular facts, it is indicative of an SEC enforcement focus on violations related to ICFR deficiencies and is a reminder that misrepresentations to a company's auditor can be a basis for SEC sanctions.