SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 210, 228, 229, 239, 240, and 249

[Release Nos. 33–7386; 34–38223; IC–22487; FR–48; International Series No. 1047; File No. S7–35–95]

RIN 3235–AG42, 3235-AG77

Disclosure of Accounting Policies for Derivative Financial Instruments and Derivative Commodity Instruments and Disclosure of Quantitative and Qualitative Information About Market Risk Inherent in Derivative Financial Instruments, Other Financial Instruments, and Derivative Commodity Instruments

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission (''Commission'' or ''SEC'') is amending rules and forms for domestic and foreign issuers to clarify and expand existing disclosure requirements for derivative financial instruments, other financial instruments, and derivative commodity instruments, as defined (collectively ''market risk sensitive instruments''). The amendments require enhanced disclosure of accounting policies for derivative financial instruments and derivative commodity instruments (collectively ''derivatives'') in the footnotes to the financial statements. In addition, the amendments expand existing disclosure requirements to include quantitative and qualitative information about market risk inherent in market risk sensitive instruments. The required quantitative and qualitative information should be disclosed outside the financial statements and related notes thereto. In addition, the quantitative and qualitative information will be provided safe harbor protection under a new Commission rule. Finally, this release reminds registrants that any disclosures about financial instruments, commodity positions, firm commitments, and anticipated transactions (''reported items''), should include disclosures about derivatives that directly or indirectly affect such reported items, to the extent such information is material and necessary to prevent the disclosures about the reported items from being misleading. In the aggregate, these amendments are designed to provide additional information about market risk sensitive instruments, which investors can use to better understand and evaluate the market risk exposures of a registrant.

DATES: Effective Date: April 11, 1997.

Compliance Dates: § 210.4–08(n) of Regulation S–X and the amendment to Item 310 of Regulation S–B shall apply, and disclosures under that rule shall be required, for filings with the Commission that include financial statements for fiscal periods ending after June 15, 1997. For bank and thrift registrants, as defined, and non-bank and non-thrift registrants with market capitalizations on January 28, 1997 in excess of $2.5 billion, Item 305 of Regulation S–K and Item 9A of Form 20–F shall apply, and disclosures under those items shall be required, for filings with the Commission that include annual financial statements for fiscal years ending after June 15, 1997. For non-bank and non-thrift registrants with market capitalizations on January 28, 1997 of $2.5 billion or less, Item 305 of Regulation S–K and Item 9A of Form 20–F shall apply, and disclosures under those items shall be required, for filings with the Commission that include annual financial statements for fiscal years ending after June 15, 1998. Under Item 305 of Regulation S–K and Item 9A of Form 20–F, interim information is not required until after the first fiscal year end in which Item 305 of Regulation S–K and Item 9A of Form 20–F are effective. Item 10(g) of Regulation S–B shall apply for filings with the Commission made on or after April 11, 1997.

FOR FURTHER INFORMATION CONTACT: Cathy J. Cole, Thomas J. Linsmeier, Russell B. Mallett, III, or Stephen M. Swad, at (202) 942–4400, Office of the Chief Accountant, Securities and Exchange Commission, 450 Fifth Street, N.W., Mail Stop 11–3, Washington, D.C. 20549, or Kurt R. Hohl, at (202) 942–2960, Division of Corporation Finance, Securities and Exchange Commission, 450 Fifth Street, N.W., Mail Stop 3–13, Washington, D.C. 20549.

SUPPLEMENTARY INFORMATION: The Commission is amending [1] Rule 4–08 of Regulation S–X [2] and adding a new Item 305 to Regulation S–K.[3]

The Commission also is making conforming amendments to Forms S–1, S–2, S–4, S–11, and F–4 [4] under the Securities Act of 1933,[5] and Rule 14a–3,[6] Schedule 14A,[7] and Forms 10, 20–F, 10–Q, and 10–K [8] under the Securities Exchange Act of 1934.[9]

I. Executive Summary

During the last several years, the use of derivative financial instruments, other financial instruments, and derivative commodity instruments [10] increased substantially.[11] The Commission recognizes that these instruments can be effective tools for managing exposures to market risk.[12] However, in using market risk sensitive instruments some registrants experienced significant, and sometimes unexpected, losses. Those losses

[1] The amendments were proposed in Securities Act Release No. 7250; Exchange Act Release No. 36643; Investment Company Act Release No. 21625; File No. S7–35–95 (December 28, 1995) [61 FR 578].

[2] 17 CFR 210.4–08. Item 310 of Regulation S-B, 17 CFR 228.310, also is amended to incorporate the changes to Rule 4–08 of Regulation S-X.

[3] 17 CFR Part 229.

[4] 17 CFR 239.11, 12, 25, 18, and 34.

[5] 15 U.S.C. 77a *et seq.*

[6] 17 CFR 240.14a–3.

[7] 17 CFR 240.14a–101.

[8] 17 CFR 249.210, 220f, 308a, and 310.

[9] 15 U.S.C. 78a *et seq.*

[10] See the instructions to Item 305 of Regulation S-K or Item 9A of Form 20-F, *infra,* for complete definitions of the terms ''derivative financial instruments,'' ''other financial instruments,'' and ''derivative commodity instruments.'' In brief, for purposes of this release: (1) Derivative financial instruments include futures, forwards, swaps, options, and other financial instruments with similar characteristics, (2) other financial instruments include, for example, investments, loans, structured notes, mortgage-backed securities, indexed debt instruments, interest-only and principal-only obligations, deposits, and other debt obligations, and (3) derivative commodity instruments include, to the extent such instruments are not derivative financial instruments, commodity futures, commodity forwards, commodity swaps, commodity options, and other commodity instruments with similar characteristics that are permitted to be settled in cash or with another financial instrument by contract or business custom. In addition, for purposes of this release, the terms (1) ''derivatives'' refer to derivative financial instruments and derivative commodity instruments, together, and (2) ''market risk sensitive instruments'' refer to derivative financial instruments, other financial instruments, and derivative commodity instruments, collectively.

[11] The worldwide notional/contract amounts for derivative financial instruments and derivative commodity instruments increased from $7.1 trillion in 1989 to $69.6 trillion in 1995. These notional amounts, while one way to measure derivative activities, do not represent a precise measure of the risk associated with these instruments. In many instances, the amount at risk is much smaller than the notional amount. See *Financial Derivatives: Actions Needed to Protect the Financial System*, United States General Accounting Office Report to Congressional Requesters (May 1994), and *Survey of Disclosures about Trading and Derivatives Activities of Banks and Securities Firms,* Basle Committee on Banking Supervision (''Basle Committee'') and the Technical Committee of the International Organisation of Securities Commissions (''IOSCO'') (November 1996).

[12] Market risk is the risk of loss arising from adverse changes in market rates and prices, such as interest rates, foreign currency exchange rates, commodity prices, and other relevant market rate or price changes (*e.g.,* equity prices). See Group of Thirty, *''Derivatives: Practices and Principles''* (July 1993), and Financial Accounting Standards Board (''FASB''), *Statement of Financial Accounting Standards No. 105, ''Disclosure of Information about Financial Instruments with Off-Balance-Sheet Risk and Financial Instruments with Concentrations of Credit Risk,''* (''FAS 105'') (March 1990), for similar definitions of market risk.

resulted from changes in interest rates, foreign currency exchange rates, and commodity prices, among other things. In light of those losses and the substantial growth in the use of market risk sensitive instruments, the adequacy of existing disclosures about market risk emerged as an important financial reporting issue.

During 1994 and 1995, the SEC staff reviewed annual reports filed with the Commission by approximately 500 registrants to better understand this emerging issue. In reviewing the annual reports, the staff intended to (i) assess the quality of current disclosures about market risk sensitive instruments, (ii) improve the quality of those disclosures through the comment process, and (iii) determine what, if any, additional disclosures are needed to help investors better assess the market risk inherent in those instruments. After reviewing the annual reports, the SEC staff noted that the 1995 disclosures were more informative than the 1994 disclosures, in part because of improved FASB disclosure guidance.[13] However, the staff observed three significant disclosure deficiencies, which are described in section II of this release. To address those deficiencies:

1. The Commission is amending Rule 4–08 of Regulation S–X and Item 310 of Regulation S–B to require enhanced descriptions of accounting policies for derivatives in the footnotes to the financial statements.[14]

2. The Commission is amending Regulation S–K to add Item 305 and Form 20–F to add Item 9A. Those amendments require disclosure of quantitative and qualitative information about market risk for derivatives and other financial instruments [15] and require that those disclosures be presented outside the financial statements.[16]

a. Items 305(a) and 9A(a) require registrants to disclose quantitative information about market risk sensitive instruments using one or more of the following alternatives:

i. Tabular presentation of fair value information and contract terms relevant to determining future cash flows, categorized by expected maturity dates;

ii. Sensitivity analysis expressing the potential loss in future earnings, fair values, or cash flows from selected hypothetical changes in market rates and prices; or

iii. Value at risk disclosures expressing the potential loss in future earnings, fair values, or cash flows from market movements over a selected period of time and with a selected likelihood of occurrence.

In preparing this quantitative information, registrants should categorize market risk sensitive instruments into instruments entered into for trading purposes [17] and instruments entered into for purposes other than trading. Within both the trading and other than trading portfolios, separate quantitative information should be presented for each market risk exposure category (i.e., interest rate risk, foreign currency exchange rate risk, commodity price risk, and other relevant market risks, such as equity price risk), to the extent material. Registrants may use different disclosure alternatives for each of the separate disclosures.

b. Items 305(b) and 9A(b) require registrants to disclose qualitative information about market risk. Those items require disclosure of:

i. a registrant's primary market risk exposures [18] at the end of the current reporting period;

ii. how the registrant manages those exposures (such as a description of the objectives, general strategies, and instruments, if any, used to manage those exposures); and

iii. changes in either the registrant's primary market risk exposures or how those exposures are managed, when compared to the most recent reporting period and what is known or expected in future periods.

c. Items 305 and 9A state that forward looking disclosures made pursuant to those items are within the statutory safe harbor under the Securities Act of 1933 and Securities Exchange Act of 1934.

3. The Commission reminds registrants that, when they provide disclosures about financial instruments, commodity positions, firm commitments, and anticipated transactions [19] (''reported items''), disclosures about derivatives that directly or indirectly affect such reported items also are required, to the extent the effects of such information are material and necessary to prevent the disclosures about the reported items from being misleading.

The amendments in Rule 4–08(n) and Item 310 relating to accounting policy disclosures apply to registered investment companies and small business issuers, among other registrants. In contrast, Item 305 and Item 9A do not apply to registered investment companies and small business issuers. However, if market risk represents a material known risk or uncertainty, small business issuers, like other registrants, will continue to be required to discuss those risks and uncertainties to the extent required by Management's Discussion & Analysis (''MD&A''). [20]

The amendments become effective over the next several months to provide registrants with time to respond to the new disclosure requirements. Rule 4–08(n) and the amendment to Item 310 will be effective for filings with the Commission that include financial statements for fiscal periods ending after June 15, 1997. For registrants that are likely to have experience with measuring market risk, such as banks, thrifts, and non-bank and non-thrift registrants with market capitalizations on January 28, 1997 in excess of $2.5 billion, Item 305 and Item 9A are effective for filings with the Commission that include annual financial statements for fiscal years ending after June 15, 1997. For other registrants, Item 305 and Item 9A are effective for filings with the Commission that include annual financial statements for fiscal years ending after June 15, 1998. Under Item 305 and Item 9A, interim information is

---

[13] See FASB, *Statement of Financial Accounting Standards No. 119, ''Disclosures about Derivative Financial Instruments and Fair Value of Financial Instruments,''* (''FAS 119'') (October 1994).

[14] Those disclosure requirements are applicable only to derivatives; the requirements do not relate to other financial instruments. Accounting policy disclosure requirements for other financial instruments are prescribed by existing generally accepted accounting principles and Commission guidance (see, *e.g.*, American Institute of Certified Public Accountants (''AICPA''), *Accounting Principles Board Opinion No. 22, ''Disclosure of Accounting Policies,''* (''APB 22'') (April 1972).

[15] Items 305 and 9A do not pertain solely to derivatives, but also to other financial instruments. Thus, disclosures under those Items are required for registrants that have material amounts of other financial instruments, even when they have no derivatives.

Items 305 and 9A also encourage registrants to include other market risk sensitive instruments, positions, and transactions (such as commodity positions, derivative commodity instruments that are not permitted by contract or business custom to be settled in cash or with another financial instrument, and cash flows from anticipated transactions) within the scope of their quantitative and qualitative disclosures about market risk. Registrants that select the sensitivity analysis or value at risk disclosure alternatives and voluntarily include those other market risk sensitive instruments, positions, and transactions within their quantitative disclosures about market risk are permitted to present comprehensive market risk disclosures, which reflect the combined effect of both the required and voluntarily selected instruments, positions, and transactions (see section III B.1.c.(vi) for details). Finally, if those other market risk sensitive instruments, positions, and transactions are not voluntarily included in the quantitative disclosures about market risk and, as a result, the disclosures do not fully reflect the net market risk exposures of the registrant, Items 305(a) and 9A(a) require that registrants discuss the absence of those items as a limitation of the disclosed market risk information.

[16] The term ''financial statements'' includes the footnotes to the financial statements. Therefore, the disclosures should be presented outside of the footnotes to the financial statements. See section III B.4.b., infra, for a more complete discussion about where these disclosures should appear.

[17] For purposes of this release, the term ''trading purposes'' has the same meaning as defined by generally accepted accounting principles (see, *e.g.*, FAS 119 ¶ 9a).

[18] See note 58, *infra*, for a definition specifying how the term ''primary market risk exposures'' is used in this release.

[19] For purposes of this release, ''anticipated transactions'' means transactions (other than transactions involving existing assets or liabilities or transactions necessitated by existing firm commitments) an enterprise expects, but is not obligated, to carry out in the normal course of business (see, *e.g.*, ¶ 9 of FASB, *Statement of Financial Accounting Standards No. 80, ''Accounting for Futures Contracts,''* (''FAS 80'') (August 1984)).

[20] See, *e.g.*, Item 303 of Regulation S-B, 17 CFR 228.303, and Item 303 of Regulation S-K, 17 CFR 229.303.

not required until after the first fiscal year end in which those Items are effective.

Taken together, Rule 4–08(n), Item 310, Item 305, and Item 9A represent one step by the Commission to improve disclosures about market risk to help investors better understand and evaluate a registrant's market risk exposures. The Commission recognizes the evolving nature of market risk sensitive instruments, market risk measurement systems, and market risk management strategies and, thus, intends to continue considering how best to meet the information needs of investors. In this regard, the Commission expects to monitor continuously the effectiveness of the new rules and final disclosure items issued today, as well as the need for additional proposals. Specifically, the Commission expects to reconsider these amendments after each of the following: (i) Issuance of a new accounting standard for derivatives by the FASB;[21] (ii) development in the marketplace of new generally accepted methods for measuring market risk; and (iii) a period of three years from the initial effective date of Item 305 and Item 9A.

II. Initiatives Regarding Disclosures About Derivatives and Market Risk

Certain private sector organizations expressed concerns that users of financial reports are dissatisfied with current disclosures about market risk sensitive instruments. For example, the Association for Investment Management and Research (''AIMR''), an organization of financial analysts, noted that users of financial information ''are confounded by the * * * complexity of financial instruments.''[22] In addition, after considerable investigation into the needs of investors and creditors, the American Institute of Certified Public Accountants' (''AICPA'') Special Committee on Financial Reporting stated:

> Users are confused. They complain that business reporting is not answering important questions, such as: * * * What [innovative financial] instruments has the company entered into, and what are their terms? How has the company accounted for those instruments, and how has that accounting affected the financial statements? What risks has the company transferred or taken on?[23]

In addition to identifying disclosure shortcomings, other organizations recommended improvements to disclosures about market risk sensitive instruments. These organizations include regulators, such as the General Accounting Office,[24] Group of 10 Central Bankers,[25] the Federal Reserve Bank of New York,[26] the Basle Committee and the Technical Committee of IOSCO,[27] and private sector bodies, such as the Group of Thirty[28] and a task force of the Financial Executives Institute (''FEI'').[29]

In general, those organizations stressed the need to make the risks inherent in market risk sensitive instruments more understandable. To that end, many recommended additional quantitative and qualitative disclosures about market risk. For example, the Federal Reserve Bank of New York recommended a new financial statement providing quantitative information about the overall market risk of an entity.[30] In addition, the FEI task force recommended that companies ''disclose some type of information which conveys overall exposure to market risk.''[31] The FEI task force specifically suggested two distinct approaches. One approach is to provide a high-level summary of relevant statistics about outstanding activity in market risk sensitive instruments at period end. The second approach is to communicate the potential loss that could occur under specified conditions using either value at risk or another comprehensive model for measuring market risk.[32]

In October 1994, the FASB, responding in part to calls for improved disclosure, issued FAS 119 (October 1994).[33] Among other things, FAS 119 prescribes disclosures in the financial statements about the policies used to account for derivative financial instruments and a discussion of the nature, terms, and cash requirements of derivative financial instruments. FAS 119 also encourages, but does not require, disclosure of quantitative information about an entity's market risk exposures.[34]

During 1994, in response, in part, to the concerns of investors, regulators, and private sector entities, the SEC staff reviewed the annual reports of approximately 500 registrants. In addition, during 1995 the SEC staff reviewed more recent annual reports to assess the effect of FAS 119 on disclosures about market risk sensitive instruments. In comparing the 1994 and 1995 annual reports, the SEC staff observed that FAS 119 had a positive effect on the quality of disclosures about derivative financial instruments. However, the staff concluded that investors still needed improved disclosures about market risk sensitive instruments. In particular, the SEC staff identified three primary disclosure issues:

1. Footnote disclosures of accounting policies for derivatives often were too general to convey adequately the diversity in accounting that exists for derivatives. Thus, it often was difficult to determine the impact of derivatives on registrants' statements of financial position, cash flows, and results of operations.
2. Disclosures about different types of market risk sensitive instruments often were reported separately. Thus, it was difficult to assess the aggregate market risk exposures inherent in these instruments.
3. Disclosure about reported items in the footnotes to the financial statements, MD&A, schedules, and selected financial data may not have reflected adequately the effect of derivatives on such reported items. Thus, information about the reported items may have been incomplete and could be misleading.

The Commission designed Rule 4–08(n), Item 310, Item 305, and Item 9A to address these issues. In forming these requirements, the Commission used the following guiding principles:

- Disclosures should make transparent the impact of derivatives on

[21] The FASB currently is working on a project to improve accounting recognition, measurement, and related disclosures for derivatives.

[22] See AIMR, *Financial Reporting in the 1990s and Beyond,* page 30, (1993).

[23] See AICPA Special Committee on Financial Reporting, *Improving Business Reporting—A Customer Focus: Meeting the Information Needs of Investors and Creditors,* at 76 (1994).

[24] See General Accounting Office, *Financial Derivatives: Actions Taken or Proposed Since May 1994* (November 1996).

[25] See Bank for International Settlements, *A Discussion Paper on Public Disclosure of Market and Credit Risks by Financial Intermediaries,* prepared by working group of the Euro-currency Standing Committee of the Central Banks of the Group of Ten Countries (September 1994).

[26] See Federal Reserve Bank of New York, *Public Disclosure of Risks Related to Market Activity: A Discussion Paper* (November 1994).

[27] See Basle Committee and the Technical Committee of IOSCO, *Framework for Supervisory Information about the Derivatives Activities of Banks and Securities Firms* (May 1995). *See also* Basle Committee and the Technical Committee of IOSCO, *Public Disclosure of the Trading and Derivatives Activities of Banks and Securities Firms* (November 1995).

[28] See Group of Thirty, *Derivatives: Practices and Principles* (July 1993).

[29] See FEI, *Derivative Financial Instruments Accounting and Disclosure Issues,* (''FEI Report'') prepared by FEI CCF/CCR Derivatives Disclosure Task Force (August 1994).

[30] See note 26, *supra.*

[31] See Attachment A, page 1 of FEI Report.

[32] See Attachment B, pages 5 and 6 of FEI Report.

[33] Similar standards were recently adopted by the International Accounting Standards Committee, the Canadian Institute of Chartered Accountants, and the Australian Accounting Standards Board. See *International Accounting Standards No. 32, ''Financial Instruments: Disclosure and Presentation,''* (''IAS 32'') (March 1995), Section 3860 of the *Handbook of the Canadian Institute of Chartered Accountants*, and the Australian Accounting Standards Board's accounting standard entitled, ''*Presentation and Disclosure of Financial Instruments*,'' (December 1996), respectively.

[34] See FAS 119 ¶ 12.

a registrant's statements of financial position, cash flows, and results of operations;

- Disclosures should provide information about a registrant's exposures to market risk;
- Disclosures should explain how market risk sensitive instruments are used in the context of the registrant's business;
- Disclosures about market risk exposures should not focus on derivatives in isolation, but rather should reflect the risk of loss inherent in all market risk sensitive instruments;
- Market risk disclosure requirements should be flexible enough to accommodate different types of registrants, different degrees of market risk exposure, and alternative ways of measuring market risk;
- Disclosures about market risk should address, where appropriate, special risks relating to leverage, option, or prepayment features; and
- New disclosure requirements should build on existing requirements, where possible, to minimize compliance costs.

III. Discussion of Amendments

A. Disclosure of Accounting Policies for Derivatives

1. Background

During the last several years, a significant number of issues relating to the accounting for derivatives have been raised. The FASB is working on a project that will address comprehensively the accounting for derivatives. However, currently there is little authoritative literature on the accounting for options and complex derivatives.[35]

In the absence of comprehensive accounting literature, registrants have developed accounting practices for options and complex derivatives by analogy to the limited amount of literature that does exist. Those analogies are complicated because, under existing accounting literature, there are at least three distinctly different methods of accounting for derivatives (*e.g.*, fair value accounting, deferral accounting, and accrual accounting).[36] Further, the underlying concepts and criteria used in determining the applicability of those accounting methods are not consistent.[37] As a result, during its 1994 and 1995 reviews of annual reports, the SEC staff observed that registrants with similar risk management objectives often accounted for derivatives with similar economic characteristics in different ways.[38] Thus, it was difficult to ascertain and compare the financial statement effects of derivatives among registrants.

To provide a better understanding of the accounting for derivative financial instruments, paragraph 8 of FAS 119 requires disclosure of the policies used to account for those instruments, pursuant to the requirements of APB 22.[39] Specifically, FAS 119 emphasizes the disclosure of ''policies for recognizing (or not recognizing) and measuring derivative financial instruments * * * and when recognized, where those instruments and related gains and losses are reported in the statements of financial position and income.''[40] Notwithstanding its helpful guidance, FAS 119 does not explicitly indicate the type of information that should be included in the accounting policies footnote to help investors understand the effects of derivatives on the statements of financial position, cash flows, and results of operations. FAS 119 also does not address disclosure of accounting policies for derivative commodity instruments.

2. Rule 4–08(n) of Regulation S-X and Item 310 of Regulation S-B

To facilitate a more informed assessment of the effects of derivatives on financial statements, Rule 4–08(n) and Item 310 explicitly require that seven items be disclosed in the derivatives accounting policies footnote, when material. For example, Rule 4–08(n) and Item 310 require a description of the methods used to account for derivatives, the types of derivatives accounted for under each method, and the criteria required to be met for each accounting method used. See Rule 4–08(n) and Item 310 for further requirements.

When assessing materiality under Rule 4–08(n) and Item 310, the Commission expects registrants to consider (i) the financial statement effects of all derivatives, including those not recognized in the statement of financial position and (ii) the relative effects of using the accounting method selected as compared to the other methods available (*e.g.*, accrual, deferral, or fair value methods of accounting).

In essence, Rule 4–08(n) and Item 310 clarify how the accounting policy disclosure requirements in FAS 119 should be applied to derivative financial instruments. They also extend those requirements to derivative commodity instruments. The Commission expects to reconsider the effectiveness of and the need for the accounting policy disclosures, prescribed under Rule 4–08(n) and Item 310, when a new accounting standard for derivatives is issued by the FASB.

---

[35] The authoritative accounting literature for options and complex derivatives generally is limited to a few consensuses from the FASB Emerging Issues Task Force (''EITF''), which by their nature address the accounting for specific transactions. See, *e.g.*, EITF Issues 88–8, ''*Mortgage Swaps*,'' and 90–17, ''*Hedging Foreign Currency Risks with Purchased Options*.''

[36] Under the fair value method, derivatives are carried on the balance sheet at fair value with changes in that value recognized in earnings or stockholders' equity (see, *e.g.*, FASB, *Statement of Financial Accounting Standards No. 52*, ''*Foreign Currency Translation*,'' (''FAS 52'') (December 1981), and FAS 80. Under the deferral method, gains and losses from derivatives are deferred on the balance sheet and recognized in earnings in conjunction with earnings of designated items (see, *e.g.*, FAS 52 and FAS 80). Under the accrual method, each net payment/receipt due or owed under the derivative is recognized in earnings during the period to which the payment/receipt relates; there is no recognition on the balance sheet for changes in the derivative's fair value (see, *e.g.*, EITF Issue 84–36, ''*Interest Rate Swap Transactions*'').

[37] For example, the risk reduction criterion in FAS 52 is different from the risk reduction criterion in FAS 80. FAS 52 specifies risk reduction on a transaction basis, while FAS 80 specifies risk reduction on an enterprise basis. In addition, FAS 80 permits the use of deferral accounting for futures contracts used to hedge probable, but not firmly committed, anticipated transactions, while FAS 52 prohibits deferral accounting for foreign currency forward exchange contracts used to hedge those same types of anticipated transactions.

[38] The Commission does not mean to imply by this statement that registrants may justify the use of any method of accounting for derivatives. Registrants must select appropriate accounting methods that are consistent with generally accepted accounting principles. In particular, generally accepted accounting principles require registrants using derivatives for trading, dealing, or speculative purposes to recognize those instruments on the balance sheet at fair value and to recognize changes in that value immediately in earnings (see, *e.g.*, FAS 80 ¶ 3).

[39] APB 22 ¶ 12 states:

Disclosure of accounting policies should identify and describe the accounting policies followed by the reporting entity and the methods of applying those principles that materially affect the determination of financial position, cash flows or results of operations. In general, the disclosure should encompass important judgments as to the appropriateness of principles relating to recognition of revenue and allocation of asset costs to current and future periods; in particular, it should encompass those accounting principles and methods that involve * * * a selection from existing acceptable alternatives.

The Accounting Principles Board was the predecessor to the FASB. Unless superseded by FASB Statements, APB Opinions continue to be regarded as the highest level of generally accepted accounting principles followed by the accounting profession. See generally *AICPA, Statements on Auditing Standards No. 69*, ''*The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles in the Independent Auditor's Report*,'' ¶ 5 (March 1992); AU § 411.05.

[40] See FAS 119 ¶ 60.

B. Disclosures of Quantitative and Qualitative Information About Market Risk

1. Quantitative Information About Market Risk

a. Nature of Disclosures. A primary objective of the quantitative disclosure requirements is to provide investors with forward looking information about a registrant's potential exposures to market risk. These quantitative disclosures are dependent on several choices about key model characteristics and assumptions (e.g., hypothetical changes in future market rates or prices).[41] By their nature, these forward looking choices are only estimates and will be different from what actually occurs in the future. As a result, actual future gains or losses will differ from those reported in the quantitative disclosures. For example, differences between actual and reported gains and losses will arise when (i) actual market rate or price changes differ from those estimated or (ii) the portfolio of market risk sensitive instruments held during the year differs from the portfolio held at the prior year-end.

Notwithstanding this limitation, the Commission believes that the reported market risk information should provide benefits to both investors and registrants. The quantitative disclosures should help investors better understand specific market risk exposures of different registrants, thereby allowing them to better manage market risks in their investment portfolios. Those disclosures also should provide a mechanism, where applicable, for registrants to disclose that their use of derivatives represents risk management, rather than speculation. Those disclosures are not precise indicators of expected future reported losses. Instead, depending on the modeling technique and assumptions used, they are indicators of remote or reasonably possible losses. Nevertheless, those disclosures should provide investors with important indicators of how a particular registrant views and manages its market risk.

The Commission has provided flexibility in the quantitative and qualitative disclosure requirements to accommodate different types of registrants, different degrees of market risk exposure, and alternative ways of measuring market risk. The Commission believes, at this time, that such flexibility is necessary and important to allow risk management and reporting practices to evolve, even though such flexibility is likely to reduce the comparability of disclosures. To address this comparability issue, registrants are required to disclose the key model characteristics and assumptions used in preparing the quantitative market risk disclosures. These disclosures are designed to allow investors to evaluate the potential impact of variations in those model characteristics and assumptions on the reported information. In addition, as more standard risk management practices and methods of reporting market risk are developed, the Commission anticipates reviewing the disclosure requirements with the view to enhancing comparability.

b. Background. Market risk is inherent in derivative and non-derivative instruments, including:

- Derivative financial instruments—futures, forwards, swaps, options, and other financial instruments with similar characteristics;
- Other financial instruments—non-derivative financial instruments, such as investments, loans, structured notes, mortgage-backed securities, indexed debt instruments, interest-only and principal-only obligations, deposits, and other debt obligations;
- Derivative commodity instruments that are permitted by contract or business custom to be settled in cash or with another financial instrument—commodity futures, commodity forwards, commodity swaps, commodity options, and other commodity instruments with similar characteristics, to the extent such instruments are not derivative financial instruments.

Generally accepted accounting principles and prior Commission rules already require disclosure of certain quantitative information pertaining to some of these instruments. For example, registrants are required to disclose notional amounts of derivative financial instruments and the nature and terms of debt obligations.[42] However, this information (i) often is abbreviated, (ii) is presented piecemeal in different parts of the financial statements, and (iii) does not apply to all market risk sensitive instruments. Thus, investors often have been unable to assess the net market risk exposures inherent in these instruments.

FAS 119 encourages, but does not require, disclosure of quantitative information about the market risk exposures inherent in market risk sensitive instruments.[43] However, without an explicit requirement, the Commission observed that registrants often were not making these disclosures.

c. Item 305(a) of Regulation S–K and Item 9A(a) of Form 20–F. In essence, Items 305(a) and 9A(a)[44] are designed to make disclosures about market risk more comprehensive by requiring disclosures of quantitative information about market risk, similar to those encouraged by FAS 119. Items 305(a) and 9A(a) apply to market risk sensitive instruments.

Under these Items, registrants should furnish quantitative information about market risk using one or more of three prescribed alternative methods.[45] The three alternative methods, described in detail below, are a tabular presentation, sensitivity analysis, and value at risk.

In preparing this quantitative information, registrants should categorize market risk sensitive instruments into instruments entered into for trading purposes and instruments entered into for purposes other than trading. Within both the trading and other than trading portfolios, separate quantitative information should be presented for each market risk exposure category (*i.e.*, interest rate risk, foreign currency exchange rate risk, commodity price risk, and other relevant market risks, such as equity price risk), when material.

A registrant may use (i) the same alternative for all market risk disclosures, (ii) one alternative, such as value at risk, for all disclosures related to instruments entered into for trading purposes, and another alternative, such as sensitivity analysis, for all disclosures related to instruments entered into for other than trading purposes, or (iii) different or the same alternatives for each category of market risk within the trading and other than trading portfolios.

(i) Tabular Presentation. The tabular presentation alternative permits

---

[41] The Commission believes that the exercise of discretion in making such choices by registrants should not subject registrants to liability with respect to private rights of action.

[42] See, *e.g.*, FAS 119 ¶ 8b and Rule 5–02 of Regulation S–X, 17 CFR 210.5–02, respectively.

[43] In particular, FAS 119 ¶ 12 lists five possible quantitative methods of measuring and disclosing market risk. They are: (i) Details about current positions and perhaps activity during the period, (ii) the hypothetical effects on equity, or on annual income, of several possible changes in market price, (iii) a gap analysis of interest rate repricing or maturity dates, (iv) the duration of the financial instruments, and (v) the entity's value at risk from derivative financial instruments and from other positions at the end of the reporting period and the average value at risk during the year.

[44] Item 9A(a) of Form 20–F, like the other portions of Item 9A, is substantively identical to related sections in Item 305.

[45] At the current time, the Commission is not prescribing standardized methods and procedures specifying how to comply with each of these disclosure alternatives. To facilitate comparison across registrants, however, Item 305(a) requires that registrants describe the model and assumptions used to prepare quantitative market risk disclosures.

registrants to provide quantitative information about market risk sensitive instruments in a tabular format. The required information includes the fair values of market risk sensitive instruments and contract terms sufficient to determine the future cash flows from those instruments, categorized by expected maturity dates. These tabular disclosures should present information sufficient to allow readers of the table to determine expected cash flows from market risk sensitive instruments for each of the next five years and the aggregate cash flows expected for the remaining years thereafter.[46] These tabular disclosure requirements were selected because expected cash flows are common inputs to market risk measurement methods and, therefore, are expected to help investors make estimates of a registrant's market risk exposures.

To facilitate an investor's ability to make such estimates, Items 305(a) and 9A(a) require that tabular information be grouped based on common market risk characteristics. In particular, those Items require separate presentation of tabular information for instruments: (i) Entered into for trading and other than trading purposes, (ii) subject to different categories of market risk exposure (*e.g.*, interest rate risk, foreign currency exchange rate risk, etc.), and (iii) subject to different market risk characteristics within a particular exposure category (*e.g.*, different functional currencies,[47] different underlying commodity exposures, different instrument types, and different contractual rates or prices). See Items 305(a)(1)(i) and 9A(a)(1)(i) for further requirements.

In particular, when preparing the tabular disclosures registrants should consider whether differences in market risk would be reflected better by separately presenting tabular information for a particular instrument or group of instruments. For example, Items 305(a)(1)(i) and 9A(a)(1)(i) require the grouping of options with similar strike prices. This grouping is required because option payouts can differ significantly depending how far the option is in or out of the money. Thus, the separate presentation of tabular information for options with dissimilar strike prices should enhance an investor's ability to determine the potential market risk inherent in those instruments. Registrants should make similar evaluations when determining which instruments should be grouped together within the tabular disclosures.

Items 305(a) and 9A(a) also require disclosure of information regarding the contents of the table and related assumptions necessary to understand a registrant's market risk disclosures. In this regard, registrants should describe, for example, the different amounts reported in the table for the various categories of the market sensitive instruments (*e.g.*, principal amounts for debt, notional amounts for swaps, and the different types of reported market rates or prices) and key prepayment or reinvestment assumptions relating to the timing of reported amounts. See Items 305(a)(1)(i) and 9A(a)(1)(i) for further details.

The Appendix to each of these Items provides a sample disclosure format.

(ii) Sensitivity Analysis. The sensitivity analysis disclosure alternative permits registrants to express the potential loss in future earnings, fair values, or cash flows of market risk sensitive instruments resulting from one or more selected hypothetical changes in interest rates, foreign currency exchange rates, commodity prices, and other relevant market rate or price changes (*e.g.*, equity prices) over a selected time period.[48] Items 305(a) and 9A(a) require that registrants select hypothetical changes in market rates and prices that are expected to reflect reasonably possible[49] near-term[50] changes in those rates and prices. Absent economic justification for the selection of a different amount, registrants should use changes that are not less than 10 percent of end of period market rates or prices.

Items 305(a) and 9A(a) also require a description of the model, assumptions, and parameters underlying the registrant's sensitivity analysis that are necessary to understand the registrant's market risk disclosure. In this regard, registrants are required to specify, for example, (i) how ''loss'' is defined by the model (*e.g.*, loss in earnings, fair values, or cash flows), (ii) a general description of the modeling technique (*e.g.*, the change in net present values arising from selected shifts in market rates or prices), (iii) the types of instruments covered by the model, and (iv) other relevant information about the model's assumptions and parameters (*e.g.*, the magnitude and timing of selected hypothetical changes in market rates or prices used). See Items 305(a)(1)(ii) and 9A(a)(1)(ii) for further requirements.

(iii) Value at Risk. The value at risk disclosure alternative permits registrants to express the potential loss in future earnings, fair values, or cash flows of market risk sensitive instruments over a selected period of time, with a selected likelihood of occurrence, from changes in interest rates, foreign currency exchange rates, commodity prices, and other relevant market rates or prices.[51] Items 305(a) and 9A(a) state that when preparing value at risk disclosures, registrants should select confidence intervals that reflect reasonably possible near-term changes in market rates and prices. In this regard, absent economic justification for the selection of different confidence intervals, registrants should use intervals that are 95 percent or higher.

For each category for which value at risk disclosures are presented, Items 305(a) and 9A(a) require registrants to provide either (i) the average, high and low amounts, or the distribution of value at risk amounts for the reporting period, (ii) the average, high and low amounts, or the distribution of actual changes in fair values, earnings, or cash flows from market risk sensitive instruments occurring during the reporting period, or (iii) the percentage or number of times the actual changes in fair values, earnings, or cash flows from market risk sensitive instruments exceeded the value at risk amounts during the reporting period.

Items 305(a) and 9A(a) also require a description of the model, assumptions, and parameters underlying the

[46] In some instances, the tabular presentation alternative is similar to the gap analysis commonly provided by financial institutions. Thus, with minor modifications, if any, those registrants could report a gap analysis and comply with the tabular information requirements.

[47] For purpose of Item 305 and Item 9A, functional currency means the currency of the primary economic environment in which the entity operates; normally, that is the currency of the environment in which an entity primarily generates and expends cash. This definition is the same as the definition of functional currency in FAS 52, Appendix E.

[48] The term ''sensitivity analysis,'' as used in Items 305(a) and 9A(a), describes a general class of models that assesses the risk of loss in market risk sensitive instruments based on hypothetical changes in market rates or prices. The term sensitivity analysis is not meant to refer to any one model for quantifying market risk. Sensitivity analysis models include, for example, duration analysis or other ''sensitivity'' measures already required to be calculated for regulatory purposes for thrift institutions (see Office of Thrift Supervision, *Regulatory Capital: Interest Rate Risk Component,* 12 CFR 567.5(c)(4) (August 1993)).

[49] See note 67, *infra,* for a definition of the term ''reasonably possible.''

[50] See note 66, *infra,* for a definition of the term ''near-term.''

[51] The term ''value at risk,'' as used in Items 305(a) and 9A(a), describes a general class of models that provides a probabilistic assessment of the risk of loss in market risk sensitive instruments. The term value at risk is not meant to refer to any one model for quantifying market risk. Value at risk models can be adapted to non-trading activities as well as trading activities and to non-financial institutions as well as financial institutions, depending on the model and assumptions selected by the registrant.

registrant's value at risk model that are necessary to understand the registrant's market risk disclosure. In this regard, registrants should specify, for example, (i) how ''loss'' is defined by the model (*e.g.*, loss in earnings, fair values, or cash flows), (ii) the type of model used (*e.g.*, variance/covariance, historical simulation, or Monte Carlo simulation and a description as to how optionality is addressed by the model), (iii) the types of instruments covered by the model, and (iv) other relevant information about the model's assumptions and parameters (*e.g.*, holding periods and confidence intervals).[52] See Items 305(a)(1)(iii) and 9A(a)(1)(iii) for further requirements.

(iv) An Alternative to Reporting Year-End Information. Items 305(a) and 9A(a) require disclosure of quantitative information about market risk as of the end of the latest fiscal year. Alternatively, registrants, such as those with proprietary concerns about reporting year-end information under the sensitivity analysis and value at risk disclosure alternatives, may report the average, high, and low amounts for the reporting period. In determining those average, high, and low amounts for the fiscal year, registrants should use sensitivity analysis or value at risk amounts relating to at least four equal time periods throughout the reporting period (*e.g.*, four quarter-end amounts, 12-month-end amounts, or 52 week-end amounts).

(v) Other Disclosure Requirements. Items 305(a) and 9A(a) require registrants to provide summarized quantitative information about market risk for the preceding fiscal year. In addition, registrants should discuss the reasons for material quantitative changes in market risk exposures between the current and preceding fiscal years.[53] In determining the amount and type of summarized information to be provided for the preceding fiscal year, registrants should evaluate whether sufficient information is disclosed to enable investors to assess material trends in quantitative market risk information. This summary should include information relating to each market risk exposure category disclosed in the preceding or latest fiscal year.

In addition, Items 305(a) and 9A(a) permit registrants to change disclosure alternatives or key model characteristics, assumptions, and parameters used in providing quantitative information about market risk (*e.g.*, changing from tabular presentation to value at risk, changing the scope of instruments included in the model, changing the definition of loss from fair values to earnings). However, if the effects of such a change are material,[54] registrants should (i) explain the reasons for the change and (ii) either provide summarized comparable information, under the new disclosure method, for the year preceding the current reporting period or, in addition to providing disclosure for the current year under the new method, provide disclosure for the current year and preceding fiscal year under the method used in the preceding year.

(vi) Encouraged Disclosures. The Commission recognizes that market risk exposures may exist in instruments, positions, and transactions other than in the market risk sensitive instruments specifically covered by Items 305 and 9A. In particular, market risk, in its broadest view, also may be inherent in the following items:

- Derivative commodity instruments that are not permitted by contract or business custom to be settled in cash or with another financial instrument—such as a commodity forward contract that must be settled in the commodity;
- Commodity positions—such as investments in corn, wheat, oil, gas, lumber, silver, gold, and other commodity inventory positions;
- Cash flows from anticipated transactions[55]—such as cash flows from anticipated purchases and sales of inventory, and operating cash flows from non-financial and non-commodity instruments (*e.g.*, cash flows generated by manufacturing activities); and
- Certain financial instruments not included among the required disclosure items—such as insurance contracts, lease contracts, and employers' and plans' obligations for pension and other post-retirement benefits.

The Commission also recognizes, however, that the amount and timing of the cash flows inherent in such instruments, positions, and transactions sometimes may be difficult to estimate. In addition, it has been represented to the staff that many risk measurement systems currently do not include such instruments, positions, and transactions in their quantitative assessments of market risk. For these practical reasons, the Commission is not requiring, at this time, that these items be included in the quantitative disclosures about market risk. Registrants, however, are encouraged to include such items within their quantitative market risk disclosures.

Registrants that choose the tabular presentation disclosure alternative should present voluntarily selected instruments, positions, or transactions in a manner consistent with the requirements in Items 305 and 9A for market risk sensitive instruments. Registrants selecting the sensitivity analysis or value at risk disclosure alternatives are not required to provide separate market risk disclosures for any voluntarily selected instruments, positions, or transactions. Instead, registrants selecting those disclosure alternatives are permitted to present comprehensive market risk disclosures, which reflect the combined market risk exposures inherent in both the required and any voluntarily selected instruments, position, or transactions.

If a registrant elects to include voluntarily a particular type of instrument, position, or transaction in their quantitative disclosures about market risk, that registrant should include all, rather than some, of those instruments, positions, or transactions within their disclosures. For example, if a registrant holds in inventory a particular type of commodity position and elects to include that commodity position within their market risk disclosures, the registrant should include the entire commodity position, rather than only a portion thereof, in their quantitative disclosures about market risk.

Finally, if instruments, positions, or transactions are not included voluntarily in the market risk disclosures and, as a result, the disclosures do not fully reflect the net market risk exposures of the registrant, the registrant should discuss the absence of those items as a limitation of the quantitative information, as discussed below.[56]

[52] The primary differences between the value at risk and sensitivity analysis disclosure alternatives are (i) value at risk analysis reports the potential loss arising from equally likely market movements across instruments, while sensitivity analysis reports the potential loss arising from hypothetical market movements with differing likelihoods of occurrence across instruments and (ii) value at risk explicitly adjusts the potential loss to reflect correlations between market movements, while sensitivity analysis is not designed explicitly to make such adjustments.

[53] For transition purposes, quantitative disclosures about market risk provided in the initial year in which a registrant must present information under Item 305 is not required to contain comparable summarized information for the preceding year. Similarly, in the first fiscal year in which a registrant must present information under Item 305, a discussion of the reasons for material changes in reported amounts as compared to the preceding year is not necessary.

[54] In this regard, the Commission believes that all changes from one disclosure alternative to another are material; however, other changes discussed in this section require judgment as to whether the effects of such changes are material.

[55] See note 19, *supra.*

[56] In addition, registrants should review the requirements of Item 303 of Regulation S–K, 17 CFR 229.303, to ensure their disclosures are sufficient to

(vii) Limitations. Items 305(a) and 9A(a) require registrants to discuss limitations that cause the quantitative information about market risk not to reflect fully the net market risk exposures of the entity. This discussion is to include a description of instruments, positions, and transactions omitted from the quantitative market risk disclosure information, or the features of instruments, positions, and transactions that are included, but not reflected fully in the quantitative information disclosed.

Two illustrative examples are provided. First, as just stated, certain instruments, positions, and transactions are excluded from the required quantitative disclosures about market risk, but may be included on a voluntary basis. The failure of a registrant to include voluntarily those instruments, positions, or transactions in the quantitative disclosures is a limitation of the quantitative information provided. This limitation should be discussed, if material, and a summarized description of the instruments, positions, or transactions not reflected fully within the quantitative market risk disclosures should be disclosed.

Second, the prescribed quantitative disclosures may not inform investors of the degree of market risk inherent in instruments with leverage, option, or prepayment features (*e.g.,* options, including written options, structured notes, collateralized mortgage obligations, leveraged swaps, and options embedded in swaps). Tabular information on fair values and contract terms may not necessarily indicate that instruments have such features. Similarly, if leverage, option, or prepayment features are triggered by changes in market rates or prices outside those reflected in the value at risk and sensitivity analysis disclosures, the potential loss from such market rate or price changes may be significantly larger than would be implied by a simple linear extrapolation of the reported numbers. Thus, to make investors fully aware of the market risk inherent in instruments with such features, Item 305(a) and Item 9A(a) require a discussion of this limitation, including a summarized description of the features of the instruments causing the limitation.

2. Qualitative Information About Market Risk

a. Background. The Commission believes that quantitative information about market risk is more meaningful when accompanied by qualitative disclosures about a registrant's market risk exposures and how those exposures are managed. Such qualitative disclosures help investors understand a registrant's market risk management activities and help place those activities in the context of the business.

FAS 119 requires qualitative disclosures about market risk management activities associated with certain derivative financial instruments. In particular, FAS 119 requires disclosure of ''the entity's objectives for holding or issuing the derivative financial instruments, the context needed to understand those objectives, and its general strategies for achieving those objectives.'' [57] However, the qualitative disclosure requirements of FAS 119 only apply to derivative financial instruments held or issued for purposes other than trading.

b. Item 305(b) and Item 9A(b). Items 305(b) and 9A(b) expand the qualitative market risk disclosure requirements of FAS 119 to (i) Encompass derivative commodity instruments, other financial instruments, and derivative financial instruments entered into for trading purposes and (ii) require registrants to evaluate and describe material changes in their primary risk exposures and in how those exposures are managed. In particular, Items 305(b) and 9A(b) require a description of (i) a registrant's primary market risk exposures [58] as of the end of the latest fiscal year, (ii) how those exposures are managed (such descriptions should include, but not be limited to, a discussion of the objectives, general strategies, and instruments, if any, used to manage those exposures), and (iii) changes in either the registrant's primary market risk exposures or in how those exposures are managed, when compared to what was in effect during the most recently completed fiscal year and what is known or expected to be in effect in future reporting periods.

Items 305(b) and 9A(b) apply to market risk sensitive instruments. In addition, the qualitative disclosures required by these items should be presented separately for market risk sensitive instruments entered into for trading purposes and those entered into for purposes other than trading.

Finally, to help make disclosures about market risk more comprehensive, the Commission encourages registrants to include within their qualitative disclosures about market risk, certain instruments, positions, and transactions not required under Items 305(b) and 9A(b). Those instruments, positions, and transactions include derivative commodity instruments not permitted by contract or business custom to be settled in cash or with another financial instrument, commodity positions, cash flows from anticipated transactions, and certain financial instruments not included among the required disclosure items. See Items 305(b) and 9A(b) for further requirements.[59]

If a registrant elects not to include those instruments, positions, and transactions in its qualitative disclosures about market risk, the Commission reminds registrants to consider whether qualitative disclosures about the market risk inherent in those items would be required under (i) Items 101 or 303 of Regulation S–K [60] or (ii) Rules 12b–20 under the Securities Exchange Act of 1934 (''Exchange Act'') or 408 under the Securities Act of 1933 (''Securities Act'') [61] Item 101 of Regulation S–K requires disclosures relating to a ''Description of the Business.'' Item 303 requires discussion of known risks and uncertainties within ''Management's Discussion and Analysis.'' Rule 12b–20 under the Exchange Act and Rule 408 under the Securities Act state that registrants should include in any filings or reports any material information necessary to make statements made, in light of the circumstances, not misleading.

3. Safe Harbor for Forward Looking Information

In the release proposing Item 305 and Item 9A, the Commission noted its intention to consider the application of an appropriate safe harbor to the

inform readers of material risks to which a registrant is exposed.

[57] See FAS 119 ¶ 11a. Footnote 4 of FAS 119 illustrates the qualitative disclosures required by ¶ 11a. That footnote states:

If an entity's objective for a derivative position is to keep a risk from the entity's non-derivative assets below a specified level, the context would be a description of those assets and their risks, and a strategy might be purchasing put options in a specified proportion to the assets at risk.

[58] For purposes of Items 305(b) and 9A(b), primary market risk exposures mean (i) the following categories of market risk: Interest rate risk, foreign currency exchange rate risk, commodity price risk, and other relevant market rate or price risks (*e.g.*, equity price risk) and (ii) within each of these categories, the particular markets that present the primary risks of loss to the registrant. For example, if a registrant (i) has a material exposure to foreign currency exchange rate risk and, within this category of market risk, (ii) is most vulnerable to changes in dollar/yen, dollar/pound, and dollar/peso exchange rates, the registrant should disclose those exposures.

[59] See section III B.1.c.(vi), *supra*, for a discussion as to why these instruments are encouraged, but not required, to be included in disclosures about market risk.

[60] See 17 CFR 228.101 and 17 CFR 228.303, respectively.

[61] See 17 CFR 240.12b-20 and 17 CFR 230.408, respectively.

forward looking aspects of the disclosures. Such a safe harbor subsequently was proposed for public comment,[62] and the Commission is adopting that provision substantially as proposed.

As adopted, the safe harbors for forward looking statements provided in Section 27A of the Securities Act and Section 21E of the Exchange Act apply to quantitative information about market risk provided outside the financial statements and related notes thereto, all of which, as described further below, is deemed to be a forward looking statement for purposes of the safe harbor, pursuant to Item 305(a) or Item 9A(a); qualitative information about market risk provided outside the financial statements and related notes thereto, pursuant to Item 305(b) or Item 9A(b); and interim information provided pursuant to Item 305(c) and Item 9A(c).

As proposed, the safe harbor would have applied to information disclosed pursuant to Items 305 and 9A regardless of whether the information was set forth in the notes to the financial statements or elsewhere in a registrant's required filings. As discussed below,[63] the Commission has determined that information required by Items 305 and 9A should be disclosed outside of the financial statements and related notes thereto. Similarly, as adopted, the safe harbor applies only to information located in accordance with the revised rule.

The safe harbors are available with respect to the specified information, regardless of whether the issuer providing it or the type of transaction otherwise is excluded from the statutory safe harbors. For example, first-time Commission registrants and those making initial public offerings are covered by the safe harbors with respect to this specific information if all other conditions are satisfied.

As is the case with the statutory safe harbors, however, the safe harbors adopted pursuant to this release apply only to a forward looking statement made by: (i) An issuer, (ii) a person acting on behalf of the issuer, (iii) an outside reviewer retained by the issuer making a statement on behalf of the issuer, or (iv) an underwriter, with respect to information provided by the issuer or information derived from information provided by the issuer.

The Commission recognizes that, due to the difficult nature of the disclosures, some registrants may require assistance in preparing the information required by Items 305 and 9A. For example, registrants may need assistance from third parties with respect to compiling the required information, assessing the reasonableness of management's assumptions, or testing the mathematical computations that translate the assumptions into the required disclosures. Moreover, some registrants may wish to have outside third parties review the information prior to its disclosure. The Commission considers such assistance and reviews relating to forward looking disclosure required by Items 305 and 9A to be ''made by an outside reviewer retained by the issuer making a statement on behalf of the issuer'' under the safe harbor rule.

The rule now clarifies two additional points about the application of the new safe harbor rules. First, the Commission deems all information required by paragraphs (a), (b)(1)(i), (b)(1)(iii) and (c) of Items 305 and 9A to be ''forward looking statements'' for purposes of the new safe harbor rules, except for historical facts such as the terms of particular contracts and number of market risk sensitive instruments held during or at the end of the reporting period. To the extent that information provided pursuant to paragraph (b)(1)(ii) of Items 305 and 9A includes forward looking statements, those statements would be eligible for safe harbor protection.

Second, the ''meaningful cautionary statements'' prong of the safe harbors will be satisfied with respect to the Items 305(a) and 9A(a) disclosures if a registrant satisfies the requirements of those Items. In this regard, the Commission notes that Items 305(a) and 9A(a) require disclosure of both the assumptions underlying, and the limitations of, the disclosure provided. For the remainder of the information required by the new items, registrants desiring to qualify for the ''meaningful cautionary statements'' prong of the safe harbor will need to consider what information should be given to alert investors to important factors that could cause actual results to differ materially from the information given in the forward looking statements.[64]

Finally, although Item 305 and Item 9A information is not required of small business issuers (as defined by Commission rule),[65] the safe harbors are available to those small issuers that voluntarily choose to disclose such information. Similarly, the safe harbors are available to non-small business issuers who voluntarily disclose information under Item 305(a) and Item 9A(a) prior to the June 15, 1997 and June 15, 1998 effective dates.

4. Implementation Issues Relating to Quantitative and Qualitative Disclosures About Market Risk

a. Disclosure Threshold. Under Items 305 and 9A, quantitative and qualitative disclosures about market risk are required, when material, for each market risk exposure category within the trading and other than trading portfolios. For purposes of assessing materiality, registrants should evaluate both (i) the materiality of the fair values of market risk sensitive instruments outstanding as of the end of the latest fiscal year and (ii) the materiality of potential near-term [66] losses in future earnings, fair values, and cash flows from reasonably possible [67] near-term changes in market rates or prices.

If either (i) or (ii) in the previous paragraph are material, the registrant should disclose quantitative and qualitative information about market risk, if such market risk for the particular market risk exposure category is material. However, the choice of methods, model characteristics, assumptions, and parameters used to comply with the quantitative market risk disclosures remain at the election of the registrant, provided disclosure is made regarding a material risk of loss in either earnings, fair values, or cash flows.

For example, if a registrant expects a material near-term loss in fair values only, that registrant should not report quantitative market risk information in terms of earnings or cash flows, rather than fair values. In these circumstances, the registrant could, of course, make additional quantitative disclosures about the loss in earnings or cash flows, but should disclose the risk of loss in fair values. In contrast, if a registrant is required to disclose market risk information because near-term losses in future earnings, fair values, and cash

[62] Securities Act Release No. 7280; Exchange Act Release No. 37086; File No. S7–10–96 (April 9, 1996) [61 FR 16672].

[63] See section III B.4.b., *infra*, for a discussion about where these disclosures should appear.

[64] Registrants are reminded that the safe harbor requires that forward looking statements be identified as such.

[65] 17 CFR part 228, *et seq.*

[66] For the purposes of Item 305 and Item 9A, the term ''near-term'' means a period of time going forward up to one year from the date of the financial statements. See generally AICPA, Statement of Position 94–6, *Disclosure of Certain Significant Risks and Uncertainties,* at paragraph 7 (December 30, 1994).

[67] For purposes of Item 305 and Item 9A, the term ''reasonably possible'' is defined by ¶ 3 of FASB, *Statement of Financial Accounting Standards No. 5, ''Accounting for Contingencies''* (''FAS 5'') (March 1975), which states that ''reasonably possible'' means the chance of a future transaction or event occurring is more than remote but less than likely.

flows all are material, it may report quantitative information in terms of either earnings, fair values, or cash flows.

In assessing the materiality of the fair values of market risk sensitive instruments, those fair values generally should not be netted, except to the extent allowed under *FASB Interpretation No. 39, ''Offsetting of Amounts Related to Certain Contracts''* (''Interpretation 39'') (March 1992).[68] For example, the fair value of assets generally should not be netted with the fair value of liabilities. Instead, the fair values of such instruments should be aggregated, without netting, for purposes of assessing materiality.

In assessing the materiality of potential near-term losses in future earnings, fair values, or cash flows from reasonably possible near-term changes in market rates or prices, registrants should consider (i) The magnitude of past market movements, (ii) the magnitude of reasonably possible, near-term market movements, and (iii) potential losses that may arise from leverage, option, and multiplier features.

b. Location of Quantitative and Qualitative Disclosures. As adopted, Items 305 and 9A require that the quantitative and qualitative market risk disclosures be placed outside the financial statements and related notes thereto. As proposed, registrants would have been permitted to disclose such information in the notes to the financial statements. Because of the evolving nature of the disclosures and the FASB's pending project on accounting for derivatives, which also will address disclosures about derivatives within the financial statements, the Commission has determined that the better course, at this time, is to require that the disclosures mandated by Items 305 and 9A be located outside of the financial statements and related notes.

The Commission believes that the information required by Items 305 and 9A should be included in the annual report delivered to shareholders; consequently Rule 14a–3 of the proxy rules has been amended to include this requirement. For other documents delivered to investors, the information should be included or incorporated by reference from other Commission filings.

c. Cross-Referencing of Disclosures. The Commission believes it is most meaningful to disclose together, in one location, quantitative and qualitative information relating to the same market risk exposure category. However, because market risk sensitive instruments often are used to manage known risks and uncertainties in market rates and prices, the disclosures provided under Items 305 and 9A may overlap with disclosures provided under Item 303 of Regulation S–K. To the extent that the disclosures in a registrant's MD&A satisfy the requirements of Items 305 or 9A, registrants need not repeat this information elsewhere in their filings. If this information is disclosed in more than one location, however, registrants should ensure that the resulting disclosures are meaningful to investors and provide cross-references to the locations of the related disclosures.

d. Application to Registrants. Items 305 and 9A are required to be followed by many different types of registrants, including, for example, commercial and industrial companies, financial institutions, broker-dealers, service companies, business development companies, and companies registering insurance contracts, such as market-value adjusted annuities and real estate funds underlying annuity contracts. Items 305 and 9A do not apply to registered investment companies and, as described further in Section IV, small business issuers.

e. Reporting Frequency. Items 305 and 9A apply to all registration statements filed under the Securities Act and all reports, proxy statements, and information statements filed under the Exchange Act that are required to include or incorporate financial statements. However, for reports that include only interim financial statements (*e.g.,* Form 10–Qs), registrants need only present market risk information if there have been material changes in reported market risks faced by the registrant since the end of the most recent fiscal year. In these circumstances, registrants should provide a discussion and analysis that enables investors to assess the sources and effects of those material changes in market risks.

IV. Applicability of Amendments

A. Application to Small Business Issuers

The Commission believes that because of (i) The evolving nature of these disclosures and (ii) the relative costs of complying with these disclosures for small business issuers,[69] it is appropriate, at this time, to exempt small business issuers from disclosing quantitative and qualitative information about market risk.[70]

Accordingly, at this time, the Commission is not adopting amendments to Regulation S–B to incorporate an item similar to Item 305. Small business issuers, however, are required (i) To comply with the amendment regarding accounting policies disclosures for derivatives, (ii) to comply with Rule 12b–20 under the Exchange Act and Rule 408 under the Securities Act, which require registrants to provide additional information about the material effects of derivatives on other information expressly required to be filed with the Commission, and (iii) to the extent market risk represents a known trend, event, or uncertainty, to discuss the impact of market risk on past and future financial condition and results of operations, pursuant to Item 303 of Regulation S–B.

B. Application to Foreign Private Issuers

Item 9A of Form 20–F requires disclosure by all foreign private issuers of quantitative and qualitative information about market risk. In addition, foreign private issuers that prepare financial statements in accordance with Item 18 of Form 20–F are required to provide all information required by U.S. generally accepted accounting principles and Regulation S–X, including descriptions in the footnotes to the financial statements of the policies used to account for derivatives. Foreign private issuers that prepare financial statements in accordance with Item 17 of Form 20–F are not required to provide financial statement disclosures required by U.S. generally accepted accounting principles and Regulation S–X. The amendments requiring disclosures of accounting policies in Rule 4–08(n) of Regulation S–X do not apply to foreign private issuers filing under Item 17 of Form 20–F. However, foreign private

[68] Interpretation 39 states that it is a general principle of accounting that the offsetting of assets and liabilities in the balance sheet is improper except where a right of set off exists. Interpretation 39 defines right of set off and specifies what conditions must be met to have that right. FAS 119 ¶ 15(d) in disclosing the fair values of instruments also prohibits the netting of fair values, except to the extent that the offsetting of carrying amounts in the statement of financial position is permitted under Interpretation 39.

[69] ''Small business issuer'' is defined to mean any entity that (1) Has revenues of less than $25,000,000, (2) is a United States or Canadian issuer, (3) is not an investment company, and (4) if a majority owned subsidiary, the parent corporation is also a small business issuer. An entity is not a small business issuer, however, if it has a public float (the aggregate market value of the outstanding securities held by non-affiliates) of $25,000,000 or more. See 17 CFR 230.405.

[70] Small business issuers will not be required to provide these market risk disclosures whether or not they file on specially designated small business forms.

In addition, as noted elsewhere in this release, the Commission has extended the safe harbor for forward looking information to Item 305 disclosures that are made voluntarily by small business issuers.

issuers filing under Item 17 of Form 20–F should consider the guidance presented in Staff Accounting Bulletin Topic 1:D (''SAB Topic 1:D'') to determine if information regarding accounting policies for derivatives should be provided in MD&A.[71]

C. Scope and Definition of Instruments

The instructions to Rule 4–08(n), Item 305, and Item 9A define financial instruments, derivative financial instruments, other financial instruments, and derivative commodity instruments as follows. ''Financial instruments'' have the same meaning as defined by generally accepted accounting principles (see, *e.g.*, FASB, *Statement of Financial Accounting Standards No. 107, ''Disclosures about Fair Value of Financial Instruments,''* (''FAS 107'') paragraphs 3 and 8 (December 1991)). ''Derivative financial instruments'' are a subset of financial instruments and include futures, forwards, swaps, options, and other financial instruments with similar characteristics, as defined by generally accepted accounting principles (see, *e.g.*, FAS 119 paragraphs 5–7 (October 1994)). See, the General Instructions to Paragraphs 305(a) and 305(b) of Item 305 or the General Instructions to Paragraphs 9A(a) and 9A(b) of Item 9A for further details.

Other financial instruments include all financial instruments that must be disclosed at fair value under FAS 107, except for derivative financial instruments, as defined above. For example, other financial instruments include trade accounts receivable, investments, loans, structured notes, mortgage-backed securities, trade accounts payable, indexed debt instruments, interest-only and principal-only obligations, deposits, and other debt obligations. However, for purposes of this release, trade accounts receivable and trade accounts payable need not be considered other financial instruments when their carrying amounts approximate fair value. Other financial instruments exclude employers' and plans' obligations for pension and other post-retirement benefits, substantively extinguished debt, insurance contracts, lease contracts, warranty obligations and rights, unconditional purchase obligations, investments accounted for under the equity method, minority interests in consolidated enterprises, and equity instruments issued by the registrant and classified in stockholders' equity in the statement of financial position.

Derivative commodity instruments include, to the extent such instruments are not derivative financial instruments, commodity futures, commodity forwards, commodity swaps, commodity options, and other commodity instruments with similar characteristics, that are permitted by contract or business custom to be settled in cash or with another financial instrument.

Thus, the instrument definitions described above do not encompass (i) commodity positions, (ii) derivative commodity instruments that are not permitted by contract or business custom to be settled in cash or with another financial instrument (*e.g.*, a commodity forward contract that must be settled in the commodity), (iii) cash flows from anticipated transactions, (*e.g.*, operating cash flows from non-financial and non-commodity instruments), and/or (iv) certain financial instruments not included among the required disclosure items.[72]

V. Disclosure of the Effects of Derivative Instruments on Disclosures about Financial Instruments, Commodity Positions, Firm Commitments, and Anticipated Transactions

In conjunction with the adoption of Items 305 and 9A, the Commission reminds registrants that other reporting obligations also require certain disclosures about derivatives. The staff's 1994 and 1995 reviews of registrant filings suggested that some registrants are not providing sufficient disclosure about how derivatives directly or indirectly affect reported items. As a result, those disclosures may not have reflected as well as they otherwise might have such matters as the effective terms or expected cash flows of the derivatives and reported items.

It is fundamental that registrants include in any filings or reports any material information necessary to make statements made, in light of the circumstances, not misleading.[73] That is, registrants should provide disclosure about derivatives that affect, directly or indirectly, the terms, fair values, or cash flows of the reported items. This includes derivative transactions that are designated to reported items under generally accepted accounting principles.[74]

Thus, for example, information required to be disclosed in the footnotes to the financial statements about the interest rates and repricing characteristics of debt obligations should include, when material, information about the effects of derivatives. Similarly, summary information and disclosures in MD&A about the interest costs of debt obligations should include, when material, disclosure of the effects of derivatives. Likewise, when derivatives directly or indirectly affect the terms and cash flows of items such as securities held as assets, servicing rights, oil and gas reserves, loan receivables, deposit liabilities, and leases, disclosure about the terms and cash flows of those items should include, when material, disclosure of the effects of derivatives to the extent such disclosure is necessary to prevent the disclosure about the reported item from being misleading.

VI. Response to Comments

A. Accounting Policies

1. Disclosure Threshold

In the proposing release, disclosures of accounting policies for derivatives would have been required if the fair values of derivative financial instruments and derivative commodity instruments were material. Commenters noted that the disclosure threshold in the proposing release is different than the threshold provided by generally accepted accounting principles (*i.e.*, APB 22) and Regulation S–X. These commenters indicated that introducing a new and different threshold could add unnecessary confusion to the disclosure process. In response to those commenters, the disclosure threshold in the final rule relies on the standards of materiality present in APB 22 and Regulation S–X. APB 22 requires disclosure of accounting policies that materially affect the determination of financial position, cash flows, or results of operations. Regulation S–X limits the information to those matters about which an average prudent investor ought reasonably be informed.

2. Future Reconsideration

Some commenters urged the Commission to coordinate its efforts with the FASB, especially by committing to review the accounting policies disclosure requirements after the FASB completes its derivatives and hedging project. Those commenters

[71] SAB Topic 1:D provides several examples of disclosures in MD&A that might be necessary to enable readers to understand the financial statements as a whole. One of those example disclosures includes significant accounting policies and measurement assumptions which may bear upon an understanding of operating trends or financial condition.

[72] See section III B.1.c.(vi), *supra*, for a further description of the instruments, positions, and transactions described in this paragraph.

[73] See, *e.g.*, Rule 12b–20 under the Exchange Act and Rule 408 under the Securities Act.

[74] See, *e.g.*, FAS 52 ¶ 21a and FAS 80 ¶ 4a.

suggested that when the accounting for derivatives is addressed comprehensively by the FASB, rules explicitly prescribing the content of derivative accounting policy disclosures may no longer be necessary. In response to those commenters concerns, after the FASB completes its project, the Commission will direct its staff to review Rule 4–08(n) and Item 310 and to recommend whether the Commission should amend those items.

B. Quantitative Disclosures About Market Risk

1. Different Alternatives for Different Categories of Instruments

A number of commenters recommended that the same quantitative market risk disclosure alternative not be required (i) For instruments entered into for trading and other than trading purposes and (ii) for each market risk exposure category (*e.g.*, interest rates, foreign currency exchange rates, and commodity prices) within the trading and other than trading portfolios. For example, some commenters indicated that market risk inherent in trading portfolios is evaluated using one approach, such as value at risk, and market risk inherent in the other than trading portfolios is evaluated using another approach, such as sensitivity analysis. Similarly, some commenters suggested that instruments exposed to foreign currency exchange rate risk are evaluated using one approach, while instruments exposed to interest rate risk are evaluated using another approach.

Those commenters suggested that Items 305(a) and 9A(a) permit the use of different quantitative disclosure alternatives for the market risks inherent in (i) The trading and other than trading portfolios and (ii) different market risk exposure categories within each of these portfolios. Due to the evolving nature of market risk management technologies, the Commission has decided it is too early to require that the same disclosure alternative be used to report market risk across (i) The trading and other than trading portfolios and (ii) each market risk exposure category within those portfolios. The Commission, therefore, has revised the disclosure items to permit the use of more than one disclosure alternative across each of those categories.

2. Use of Additional Disclosure Methods

Some commenters suggested adding an alternative that would allow disclosure of quantitative information about market risk using a ''management approach''; that is, the approach that management uses internally to manage market risk. They commented that the approaches in the proposing release (i) Do not appear to allow gap and duration analyses, which are currently used by some to measure market risk and (ii) may become outdated as new measurement approaches are developed in the market place. Other commenters, however, support more consistent reporting and requested that the Commission limit the quantitative disclosure alternatives for the sake of comparability.

The approach taken in the final disclosure items strikes a balance between the different commenters' perspectives. The Commission believes that the final disclosure items allow most registrants, if they so desire, to report market risk using one or more of four common methods of managing market risk. These methods are: (i) Gap analysis, (ii) duration, (iii) sensitivity analysis, and (iv) value at risk. Gap analysis is a tabular disclosure approach and with minor revision would satisfy the tabular disclosure requirements. Likewise, duration is a form of sensitivity analysis and with minor revision would satisfy the sensitivity analysis disclosure requirements.

Registrants that do not internally manage market risk using any of these four common quantitative methods, however, still are required to report market risk disclosures using the methods specified by the final disclosure items. The Commission believes that reporting using a management approach outside of this framework could result in disclosures that could make it difficult for investors to assess market risk.

Finally, to address commenters concerns that the alternatives for reporting market risk may become outdated, the Commission expects the staff to review the disclosure requirements periodically and to recommend amendments to those requirements, when appropriate, to reflect new developments in market risk management techniques.

3. Proprietary Information

Some commenters indicated that they were concerned that the proposed quantitative disclosure requirements, particularly the tabular disclosure, would result in presentation of proprietary information. They expressed concern that the tabular information required by the proposal was so detailed and disaggregated that competitors, suppliers, and market traders potentially may be able to use the information to exploit the registrants' positions in the market. Other commenters maintained that, in certain limited circumstances, period-end reporting of sensitivity analysis and value at risk amounts also may reveal proprietary information. Of principal proprietary concern were the requirements to disclose market risk information for derivative commodity instruments at both year-end and quarter-end.

After careful consideration of these comments, the Commission has determined to require disclosure of quantitative information about market risk. However, the final disclosure items include the following four provisions to address proprietary concerns. First, the final disclosure items contain two alternatives for providing quantitative information about market risk (*i.e.*, sensitivity analysis and value at risk), which do not require disclosure of detailed information about specific positions held by the registrant at period end. Second, the final disclosure items allow registrants with concerns about reporting fiscal year-end information, to report the average, high, and low sensitivity analysis or value at risk amounts for the reporting period, instead of requiring the reporting of potentially proprietary year-end information. Third, for interim reporting, the final disclosure items require registrants to provide a discussion and analysis of the sources and effects of material changes in market risk information since the end of the preceding fiscal year, rather than requiring that registrants always furnish complete Item 305(a) or Item 9A(a) information when such material changes occur. Fourth, registrants selecting the sensitivity analysis or value at risk disclosure alternatives are not required to provide separate market risk disclosures for any voluntarily selected instruments, positions, or transactions. Instead, registrants selecting the sensitivity analysis and value at risk disclosure alternatives are permitted to present comprehensive market risk disclosures, which reflect the combined market risk exposures inherent in both the required and voluntarily selected instruments, positions, and transactions. Such comprehensive disclosures do not reveal proprietary information about the relative amount of market risk inherent in market risk sensitive instruments and any voluntarily selected instruments, positions, and transactions.

4. Static Disclosures, Dependence on Assumptions

Some commenters criticized the sensitivity analysis and value at risk disclosures as being too dependent on assumptions. They also commented that sensitivity analysis and value at risk measures are static and may not yield amounts that fairly represent the dynamic nature of market risk.

The Commission has considered those comments and has determined to continue to permit use of both the sensitivity analysis and value at risk disclosure alternatives for the following primary reasons. First, the sensitivity analysis and value at risk disclosure alternatives are the most common and widely accepted methods of measuring net market risk exposures currently available in the market place. Second, while the reported quantitative information depends on assumptions, registrants are required to disclose key assumptions, which should allow investors to assess the quality of those assumptions and evaluate the potential impact of variations in those assumptions on the reported information. Third, an evaluation of reported quantitative information about market risk, over time, should help investors assess the dynamic nature of that risk.

5. Summarized Tabular Information

Some commenters indicated that the proposed tabular presentation of terms and information related to market risk sensitive instruments would produce lengthy and complex disclosures. They also asserted that grouping (i) foreign currency sensitive instruments by functional currency and (ii) other instruments by the common characteristics specified in the proposing release (*e.g.*, fixed or variable rate assets or liabilities, long or short forwards or futures, etc.) would be burdensome for registrants and the resulting information complex to analyze. Those commenters suggested that more summarized information be permitted in the tables. Finally, other commenters suggested that the proposal was unclear as to the information that must be disclosed, particularly with regard to options instruments.

The Commission is concerned that highly summarized tabular information will not allow investors to analyze and develop an understanding of a registrant's market risk exposures. Thus, the grouping requirements in the proposed disclosure items have not been changed substantially in this release. However, the Commission has revised the instructions to the final disclosure items to permit combined disclosure of foreign currency sensitive instruments exposed to different functional currencies, provided that those functional currencies (i) are economically related, (ii) are managed together for internal risk management purposes, and (iii) have statistical correlations of greater than 75% over each of the past three years. In addition, the Commission has provided instructions to the final disclosure items to require the disaggregated reporting of instruments based on common characteristics only to the extent such disaggregation is material. Finally, the Commission has decided to exempt certain currency swaps and foreign currency denominated debt instruments from disclosure in the foreign currency risk exposure category if the currency swap eliminates all foreign currency exposure in the cash flows of the foreign currency denominated debt instrument. However, both the currency swap and the foreign currency denominated debt instrument still should be disclosed in the interest rate risk exposure category.

With regard to the need for guidance on information to be included in the table, the Commission has clarified in the final disclosure items that the table should provide information about contract terms sufficient to estimate the future cash flows from market risk sensitive instruments, categorized by expected maturity dates. In addition, for disclosures about options in particular, the Commission has made clear in the instructions to the final disclosure items that tabular information on options with dissimilar strike prices should be disclosed separately to help reflect the different market risk exposures inherent in option instruments.

6. Sensitivity Analysis—Multiple Risk Exposures

Commenters requested additional guidance on how to perform the sensitivity analysis calculations for registrants with (i) multiple foreign currency exchange rate exposures and (ii) instruments that are exposed to rate or price changes in more than one market risk exposure category (*e.g.*, interest rate risk and foreign currency rate risk).

In response to those comments, the Commission has added two clarifying instructions to the disclosure items. First, registrants with multiple foreign currency exchange rate exposures should present foreign currency sensitivity analyses that measure the aggregate sensitivity to all changes in foreign currency exchange rate exposures, including the changes in both transactional currency/functional currency exchange rate exposures and functional currency/reporting currency exchange rate exposures.[75] Second, for sensitivity analysis calculation purposes, registrants with instruments that are exposed to rate or price changes in more than one market risk exposure category should include the instrument in each market risk category to which the instrument is exposed. Similar instructions also were added to the value at risk disclosure requirements.

7. Value at Risk—Contextual Disclosures

To help place reported value at risk amounts in context, the disclosure items in the proposing release specified that registrants should report either (i) the average or range in value at risk amounts for the current reporting period, (ii) the average or range in actual changes in fair values, earnings, or cash flows from market risk sensitive instruments occurring during the current reporting period, or (iii) the percentage of actual changes in fair values, earnings, or cash flows from market risk sensitive instruments that exceeded the reported value at risk amounts during the current reporting period ((i), (ii), and (iii) collectively are referred to as the ''contextual value at risk disclosures'').

Some commenters suggested that the final disclosure items should encourage, but not require, the contextual value at risk disclosures. Those commenters stated that the Commission would be penalizing registrants for choosing the value at risk disclosure alternative by requiring contextual disclosures that are not required for the other two disclosure alternatives. Other commenters, while supporting the disclosure requirements generally, objected to one or more of the contextual value at risk disclosures.

The Commission acknowledges the concerns of those commenters, but has decided not to change significantly the contextual disclosure requirements because it believes those disclosures provide investors with information that is important in evaluating the reported value at risk amounts. The disclosure items have been modified only to the extent necessary to clarify the contextual disclosure requirements. These contextual disclosures are common elements to value at risk management systems. Similar disclosures are not available for the

[75] For example, assume a French division of a registrant presenting its financial statements in U.S. dollars ($US) invests in a deutschmark(DM)-denominated debt security. This division determines that: (i) The French franc (FF) is its functional currency according to FAS 52, (ii) the $US is its reporting currency, and (iii) the DM is its transactional currency. In preparing the foreign currency sensitivity analysis disclosures, this registrant should report the aggregate potential loss from hypothetical changes in both the DM/FF exchange rate exposure and the FF/$US exchange rate exposure.

tabular presentation and sensitivity analysis alternatives; thus, comparable contextual disclosures are not required for those alternatives.

8. Value at Risk—Aggregated Values

The proposed disclosure items would have required disclosure of an aggregate value at risk amount across all market risk sensitive instruments. A similar aggregate amount would not have been required for the other two disclosure alternatives.

Some commenters suggested that it may not be practical to require an aggregate value at risk amount because most registrants do not use a single risk measurement method for all market risk exposures. Other commenters suggested that registrants providing an aggregate value at risk amount for all categories of market risk should not be required to disclose separate value at risk amounts for each market risk exposure category.

Recognizing that registrants often do not use the same method internally for managing risk across the different market risk exposure categories within the trading and other than trading portfolios, the final disclosure items encourage, but do not require, reporting of aggregate value at risk (and sensitivity analysis) amounts for the trading and other than trading portfolios. Registrants also should note that they may not report aggregate value at risk amounts for the trading and other than trading portfolios in lieu of the required separate value at risk amounts for each market risk exposure category. Separate value at risk amounts provide information about a registrant's specific market risk exposures, which the Commission believes is useful for investors trying to manage specific risks in their investment portfolios.

9. Model Parameters

In order to enhance the comparability of sensitivity analysis and value at risk disclosures, some commenters from the user community suggested that the Commission specify certain model parameters. In particular, those commenters suggested that the Commission establish several standard stress tests to be used to calculate sensitivity analysis disclosures, such as the greater of a 15% or 100 basis point adverse interest rate shift along the entire yield curve. Those standard stress tests would require measurement of the potential loss from reasonably expected market movements. Other commenters, however, requested that the Commission not specify model parameters at this time to allow the reporting to be responsive to the ongoing evolution in risk management systems.

Due to these evolving practices, a guiding principle in the proposing release was to provide flexibility in the sensitivity analysis and value at risk market risk disclosure requirements to accommodate different types of registrants, different degrees of market risk exposure, and alternative ways of measuring market risk. The Commission continues to believe such flexibility is necessary at this time and, therefore, is not specifying uniform model parameters for the calculation of sensitivity analysis and value at risk disclosures.

The need for such flexibility, however, should not result in selection of model parameters that are not realistic and meaningful measures of reasonably expected market rate and price changes. Accordingly, the Commission has included guidance in the final disclosure items on certain model parameters that should be used by registrants. In particular, this guidance requires registrants to select both hypothetical changes in market rates or prices for sensitivity analysis and confidence intervals for value at risk that reflect reasonably possible near-term changes in market rates and prices. In this regard, the disclosure items indicate that, absent economic justification for the selection of different model parameters, registrants should use hypothetical changes in market rates or prices that are not less than 10 percent of end of period market rates or prices for sensitivity analysis disclosures and confidence intervals that are 95 percent or higher for value at risk disclosures. In the long-term, as more standard risk management practices and methods of reporting market risk are developed, the Commission anticipates that it will further limit the models, assumptions, and parameters permitted in Items 305(a) and 9A(a) to enhance comparability of reported information.

10. Comparative Information

Many commenters requested that, if a registrant changes its method of providing quantitative information about market risk from one year to the next, it should not be required to provide comparable summarized information for the preceding period because preparing such presentations and analyses using the new method for preceding periods would be burdensome and costly. Moreover, they suggested that the cost associated with providing comparable summarized information for the preceding year may be a sufficient disincentive to prevent change to a more sophisticated disclosure alternative.

The Commission believes that information about market risk is most useful for investors when compared to one or more prior periods. For such information to be meaningful, the information needs to be prepared on a consistent basis from period-to-period. The Commission also believes that registrants should be able to change methods of preparing market risk information as their risk management practices evolve. To mitigate the costs of preparing prior period market risk disclosures, the final disclosure items provide two alternatives to registrants that change disclosure alternatives, key model characteristics, assumptions, or parameters. First, a registrant may provide summarized comparable information, under the new disclosure method, for the year preceding the current year. Alternatively, in addition to providing disclosure for the current year under the new method, the registrant may provide disclosure for the current year and preceding fiscal year under the method used in the preceding year.

11. Effective Dates

Commenters suggested that time is needed to allow registrants to prepare and implement the new quantitative disclosures about market risk. The Commission agrees with those commenters and, thus, will phase in the amendments over the next several months so that registrants will have time to respond to the new disclosure requirements. For registrants that are likely to have experience with measuring market risk, such as banks, thrifts, and non-bank and non-thrift registrants with market capitalizations on January 28, 1997 in excess of $2.5 billion, Items 305 and 9A are effective for filings with the Commission that include annual financial statements for fiscal years ending after June 15, 1997. For other registrants, those Items are effective for filings with the Commission that include annual financial statements for fiscal years ending after June 15, 1998. In addition, under Items 305 and 9A, interim information is not required until after the first fiscal year end in which those Items are effective.

C. Qualitative Disclosures About Market Risk

1. Proprietary Information

Some commenters expressed concerns that a discussion of primary market risk exposures and how those exposures are managed would be proprietary. The

Commission acknowledges those concerns, but believes that qualitative information about market risk is important to investors. Without the disclosures required by Item 305(b) and Item 9A(b), investors would be unable to understand a registrant's exposures to market risk and unable to place that registrant's market risk management practices within the context of its business. In addition, the qualitative disclosures are not so specific as to require disclosure of the type of information (*e.g.*, current positions) that may harm a registrant's competitive positions. For these primary reasons the Commission has decided to retain the qualitative market risk disclosure requirements.

2. Examples of How Market Risks Are Managed

Proposed Items 305(b) and 9A(b) provide examples of possible disclosures regarding how a registrant manages market risk. These examples include a description of the objectives, general strategies, and instruments used to manage market risk. Some commenters inquired whether the description of one or two of these items would be sufficient. Others asked if the examples are intended to be an all-inclusive list of items required by Items 305(b) and 9A(b).

In general, the examples were intended to reflect minimum disclosures that would be necessary to comply with the qualitative market risk disclosure requirements. The examples were neither meant to address all circumstances nor to be all inclusive. The final disclosure items clearly state that the listed items should be addressed within the required disclosures and that registrants also are responsible for providing any additional information necessary to describe completely their primary market risks and how those risks are managed.

D. Implementation Issues

1. Scope of Disclosures

Several commenters raised issues about the scope of instruments included in the proposed disclosure items. For example, some suggested that information about derivative commodity instruments should not be required because offsetting exposures relating to commodities held or owned were not required. Thus, the disclosures would be presenting only part of registrants' exposure to market risk. Furthermore, they indicated that registrants that hedge commodity exposures could be disclosing more market risk than those that do not participate in hedging activities, even though they may have less exposure to market risk. Similar arguments were made regarding (i) Hedges of anticipated transactions, foreign currency operating cash flows, and inventories and (ii) issuances of debt to fund property, plant, and equipment. In essence, those commenters suggested that the scope of the disclosure requirements is limited and as a result the information required to be disclosed is incomplete. Some commenters suggested that, to address this issue, the instruments covered by the disclosures be expanded to include all types of instruments with market risk. Other commenters suggested reducing the scope of instruments covered by the disclosures, primarily by eliminating derivative commodity instruments.

The Commission considered expanding the required quantitative disclosures about market risk to include commodity positions and anticipated transactions. However, many internal risk measurement systems currently do not incorporate many commodity positions and anticipated transactions. Thus, the Commission is not requiring the inclusion of these items at this time.

The Commission believes that derivative commodity instruments often have risks similar to other derivatives and can be used to alter significantly a registrant's commodity risk profile by, for example, locking in the price of a significant portion of its future purchases of commodity inventory. Accordingly, the Commission continues to include those instruments within the scope of the final disclosure items. Without including such instruments in the required disclosures, it would be difficult for investors to distinguish, for example, between those registrants that are sensitive to changes in commodity prices from those that are not.

In an effort to make disclosures about market risk more comprehensive, the Commission encourages registrants to include voluntarily commodity positions, anticipated transactions, and other market risk sensitive instruments and positions within their market risk disclosures. When these instruments, transactions, and positions are not included in the quantitative disclosures and, as a result, the disclosures do not fully reflect the net market risk exposures of the registrant, Items 305(a) and 9A(a) require that registrants discuss the limitations of the disclosed market risk information resulting from the absence of those items.

2. The Definition of Financial Instrument

Commenters suggested that the definition of financial instruments be clarified to exclude explicitly financial instruments that the FASB excluded from FAS 107. Financial instruments excluded from FAS 107 disclosures include insurance contracts, lease contracts, and employers' and plans' obligations for pension and other post-retirement obligations. The cash flows in many of these instruments are affected significantly by more than market risk factors, thereby making the quantification of market risk more difficult. The Commission agrees that these instruments should be excluded from the scope of the final disclosure items. Thus, the relevant instructions to Items 305 and 9A indicate that instruments excluded from FAS 107 are excluded from the scope of the final disclosure items. However, registrants are encouraged to include voluntarily such instruments in their market risk disclosures, if such inclusion would make the information more complete and meaningful.

3. The Definition of Derivative Commodity Instrument

In the proposed disclosure items, "derivative commodity instruments" were defined to include commodity futures, commodity forwards, commodity swaps, commodity options, and other commodity instruments with similar characteristics that are reasonably possible to be settled in cash or with another financial instrument. Some commenters indicated that a reasonably possible test would be too difficult to apply in practice. That is, it may be difficult to distinguish between a commodity contract for which settlement in cash is reasonably possible and a contract for which settlement in cash is not reasonably possible. Some commenters suggested that derivative commodity instruments be defined as those that may be settled in cash in the normal course of business. Those commenters also suggested that the definition of derivative commodity instruments include specifically derivative instruments in which cash settlement is based on the net change in value of the commodity contract.

In response to those comments, the Commission has amended the definition of derivative commodity instruments to include commodity futures, commodity forwards, commodity swaps, commodity options, and other commodity instruments with similar characteristics that are permitted by contract or business custom to be settled in cash or with another financial instrument. In addition, the final disclosure items make clear that settlement in cash includes settlement in cash of the net change in value of the derivative commodity instrument.

4. Small Business Issuers

Some commenters suggested that the disclosure requirements in Items 305 and 9A should apply to all registrants that have material positions in instruments covered by the proposed disclosure items, including small business issuers filing documents with the Commission in accordance with Regulation S–B. Due to cost-benefit concerns, however, the Commission has determined that some experience should be gained with the disclosure items before proposing that they be applied to small business issuers.

5. The Disclosure Threshold

Some commenters suggested that the Commission change the threshold for requiring disclosures of quantitative information about market risk to conform with the disclosure threshold in MD&A. That suggestion was based on a general observation that both MD&A and proposed Items 305 and 9A require disclosure of information about known risks and uncertainties and, therefore, should be subject to the same threshold for determining whether disclosure is required. Those commenters indicated that introducing a new and different disclosure threshold could add unnecessary confusion to the disclosure process.

MD&A addresses a wide array of risks and uncertainties. Thus, the MD&A disclosure threshold (i) Is broad, applying to many different types of exposures, not just market risk and (ii) does not provide specific guidance directly relevant to a threshold for disclosure of quantitative market risk information. In addition, MD&A focuses on events that are judged to be reasonably likely of occurring.

In contrast, consistent with many internal risk management systems, Item 305 and Item 9A require reporting of losses from events beyond those deemed reasonably likely of occurring. For example, those disclosure Items require reporting of value at risk information on possible future losses, which, at a minimum, are not expected to be exceeded 95% of the time. Likewise, those disclosure Items require reporting of sensitivity analysis information on possible future losses from reasonably possible, not reasonably likely, near-term changes in market rates and prices. Thus, Item 305 and Item 9A are intended to obtain quantitative information about market risk that is incremental to the disclosures about reasonably likely risks and uncertainties required by MD&A.

As a result, the Commission has decided to retain the disclosure threshold that was proposed. That threshold provides guidelines that focus on market risk, apply explicitly to quantitative disclosures, and most importantly, require disclosure of losses beyond those deemed reasonably likely of occurring.

6. ‘‘Future’’ Losses

With respect to the disclosure threshold noted above, commenters suggested that the Commission define how far into the future registrants must look to conclude whether or not they may experience material future losses. They suggested replacing the word ‘‘future’’ with either the phrase ‘‘near term’’ as it is defined in AICPA Statement of Position 94–6, ‘‘Disclosure of Risks and Uncertainties’’ (‘‘SOP 94–6’’) (December 1994) or ‘‘one year.’’

The Commission agrees with the commenters and has limited the time period over which losses in earnings, fair values, and cash flows should be evaluated to the ‘‘near term.’’ In the final disclosure items, the Commission defines ‘‘near term’’ to mean a period of time going forward up to one year from the date of the financial statements, which is consistent with the definition in SOP 94–6.

7. Safe Harbor

Nearly all of the commenters favored explicit safe harbor protection for the new disclosure of quantitative and qualitative information about market risk. Commenters did not object to the Commission’s proposal to extend the Item 305 and Item 9A safe harbors to all types of issuers and transactions.

Several commenters suggested modifications to the proposed safe harbor. Those commenters argued that the safe harbors should protect all of the qualitative information required by paragraph (b) of Item 305 and Item 9A, and not just statements with respect to future reporting periods provided pursuant to paragraph (b)(1)(iii), as proposed.[76] A few of these commenters provided examples of disclosures responsive to paragraphs (b)(1)(i) and (b)(1)(ii) of Item 305 and Item 9A that they thought could be viewed as being forward looking. As noted above,[77] the rule has been clarified to provide that all statements (other than statements of historical fact) provided pursuant to paragraphs (b)(1)(i), (b)(1)(iii) and (c) of Items 305 and 9A are ‘‘forward looking statements’’ for purposes of the new safe harbor rules. To the extent that information provided pursuant to paragraph (b)(1)(ii) of Items 305 and 9A includes forward looking statements, those statements would be eligible for safe harbor protection.

Second, most of the commenters remarking on the issue thought that small business issuers voluntarily providing any of the Item 305 and Item 9A disclosures should have the protection of the safe harbor. Under the proposals, the safe harbor would have applied to voluntary disclosures only if all of the quantitative disclosures or all of the qualitative disclosures were provided. In an effort to encourage small business issuers to provide information that they think is appropriate to an understanding of their market risks, Item 10 of Regulation S-B has been changed to extend the Item 305 safe harbor to any Item 305 disclosure that is voluntarily provided by a small business issuer.

Finally, several commenters requested guidance as to whether registrants would have to include ‘‘meaningful cautionary statements’’ in addition to the Item 305 and Item 9A disclosures to obtain the protection of the Item 305 and Item 9A safe harbors. In response to these comments, the Commission has clarified in the rule that, for purposes of the Item 305(a) and 9A(a) quantitative disclosures, a registrant will be deemed to have satisfied the ‘‘meaningful cautionary statements’’ prong of the safe harbors if it satisfies the requirements of those items. In particular, these items require a description of the assumptions underlying, and the limitations of, the disclosure provided. For the remainder of the information required by the new items, registrants desiring to qualify for the ‘‘meaningful cautionary statements’’ prong of the safe harbor will need to consider what information should be given to alert investors to important factors that could cause actual results to differ materially from the information given in the forward looking statements.

VII. Certain Findings

Section 23(a) of the Exchange Act[78] requires the Commission, in adopting final rules under the Exchange Act, to consider the anti-competitive effect of such rules, if any, and to balance them against the regulatory benefits that further the purposes of the Exchange Act. Furthermore, Section 2 of the

[76] Item 305(b)(1)(iii) was proposed as Item 305(b)(3).

[77] See section III B.3.

[78] 15 U.S.C. 78w(a).

Securities Act[79] and Section 3 of the Exchange Act,[80] as amended by the recently enacted National Securities Market Improvement Act of 1996 (''Market Improvement Act''),[81] provide that whenever the Commission is engaged in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission also shall consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.

As discussed in earlier subsections of this release, the Commission has considered carefully the comments that the Item 305(a) and Item 9A(a) quantitative disclosures of market risk, as originally proposed, might provide information useful to a registrant's competitors. The Commission has determined, however, that quantitative disclosures will be helpful to investors' understanding of a registrant's market risk exposures and that sensitivity analysis and value at risk disclosures normally do not allow readers to ascertain detailed information about positions held by registrants. However, in response to registrants with proprietary concerns about reporting period-end information under the sensitivity and value at risk disclosure alternatives, the final disclosure items allow reporting of the average, high, and low sensitivity analysis or value at risk amounts for the fiscal year, as an alternative to year-end amounts. In addition, the final disclosure items also require registrants filing interim reports to provide a discussion and analysis of the sources and effects of material changes in market risk information since the end most recent preceding fiscal year, rather than requiring, as originally proposed, that registrants always furnish complete Item 305(a) or Item 9A(a) information, when such material changes occur.

The Commission has considered the amendments and new disclosure items discussed in this release in light of the comments received in response to the proposing release and the standards embodied in Section 2 of the Securities Act and Sections 3 and 23(a) of the Exchange Act. The Commission believes that any burdens on competition imposed by the adoption of these amendments and disclosure items are necessary and appropriate in furtherance of the purposes of the Exchange Act. Some commenters suggested Items 305 and 9A could create incentives for the development of new products that do not trade on exchanges and would not be subject to the new disclosures because of their non-cash-settlement feature. The Commission intends to review the effects of the disclosures on the markets and expects to reconsider the disclosure items after three years. The Commission will be able to address any such concerns at such time. The Commission believes that Items 305 and 9A are necessary and appropriate in the public interest and for the protection of investors because of the need for improved disclosure about market risk to help investors better understand and evaluate a registrant's exposures to market risk.

As described in more detail in the cost-benefit section of this release, the Commission made a number of changes from the rules as proposed to increase flexibility for registrants in providing the required disclosures and keeping the cost of compliance to a minimum, thus promoting efficiency. In addition, by enhancing investor's understanding of registrants' market risk exposures the disclosure items should promote the efficient allocation of capital. Thus, the disclosure items will promote competition, efficiency, and enhance the U.S. capital formation process.

VIII. Cost-Benefit Analysis

A. Background

In general, Rule 4–08(n), Item 305, and Item 9A, clarify existing standards and rules, include additional instruments within existing standards, and require specific disclosure alternatives for providing quantitative disclosures regarding market risk sensitive instruments. In particular, these provisions include:

1. Enhanced descriptions of accounting policies for derivatives;
2. Quantitative disclosures about market risk; and
3. Additional qualitative disclosures about market risk.

These provisions are being adopted in response to requests from investors and others to provide more meaningful information about market risk sensitive instruments.[82] The expected benefits of these rules and items are to make information about market risk sensitive instruments, including derivatives, more understandable to investors and others. This increased understanding is expected to enhance the ability of investors to make investment decisions and to improve the efficiency of the markets. The Commission believes these benefits will outweigh the related costs, which are discussed below.

B. Descriptions of Accounting Policies for Derivatives

FAS 119 was designed, in part, to help investors and others understand how derivative financial instruments are reported in the financial statements.[83] FAS 119 requires, among other things, disclosure of the policies used to account for derivative financial instruments, pursuant to the requirements of APB 22.[84] However, the scope of FAS 119 is limited to derivative financial instruments and, therefore, it does not apply to other derivative instruments with similar characteristics, such as derivative commodity instruments. In addition, FAS 119 does not provide explicit guidance indicating what must be described in accounting policies footnotes to make the financial statement effects of derivatives more understandable. The SEC staff found that the accounting policies footnotes for derivatives often were too general in nature, not reflecting adequately the choices made by registrants in their accounting for derivatives.

New Rule 4–08(n) requires descriptions of accounting policies for derivative financial instruments and derivative commodity instruments, unless the registrant's derivative activities are not material. Thus, the scope of the amendments is broader than the scope of FAS 119. In addition, to help make clear the impact of derivatives on the financial statements, Rule 4–08(n) makes explicit the items to be disclosed in the accounting policies footnotes.

Rule 4–08(n) is likely to result in a more focused and descriptive discussion of the accounting policies for both derivative financial instruments and derivative commodity instruments. This additional information is likely to result in additional preparation, audit, and printing costs. However, because accounting policies for these instruments are known by registrants and should be known by their auditors, most of the preparation and audit costs are expected to relate to initial compliance with the amendments. These costs, along with expected printing costs, are not estimated to be significant. Other costs, such as ongoing recordkeeping and compliance costs, also are not expected to be significant.

[79] 15 U.S.C. 77b.

[80] 15 U.S.C. 78c.

[81] Pub. L. 104–290, 106, 110 Stat. 3416 (1996).

[82] See notes 22–29, *supra*, for examples of investors, regulators, and other private bodies endorsing or recommending improved quantitative disclosures about market risk.

[83] See FAS 119 ¶ 60.

[84] See FAS 119 ¶ 8. See also note 39, *supra*, for a discussion of the requirements of APB 22.

C. Quantitative Information About Market Risk

As discussed earlier in this release, under Item 305(a) and Item 9A(a), registrants are required to present quantitative information about market risk. An important aspect of this requirement, from a cost perspective, is that registrants will have the flexibility to choose one or more of three disclosure alternatives (tabular presentation, sensitivity analysis, or value at risk) to provide such quantitative information about market risk.

The Commission believes that, for registrants electing to provide tabular disclosure, much of the required information is currently available. Thus, additional costs relating to recordkeeping are not expected to be significant. While increased reporting and compliance burdens may result, in many cases the information presented in the tabular disclosures is used in managing the business activities of the registrant and may be available at relatively low incremental costs. Further, registrants complying with Securities Act Industry Guide 3,[85] principally financial institutions, already disclose a significant amount of the required information.

Registrants that choose to use either the sensitivity or value at risk disclosure alternatives may incur significant additional costs if they currently do not use these methodologies to manage market risk. In contrast, if registrants currently use sensitivity or value at risk analyses to manage market risk, the Commission believes that any additional costs associated with complying with Item 305(a) or Item 9A(a) are not expected to be significant. The Commission recognizes that, for some registrants, the start-up costs to prepare the quantitative disclosures about market risk may be significant. However, in the near term, the Commission expects that the development of software related to market risk analysis will reduce these costs materially. In addition, the Commission understands that some of the data and the systems needed to develop these analyses recently have been made available at a relatively moderate cost.[86] Moreover, some registrants are required to prepare such information for regulatory capital measurement purposes. In particular, thrift institutions are required to prepare fair value sensitivity analyses for risk-based capital purposes.[87] Also, banks and bank holding companies with significant exposure to market risk are required to prepare a value at risk analysis for risk-based capital purposes.[88] Thus, the costs associated with the sensitivity and value at risk analyses may vary depending on (i) Whether the registrant currently engages in these analyses for other management or regulatory purposes; and (ii) the particular model and assumptions used in the registrant's calculations. Any registrant that believes the cost of such analyses outweigh the benefits of disclosing them, however, may elect to provide tabular presentation of information about market risk sensitive instruments.

In response to the comment letters, the Commission made several changes in Item 305(a) and Item 9A(a) that should reduce the cost for registrants preparing disclosures of quantitative information about market risk. These changes are described in detail above, under the caption ''Response to Comments.'' In brief, changes that should reduce registrants' costs include:

- Delaying the effective date of the market risk disclosure requirements for banks, thrifts, and non-bank and non-thrift registrants with market capitalizations on January 28, 1997 in excess of $2.5 billion until filings made with the Commission include annual financial statements for years ending after June 15, 1997. For non-bank and non-thrift registrants with market capitalizations on January 28, 1997 of $2.5 billion or less, the effective date is delayed until filings with the Commission include annual financial statements for fiscal years ending after June 15, 1998.
- Permitting the use of different quantitative disclosure alternatives for market risks inherent in (1) the trading portfolio, (2) the ''other than trading'' portfolio, and (3) different market risk exposure categories within each of those portfolios. This often will allow registrants that use different methods to manage different types of market risk to report quantitative information according to the method used for internal risk management purposes, instead of having to conform all disclosures to one disclosure alternative.
- For the tabular presentation alternative, permitting entities to report together (or group) foreign currency sensitive instruments according to functional currencies that are economically related, are managed together for internal risk purposes, and have statistical correlations of greater than 75% over each of the past three years.
- For the tabular presentation alternative, requiring that instruments be reported based on specified common characteristics only if, or to the extent that, such disaggregation provides material information to investors.
- For the tabular presentation alternative, allowing elimination of disclosure in the foreign currency risk exposure category of currency swaps and foreign currency denominated debt instruments, if the currency swap eliminates all foreign currency exposure in the cash flows of the foreign currency denominated debt instrument.
- Encouraging, rather than requiring, that registrants provide aggregate sensitivity analysis and value at risk amounts for the trading and other than trading portfolios.
- When a registrant changes quantitative disclosure methods from one year to the next, providing two alternatives, rather than one, for disclosing comparative, year-to-year information. First, a registrant may restate the prior year's disclosures based on the new alternative that has been selected for the current year. Second, instead of recreating prior records and information in order to prepare restated information, the registrant may report the prior year's disclosures as originally presented and, in addition to disclosing the current year's information in accordance with the new method, disclose the current year's information under the method used in the prior year.
- Specifically excluding from the scope of the disclosure item certain financial instruments that are not required by generally accepted accounting principles to be disclosed at fair value. Such instruments include but are not limited to pension and other post-retirement benefits, insurance contracts, lease contracts, warranty obligations and rights, and minority positions in consolidated enterprises.
- Limiting to one year how far into the future a registrant must look to determine whether it is reasonably possible that it will experience a loss from its derivative and other financial instruments.

The comment letters did not provide empirical or statistical information about the costs to comply with the proposed quantitative disclosures of market risk. After reviewing the anecdotal information in those letters, however, and despite the changes listed above that further reduce compliance costs, the Commission has reconsidered and increased the estimated time that it may take registrants, on average, to prepare and report quantitative information under Items 305(a) and 9A(a). The Commission is increasing to 80 hours the estimated average hours per registrant to comply with Item 305(a) or Item 9A(a). In addition, the

[85] Securities Act Industry Guide 3, ''*Statistical Disclosure by Bank Holding Companies.*'' Exchange Act Industry Guide 3 is identical to the Securities Act guide. Detailed disclosures are required under Guide 3 of, among other things, the registrant's: (i) Distribution of assets, liabilities and stockholders' equity; interest rates and interest differential; (ii) investment portfolio; (iii) loan portfolio (including types of loans, maturities and sensitivities of loans to changes in interest rates, risk elements, and loans outstanding in foreign countries); (iv) deposits; and (v) short-term borrowings.

[86] See Wall Street Journal, ''Morgan Unveils the Way It Measures Market Risk'' C1 (October 11, 1994).

[87] See note 48, *supra.*

[88] See Department of the Treasury, Federal Reserve System, and Federal Deposit Insurance Corporation Joint final rule, ''*Risk-Based Capital Standards: Market Risk,*'' 61 FR 47358 (September 6, 1996).

estimated cost of $40 per hour has been increased to $100 per hour because the Commission believes that the levels of professional services that may be needed to prepare the information may be higher than originally expected. The revised overall cost estimate is approximately $40 million for all registrants complying with the required disclosures of quantitative and qualitative information about market risks.

D. Qualitative Information About Market Risk

FAS 119 requires certain qualitative disclosures about the market risk management activities associated with derivative financial instruments held or issued for purposes other than trading. In particular, FAS 119 requires disclosure of ''the entity's objectives for holding or issuing the derivative financial instruments, the context needed to understand those objectives, and its general strategies for achieving those objectives.'' [89] However, as indicated above, these requirements of FAS 119 only apply to certain derivative financial instruments, and the SEC staff has observed that these disclosures typically have been general in nature, providing only limited insight into an entity's overall market risk management activities.

In essence, Items 305(b) and 9A(b) expand certain disclosure requirements set forth in FAS 119 to (1) encompass derivative financial instruments entered into for trading purposes, other financial instruments, and derivative commodity instruments and (2) require registrants to evaluate and describe material changes in their primary risk exposures and their market risk management activities. The Commission believes this will present a more complete discussion of a registrant's exposure to market risks and the way it manages those risks. Because this information is likely to be used by registrants as part of their risk management activities, incremental costs relating to such disclosure are not expected to be significant.

E. Small Business Issuers

As noted earlier, the Commission has determined not to amend Regulation S–B [90] to incorporate an item similar to Item 305. Regulation S–B may be used by small business issuers [91] required to register their securities with the Commission. By excluding small business issuers from all but the accounting policies disclosures that are required by the amendments, the Commission has limited substantially the cost of those proposals for small entities.

IX. Summary of Final Regulatory Flexibility Analysis

The Commission has prepared a Final Regulatory Flexibility Analysis pursuant to the requirements of the Regulatory Flexibility Act, [92] regarding the amendments to Rule 4–08 of Regulation S–X, to Regulation S–K to create Item 305, and the conforming amendments to Forms S–1, S–2, S–4, S–11, and F–4 under the Securities Act, and Rule 14a–3, Schedule 14A and Forms 10, 20–F, 10–Q, and 10–K under the Exchange Act. This section summarizes that analysis. A copy of the final analysis may be obtained by contacting Robert E. Burns, Chief Counsel, Office of the Chief Accountant, U.S. Securities and Exchange Commission, Mail Stop 11–3, 450 Fifth Street, N.W., Washington, D.C. 20549.

The final regulatory flexibility analysis notes that the amendments clarify existing disclosure requirements, include additional instruments within existing disclosure requirements, and require specific disclosure alternatives for providing quantitative information regarding market sensitive instruments. These amendments are intended to provide investors with a clearer understanding of registrants' use of such instruments and the market risks inherent in those instruments.

For purposes of the Securities Act of 1933, the term ''small business,'' as used with reference to a registrant (other than an investment company) [93] for the purposes of the Regulatory Flexibility Act, is defined by Rule 157 as an issuer with total assets on the last day of its most recent fiscal year of $5 million or less and which is engaged or proposing to engage in an offering of securities that does not exceed $5 million. [94] For purposes of the Securities Exchange Act of 1934, small business (other than an investment company) is defined in Rule 0–10 to mean issuers having total assets of $5 million or less as of the end of the most recent fiscal year. [95]

Approximately 1100 Exchange Act reporting companies satisfy the definition of ''small business'' under Rule 157. As of December 1995, there were approximately 5200 broker-dealers classified as small businesses under the above regulations.

As fully discussed in the analysis and elsewhere in this release, the Commission has determined not to amend Regulation S–B to incorporate an item similar to Items 305 and 9A. By excluding small business issuers from these new disclosure requirements, the Commission has reduced substantially the impact of the amendments on small entities. Nonetheless, the final regulatory flexibility analysis describes various factors, including changes to the disclosure requirements adopted in response to the comments on the proposing release, that reduce compliance costs for all registrants. These factors also are set forth in the *Cost-Benefit Analysis* section of this release.

Rule 4–08 clarifies how the accounting policy disclosure requirements under APB 22 should be applied to derivatives and, therefore, should not place significant additional costs on small entities. The disclosures, however, are likely to result in a more focused and descriptive discussion of the accounting policies for derivatives. Disclosure of this information may result in an increase in costs to prepare and print the disclosures. However, most of the preparation costs are expected to relate to complying initially with the new rule, as the disclosures documenting those policies generally may remain consistent from year to year. These initial costs are not expected to be significant. In addition, because the accounting policies must be known by the registrant in order for the registrant to prepare its financial statements, and should be known by its auditors, no new compliance procedures or recordkeeping is required and there should not be a significant increase, if any, in ongoing compliance costs.

Moreover, the Commission has determined that, due to the existing disclosure requirements for accounting policies under generally accepted accounting principles and the insignificant economic impact of the enhanced accounting policy disclosures under Rule 4–08, it is neither necessary nor appropriate for the Commission to establish for small entities different compliance or reporting timetables, simplified disclosure requirements, performance standards, or an exemption from the disclosure requirement.

Only one request was made for the initial regulatory flexibility analysis, and no comments specifically addressed that analysis. Significant cost-benefit issues raised by commenters in response to the proposing release are discussed under the *Response to Comments* and

[89] See FAS 119 ¶ 11a.

[90] 17 CFR 228.10 *et seq.*

[91] See note 69, *supra.*

[92] 5 U.S.C. 604.

[93] As noted elsewhere in this release, the amendments do not apply to investment companies.

[94] 17 C.F.R. 230.157.

[95] 17 C.F.R. 240.0–10.

Cost-Benefit Analysis sections of this release, above.

X. Paperwork Reduction Act

The amendments and disclosure items were submitted for review in accordance with the Paperwork Reduction Act of 1995 (''the Act'') [96] and were approved by the Office of Management and Budget (''OMB'') in accordance with the clearance procedures of that Act. [97] As Regulation S-X, Regulation S-K, and the various forms and rules that are being amended already possess OMB control numbers, new control numbers were not assigned to the collections of information under the amendments. The collection of information requirements under these amendments are mandatory and responses are not confidential. The collections of information are in accordance with 44 U.S.C. 3507. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number.

Also in accordance with the Paperwork Reduction Act, the Commission solicited comment on the compliance burdens associated with the proposals, and received no public comment in response. Comments were received, however, that addressed the general costs and benefits associated with the proposed amendment to disclosure Items 305 and 9A. These comments, and the Commission's response, are discussed in the *Response to Comments* and *Cost-Benefit Analysis* sections, above.

As part of its submission to the OMB under the Paperwork Reduction Act, the Commission estimated that approximately 5000 registrants would disclose quantitative and qualitative information under Item 305 or Item 9A. In view of the factors discussed in the *Cost-Benefit Analysis* section and elsewhere in this release, the Commission recognized that the time required to prepare these disclosures would vary significantly depending on, among other factors, the nature of the registrant's business, its market risk management activities, and other applicable regulatory requirements. The Commission originally estimated that it would take, on average, approximately 40 hours per registrant to prepare such disclosures.

Upon review of the comment letters, the Commission continues to believe that approximately 5000 registrants will provide Item 305 and Item 9A disclosures. The Commission also continues to believe that many financial services companies will not incur additional expense because they already provide such disclosures. In fact, for some of these companies, their costs may go down as less information may be disclosed. In addition, a significant number of registrants, because of the size or nature of their businesses, do not have a significant number of derivative instruments or do not have complex instruments. For these companies, a simple tabular presentation of debt and similar instruments may suffice. The time and cost to prepare such disclosures should not be significant. For larger commercial corporations, however, the time for preparation and presentation of the required Item 305 or Item 9A information may be more than the Commission initially anticipated. Although no commenter provided statistical or empirical information about the cost to gather, prepare, and disclose such information, several mid to large commercial corporations indicated that they believe they may experience noticeable costs associated with such disclosures. As a result, the Commission is increasing to 80 hours the estimated average hour burden per registrant to comply with Item 305 or Item 9A.

XI. Codification Update

The ''Codification of Financial Report Policies'' announced in Financial Reporting Release No. 1 (April 15, 1982) [47 FR 21028] is updated to:

1. Include a new Section 219, ''Disclosure of Accounting Policies for Derivative Financial Instruments and Derivative Commodity Instruments.''

2. Include a new paragraph 219.01 to include the text in topic III.A of this release, ''Discussion of Amendments: Disclosure of Accounting Policies for Derivatives.''

3. Include a new Section 507, ''Disclosure of Quantitative and Qualitative Information About Market Risk Inherent in Derivative Financial Instruments, Other Financial Instruments, and Derivative Commodity Instruments.''

4. Include a new paragraph 507.01 to include the text in topic II of this release, ''Initiatives Regarding Disclosures About Derivatives.''

5. Include a new paragraph 507.02 to include the text in topic III.B. of this release, ''Discussion of Amendments: Disclosures of Quantitative and Qualitative Information About Market Risk.''

6. Include a new paragraph 507.03 to include the text in topic IV of this release, ''Applicability of Amendments.''

7. Include a new paragraph 507.04 to include the text in topic V of this release, ''Disclosure of the Effects of Derivative Instruments on Reporting Financial Instruments, Commodity Positions, Firm Commitments, and Anticipated Transactions.''

The Codification is a separate publication of the Commission. It will not be published in the Federal Register/Code of Federal Regulations System.

Statutory Basis

The additions and amendments to the Commission's rules and forms are adopted pursuant to Sections 7, 10, 19, and 27A of the Securities Act of 1933 and Sections 12, 13, 14, 21E, and 23 of the Securities Exchange Act of 1934.

List of Subjects in 17 CFR Parts 210, 228, 229, 239, 240, and 249

Accounting, Reporting and recordkeeping requirements, Securities.

Text of Amendments

In accordance with the foregoing, Title 17, Chapter II of the Code of Federal Regulations is amended as follows:

PART 210—FORM AND CONTENT OF AND REQUIREMENTS FOR FINANCIAL STATEMENTS, SECURITIES ACT OF 1933, SECURITIES EXCHANGE ACT OF 1934, PUBLIC UTILITY HOLDING COMPANY ACT OF 1935, INVESTMENT COMPANY ACT OF 1940, AND ENERGY POLICY AND CONSERVATION ACT OF 1975

1. The general authority citation for Part 210 is revised to read as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77z-2, 77aa(25), 77aa(26), 78*l*, 78m, 78n, 78o(d), 78u-5, 78w(a), 78*ll*(d), 79e(b), 79j(a), 79n, 79t(a), 80a-8, 80a-20, 80a-29, 80a-30, 80a-37a, unless otherwise noted.

2. By amending 210.4–08 by adding paragraph (n) to read as follows:

§ 210.4–08 General notes to financial statements.

* * * * *

(n) *Accounting policies for certain derivative instruments.* Disclosures regarding accounting policies shall include descriptions of the accounting policies used for derivative financial instruments and derivative commodity instruments and the methods of applying those policies that materially affect the determination of financial position, cash flows, or results of operation. This description shall include, to the extent material, each of the following items:

[96] 44 U.S.C. 3501 *et seq.*

[97] 44 U.S.C. 3507.

(1) A discussion of each method used to account for derivative financial instruments and derivative commodity instruments;

(2) The types of derivative financial instruments and derivative commodity instruments accounted for under each method; (3) The criteria required to be met for each accounting method used, including a discussion of the criteria required to be met for hedge or deferral accounting and accrual or settlement accounting (*e.g.*, whether and how risk reduction, correlation, designation, and effectiveness tests are applied);

(4) The accounting method used if the criteria specified in paragraph (n)(3) of this section are not met;

(5) The method used to account for terminations of derivatives designated as hedges or derivatives used to affect directly or indirectly the terms, fair values, or cash flows of a designated item;

(6) The method used to account for derivatives when the designated item matures, is sold, is extinguished, or is terminated. In addition, the method used to account for derivatives designated to an anticipated transaction, when the anticipated transaction is no longer likely to occur; and

(7) Where and when derivative financial instruments and derivative commodity instruments, and their related gains and losses, are reported in the statements of financial position, cash flows, and results of operations.

Instructions to Paragraph (n)

1. For purposes of this paragraph (n), derivative financial instruments and derivative commodity instruments (collectively referred to as ''derivatives'') are defined as follows:

(i) *Derivative financial instruments* have the same meaning as defined by generally accepted accounting principles (see, *e.g.*, Financial Accounting Standards Board (''FASB''), *Statement of Financial Accounting Standards No. 119, ''Disclosure about Derivative Financial Instruments and Fair Value of Financial Instruments,''* (''FAS 119'') paragraphs 5–7, (October 1994)), and include futures, forwards, swaps, options, and other financial instruments with similar characteristics.

(ii) *Derivative commodity instruments* include, to the extent such instruments are not derivative financial instruments, commodity futures, commodity forwards, commodity swaps, commodity options, and other commodity instruments with similar characteristics that are permitted by contract or business custom to be settled in cash or with another financial instrument. For purposes of this paragraph, settlement in cash includes settlement in cash of the net change in value of the derivative commodity instrument (*e.g.*, net cash settlement based on changes in the price of the underlying commodity).

2. For purposes of paragraphs (n)(2), (n)(3), (n)(4), and (n)(7), the required disclosures should address separately derivatives entered into for trading purposes and derivatives entered into for purposes other than trading. For purposes of this paragraph, *trading purposes* has the same meaning as defined by generally accepted accounting principles (see, *e.g.*, FAS 119, paragraph 9a (October 1994)).

3. For purposes of paragraph (n)(6), *anticipated transactions* means transactions (other than transactions involving existing assets or liabilities or transactions necessitated by existing firm commitments) an enterprise expects, but is not obligated, to carry out in the normal course of business (see, *e.g.*, FASB, *Statement of Financial Accounting Standards No. 80, ''Accounting for Futures Contracts,''* paragraph 9, (August 1984)).

4. Registrants should provide disclosures required under paragraph (n) in filings with the Commission that include financial statements of fiscal periods ending after June 15, 1997.

PART 228—INTEGRATED DISCLOSURE SYSTEM FOR SMALL BUSINESS ISSUERS

3. The general authority citation for Part 228 is revised to read as follows:

Authority: 15 U.S.C. 77e, 77f, 77g, 77h, 77j, 77k, 77s, 77z–2, 77aa(25), 77aa(26), 77ddd, 77eee, 77ggg, 77hhh, 77jjj, 77nnn, 77sss, 78*l*, 78m, 78n, 78u–5, 78o, 78w, 78*ll*, 80a–8, 80a–29, 80a–30, 80a–37, 80b–11, unless otherwise noted.

4. By amending § 228.10 by adding paragraph (g) to read as follows:

§ 228.10 (Item 10) General.

* * * * *

(g) *Quantitative and qualitative disclosures about market risk.* The safe harbor provision included in paragraph (d) of Item 305 of Regulation S–K (§ 229.305(d) of this chapter) shall apply to information required by Item 305 of Regulation S–K (§ 229.305 of this chapter) that is voluntarily provided by or on behalf of a small business issuer as defined in Rule 12b–2 of the Exchange Act.

Note to paragraph (g): Such small business issuers are not required to provide the information required by Item 305 of Regulation S–K.

5. By amending § 228.310 by revising the first sentence of Note 2 to read as follows:

§ 228.310 (Item 310) Financial Statements.

Notes—1. * * *.

2. Regulation S–X (17 CFR 210.1 through 210.12) Form and Content of and Requirements for Financial Statements shall not apply to the preparation of such financial statements, except that the report and qualifications of the independent accountant shall comply with the requirements of Article 2 of Regulation S–X (17 CFR 210.2), Articles 3–19 and 3–20 (17 CFR 210.3–19 and 210.3–20) shall apply to financial statements of foreign private issuers, the description of accounting policies shall comply with Article 4–08(n) of Regulation S–X (17 CFR 210.4–08(n)), and small business issuers engaged in oil and gas producing activities shall follow the financial accounting and reporting standards specified in Article 4–10 of Regulation S–X (17 CFR 210.4–10) with respect to such activities. * * *

* * * * *

PART 229—STANDARD INSTRUCTIONS FOR FILING FORMS UNDER SECURITIES ACT OF 1933, SECURITIES EXCHANGE ACT OF 1934 AND ENERGY POLICY AND CONSERVATION ACT OF 1975—REGULATION S–K

6. The general authority citation for Part 229 is revised to read in part as follows:

Authority: 15 U.S.C. 77e, 77f, 77g, 77h, 77j, 77k, 77s, 77z–2, 77aa(25), 77aa(26), 77ddd, 77eee, 77ggg, 77hhh, 77iii, 77jjj, 77nnn, 77sss, 78c, 78i, 78j, 78*l*, 78m, 78n, 78o, 78u–5, 78w, 78*ll*(d), 79e, 79n, 79t, 80a–8, 80a–29, 80a–30, 80a–37, 80b–11, unless otherwise noted.

* * * * *

7. By adding § 229.305 to read as follows:

§ 229.305 (Item 305) Quantitative and qualitative disclosures about market risk.

(a) *Quantitative information about market risk.* (1) Registrants shall provide, in their reporting currency, quantitative information about market risk as of the end of the latest fiscal year, in accordance with one of the following three disclosure alternatives. In preparing this quantitative information, registrants shall categorize market risk sensitive instruments into instruments entered into for trading purposes and instruments entered into for purposes other than trading purposes. Within both the trading and other than trading portfolios, separate quantitative information shall be presented, to the extent material, for each market risk exposure category (*i.e.*, interest rate risk, foreign currency exchange rate risk, commodity price risk, and other relevant market risks, such as equity price risk). A registrant may use one of the three alternatives set forth in this section for all of the required quantitative disclosures about market risk. A registrant also may choose, from among the three alternatives, one disclosure alternative for market risk sensitive instruments entered into for trading purposes and another disclosure alternative for market risk sensitive instruments entered into for other than trading purposes. Alternatively, a registrant may choose any disclosure alternative, from among the three alternatives, for each risk exposure category within the trading and other than trading portfolios. The three disclosure alternatives are:

(i)(A)(*1*) Tabular presentation of information related to market risk sensitive instruments; such information shall include fair values of the market risk sensitive instruments and contract terms sufficient to determine future cash flows from those instruments, categorized by expected maturity dates.

(*2*) Tabular information relating to contract terms shall allow readers of the table to determine expected cash flows from the market risk sensitive instruments for each of the next five years. Comparable tabular information for any remaining years shall be displayed as an aggregate amount.

(*3*) Within each risk exposure category, the market risk sensitive instruments shall be grouped based on common characteristics. Within the foreign currency exchange rate risk category, the market risk sensitive instruments shall be grouped by functional currency and within the commodity price risk category, the market risk sensitive instruments shall be grouped by type of commodity.

(*4*) See the Appendix to this Item for a suggested format for presentation of this information; and

(B) Registrants shall provide a description of the contents of the table and any related assumptions necessary to understand the disclosures required under paragraph (a)(1)(i)(A) of this Item 305; or

(ii)(A) Sensitivity analysis disclosures that express the potential loss in future earnings, fair values, or cash flows of market risk sensitive instruments resulting from one or more selected hypothetical changes in interest rates, foreign currency exchange rates, commodity prices, and other relevant market rates or prices over a selected period of time. The magnitude of selected hypothetical changes in rates or prices may differ among and within market risk exposure categories; and

(B) Registrants shall provide a description of the model, assumptions, and parameters, which are necessary to understand the disclosures required under paragraph (a)(1)(ii)(A) of this Item 305; or

(iii)(A) Value at risk disclosures that express the potential loss in future earnings, fair values, or cash flows of market risk sensitive instruments over a selected period of time, with a selected likelihood of occurrence, from changes in interest rates, foreign currency exchange rates, commodity prices, and other relevant market rates or prices;

(B)(*1*) For each category for which value at risk disclosures are required under paragraph (a)(1)(iii)(A) of this Item 305, provide either:

(*i*) The average, high and low amounts, or the distribution of the value at risk amounts for the reporting period; or

(*ii*) The average, high and low amounts, or the distribution of actual changes in fair values, earnings, or cash flows from the market risk sensitive instruments occurring during the reporting period; or

(*iii*) The percentage or number of times the actual changes in fair values, earnings, or cash flows from the market risk sensitive instruments exceeded the value at risk amounts during the reporting period;

(*2*) Information required under paragraph (a)(1)(iii)(B)(*1*) of this Item 305 is not required for the first fiscal year end in which a registrant must present Item 305 information; and

(C) Registrants shall provide a description of the model, assumptions, and parameters, which are necessary to understand the disclosures required under paragraphs (a)(1)(iii)(A) and (B) of this Item 305.

(2) Registrants shall discuss material limitations that cause the information required under paragraph (a)(1) of this Item 305 not to reflect fully the net market risk exposures of the entity. This discussion shall include summarized descriptions of instruments, positions, and transactions omitted from the quantitative market risk disclosure information or the features of instruments, positions, and transactions that are included, but not reflected fully in the quantitative market risk disclosure information.

(3) Registrants shall present summarized market risk information for the preceding fiscal year. In addition, registrants shall discuss the reasons for material quantitative changes in market risk exposures between the current and preceding fiscal years. Information required by this paragraph (a)(3), however, is not required if disclosure is not required under paragraph (a)(1) of this Item 305 for the current fiscal year. Information required by this paragraph (a)(3) is not required for the first fiscal year end in which a registrant must present Item 305 information.

(4) If registrants change disclosure alternatives or key model characteristics, assumptions, and parameters used in providing quantitative information about market risk (*e.g.*, changing from tabular presentation to value at risk, changing the scope of instruments included in the model, or changing the definition of loss from fair values to earnings), and if the effects of any such change is material, the registrant shall:

(i) Explain the reasons for the change; and

(ii) Either provide summarized comparable information, under the new disclosure method, for the year preceding the current year or, in addition to providing disclosure for the current year under the new method, provide disclosures for the current year and preceding fiscal year under the method used in the preceding year.

Instructions to Paragraph 305(a)

1. Under paragraph 305(a)(1):

A. For each market risk exposure category within the trading and other than trading portfolios, registrants may report the average, high, and low sensitivity analysis or value at risk amounts for the reporting period, as an alternative to reporting year-end amounts.

B. In determining the average, high, and low amounts for the fiscal year under instruction 1.A. of the Instructions to Paragraph 305(a), registrants should use sensitivity analysis or value at risk amounts relating to at least four equal time periods throughout the reporting period (*e.g.*, four quarter-end amounts, 12 month-end amounts, or 52 week-end amounts).

C. Functional currency means functional currency as defined by generally accepted accounting principles (see, *e.g.*, FASB, *Statement of Financial Accounting Standards No. 52, ''Foreign Currency Translation''*, (''FAS 52'') paragraph 20 (December 1981)).

D. Registrants using the sensitivity analysis and value at risk disclosure alternatives are encouraged, but not required, to provide quantitative amounts that reflect the aggregate market risk inherent in the trading and other than trading portfolios.

2. Under paragraph 305(a)(1)(i):

A. Examples of contract terms sufficient to determine future cash flows from market risk sensitive instruments include, but are not limited to:

i. Debt instruments—principal amounts and weighted average effective interest rates;

ii. Forwards and futures—contract amounts and weighted average settlement prices;

iii. Options—contract amounts and weighted average strike prices;

iv. Swaps—notional amounts, weighted average pay rates or prices, and weighted average receive rates or prices; and

v. Complex instruments—likely to be a combination of the contract terms presented in 2.A.i. through iv. of this Instruction;

B. When grouping based on common characteristics, instruments should be categorized, at a minimum, by the following characteristics, when material:

i. Fixed rate or variable rate assets or liabilities;

ii. Long or short forwards and futures;

iii. Written or purchased put or call options with similar strike prices;

iv. Receive fixed and pay variable swaps, receive variable and pay fixed swaps, and receive variable and pay variable swaps;

v. The currency in which the instruments' cash flows are denominated;

vi. Financial instruments for which foreign currency transaction gains and losses are reported in the same manner as translation adjustments under generally accepted accounting principles (see, *e.g.*, FAS 52 paragraph 20 (December 1981)); and

vii. Derivatives used to manage risks inherent in anticipated transactions;

C. Registrants may aggregate information regarding functional currencies that are economically related, managed together for internal risk management purposes, and have statistical correlations of greater than 75% over each of the past three years;

D. Market risk sensitive instruments that are exposed to rate or price changes in more than one market risk exposure category should be presented within the tabular information for each of the risk exposure categories to which those instruments are exposed;

E. If a currency swap (see, *e.g.*, FAS 52 Appendix E for a definition of currency swap) eliminates all foreign currency exposures in the cash flows of a foreign currency denominated debt instrument, neither the currency swap nor the foreign currency denominated debt instrument are required to be disclosed in the foreign currency risk exposure category. However, both the currency swap and the foreign currency denominated debt instrument should be disclosed in the interest rate risk exposure category; and

F. The contents of the table and related assumptions that should be described include, but are not limited to:

i. The different amounts reported in the table for various categories of the market risk sensitive instruments (*e.g.*, principal amounts for debt, notional amounts for swaps, and contract amounts for options and futures);

ii. The different types of reported market rates or prices (*e.g.*, contractual rates or prices, spot rates or prices, forward rates or prices); and

iii. Key prepayment or reinvestment assumptions relating to the timing of reported amounts.

3. Under paragraph 305(a)(1)(ii):

A. Registrants should select hypothetical changes in market rates or prices that are expected to reflect reasonably possible near-term changes in those rates and prices. In this regard, absent economic justification for the selection of a different amount, registrants should use changes that are not less than 10 percent of end of period market rates or prices;

B. For purposes of instruction 3.A. of the Instructions to Paragraph 305(a), the term *reasonably possible* has the same meaning as defined by generally accepted accounting principles (see, *e.g.*, FASB, *Statement of Financial Accounting Standards No. 5*, ''*Accounting for Contingencies*,'' (''FAS 5'') paragraph 3 (March 1975));

C. For purposes of instruction 3.A. of the Instructions to Paragraph 305(a), the term *near term* means a period of time going forward up to one year from the date of the financial statements (see generally AICPA, Statement of Position 94–6, ''*Disclosure of Certain Significant Risks and Uncertainties*,'' (''SOP 94–6'') at paragraph 7 (December 30, 1994));

D. Market risk sensitive instruments that are exposed to rate or price changes in more than one market risk exposure category should be included in the sensitivity analysis disclosures for each market risk category to which those instruments are exposed;

E. Registrants with multiple foreign currency exchange rate exposures should prepare foreign currency sensitivity analysis disclosures that measure the aggregate sensitivity to changes in all foreign currency exchange rate exposures, including the effects of changes in both transactional currency/functional currency exchange rate exposures and functional currency/reporting currency exchange rate exposures. For example, assume a French division of a registrant presenting its financial statements in U.S. dollars ($US) invests in a deutschmark(DM)-denominated debt security. In these circumstances, the $US is the reporting currency and the DM is the transactional currency. In addition, assume this division determines that the French franc (FF) is its functional currency according to FAS 52. In preparing the foreign currency sensitivity analysis disclosures, this registrant should report the aggregate potential loss from hypothetical changes in both the DM/FF exchange rate exposure and the FF/$US exchange rate exposure; and

F. Model, assumptions, and parameters that should be described include, but are not limited to, how *loss* is defined by the model (*e.g.*, loss in earnings, fair values, or cash flows), a general description of the modeling technique (*e.g.*, duration modeling, modeling that measures the change in net present values arising from selected hypothetical changes in market rates or prices, and a description as to how optionality is addressed by the model), the types of instruments covered by the model (*e.g.*, derivative financial instruments, other financial instruments, derivative commodity instruments, and whether other instruments are included voluntarily, such as certain commodity instruments and positions, cash flows from anticipated transactions, and certain financial instruments excluded under instruction 3.C.ii. of the General Instructions to Paragraphs 305(a) and 305(b)), and other relevant information about the model's assumptions and parameters, (*e.g.*, the magnitude and timing of selected hypothetical changes in market rates or prices used, the method by which discount rates are determined, and key prepayment or reinvestment assumptions).

4. Under paragraph 305(a)(1)(iii):

A. The confidence intervals selected should reflect reasonably possible near-term changes in market rates and prices. In this regard, absent economic justification for the selection of different confidence intervals, registrants should use intervals that are 95 percent or higher;

B. For purposes of instruction 4.A. of the Instructions to Paragraph 305(a), the term *reasonably possible* has the same meaning as defined by generally accepted accounting principles (see, *e.g.*, FAS 5, paragraph 3 (March 1975));

C. For purposes of instruction 4.A. of the Instructions to Paragraphs 305(a), the term *near term* means a period of time going forward up to one year from the date of the financial statements (see generally SOP 94–6, at paragraph 7 (December 30, 1994));

D. Registrants with multiple foreign currency exchange rate exposures should prepare foreign currency value at risk analysis disclosures that measure the aggregate sensitivity to changes in all foreign currency exchange rate exposures, including the aggregate effects of changes in both transactional currency/functional currency exchange rate exposures and functional currency/reporting currency exchange rate exposures. For example, assume a French division of a registrant presenting its financial statements in U.S. dollars ($US) invests in a deutschmark(DM)-denominated debt security. In these circumstances, the $US is the reporting currency and the DM is the transactional currency. In addition, assume this division determines that the French franc (FF) is its functional currency according to FAS 52. In preparing the foreign currency value at risk disclosures, this registrant should report the aggregate potential loss from hypothetical changes in both the DM/FF exchange rate exposure and the FF/$US exchange rate exposure; and

E. Model, assumptions, and parameters that should be described include, but are not limited to, how *loss* is defined by the model (*e.g.*, loss in earnings, fair values, or cash flows), the type of model used (*e.g.*, variance/covariance, historical simulation, or Monte Carlo simulation and a description as to how optionality is addressed by the model), the types of instruments covered by the model (*e.g.*, derivative financial instruments, other financial instruments, derivative commodity instruments, and whether other instruments are included voluntarily, such as certain commodity instruments and positions, cash flows from anticipated transactions, and certain financial instruments excluded under instruction 3.C.ii. of the General Instructions to Paragraphs 305(a) and 305(b)), and other relevant information about the model's assumptions and parameters, (*e.g.*, holding periods, confidence intervals, and, when appropriate, the methods used for aggregating value at risk amounts across market risk exposure categories, such as by assuming perfect positive correlation, independence, or actual observed correlation).

5. Under paragraph 305(a)(2), limitations that should be considered include, but are not limited to:

A. The exclusion of certain market risk sensitive instruments, positions, and transactions from the disclosures required under paragraph 305(a)(1) (*e.g.*, derivative commodity instruments not permitted by contract or business custom to be settled in cash or with another financial instrument, commodity positions, cash flows from anticipated transactions, and certain financial instruments excluded under instruction 3.C.ii. of the General Instructions to Paragraphs 305(a) and 305(b)). Failure to include such instruments, positions, and transactions in preparing the disclosures under paragraph 305(a)(1) may be a limitation because the resulting disclosures may not fully reflect the net market risk of a registrant; and

B. The ability of disclosures required under paragraph 305(a)(1) to reflect fully the market risk that may be inherent in instruments with leverage, option, or prepayment features (*e.g.*, options, including written options, structured notes, collateralized mortgage obligations, leveraged swaps, and options embedded in swaps).

(b) *Qualitative information about market risk.* (1) To the extent material, describe:

(i) The registrant's primary market risk exposures;

(ii) How those exposures are managed. Such descriptions shall include, but not be limited to, a discussion of the objectives, general strategies, and instruments, if any, used to manage those exposures; and

(iii) Changes in either the registrant's primary market risk exposures or how those exposures are managed, when compared to what was in effect during the most recently completed fiscal year and what is known or expected to be in effect in future reporting periods.

(2) Qualitative information about market risk shall be presented separately for market risk sensitive instruments entered into for trading purposes and those entered into for purposes other than trading.

Instructions to Paragraph 305(b)

1. For purposes of disclosure under paragraph 305(b), *primary market risk exposures* means:

A. The following categories of market risk: interest rate risk, foreign currency exchange rate risk, commodity price risk, and other relevant market rate or price risks (*e.g.*, equity price risk); and

B. Within each of these categories, the particular markets that present the primary risk of loss to the registrant. For example, if a registrant has a material exposure to foreign currency exchange rate risk and, within this category of market risk, is most vulnerable to changes in dollar/yen, dollar/pound, and dollar/peso exchange rates, the registrant should disclose those exposures. Similarly, if a registrant has a material exposure to interest rate risk and, within this category of market risk, is most vulnerable to changes in short-term U.S. prime interest rates, it should disclose the existence of that exposure.

2. For purposes of disclosure under paragraph 305(b), registrants should describe primary market risk exposures that exist as of the end of the latest fiscal year, and how those exposures are managed.

General Instructions to Paragraphs 305(a) and 305(b)

1. The disclosures called for by paragraphs 305(a) and 305(b) are intended to clarify the registrant's exposures to market risk associated with activities in derivative financial instruments, other financial instruments, and derivative commodity instruments.

2. In preparing the disclosures under paragraphs 305(a) and 305(b), registrants are required to include derivative financial instruments, other financial instruments, and derivative commodity instruments.

3. For purposes of paragraphs 305(a) and 305(b), derivative financial instruments, other financial instruments, and derivative commodity instruments (collectively referred to as ''market risk sensitive instruments'') are defined as follows:

A. *Derivative financial instruments* has the same meaning as defined by generally accepted accounting principles (see, *e.g.*, FASB, *Statement of Financial Accounting Standards No. 119, ''Disclosure about Derivative Financial Instruments and Fair Value of Financial Instruments,''* (''FAS 119'') paragraphs 5–7 (October 1994)), and includes futures, forwards, swaps, options, and other financial instruments with similar characteristics;

B. *Other financial instruments* means all financial instruments as defined by generally accepted accounting principles for which fair value disclosures are required (see, *e.g.*, FASB, *Statement of Financial Accounting Standards No. 107, ''Disclosures about Fair Value of Financial Instruments,''* (''FAS 107'') paragraphs 3 and 8 (December 1991)), except for derivative financial instruments, as defined above;

C.i. Other financial instruments include, but are not limited to, trade accounts receivable, investments, loans, structured notes, mortgage-backed securities, trade accounts payable, indexed debt instruments, interest-only and principal-only obligations, deposits, and other debt obligations;

ii. Other financial instruments exclude employers' and plans' obligations for pension and other post-retirement benefits, substantively extinguished debt, insurance contracts, lease contracts, warranty obligations and rights, unconditional purchase obligations, investments accounted for under the equity method, minority interests in consolidated enterprises, and equity instruments issued by the registrant and classified in stockholders' equity in the statement of financial position (see, *e.g.*, FAS 107, paragraph 8 (December 1991)). For purposes of this item, trade accounts receivable and trade accounts payable need not be considered other financial instruments when their carrying amounts approximate fair value; and

D. *Derivative commodity instruments* include, to the extent such instruments are not derivative financial instruments, commodity futures, commodity forwards, commodity swaps, commodity options, and other commodity instruments with similar characteristics that are permitted by contract or business custom to be settled in cash or with another financial instrument. For purposes of this paragraph, settlement in cash includes settlement in cash of the net change in value of the derivative commodity instrument (*e.g.*, net cash settlement based on changes in the price of the underlying commodity).

4.A. In addition to providing required disclosures for the market risk sensitive instruments defined in instruction 2. of the General Instructions to Paragraphs 305(a) and 305(b), registrants are encouraged to include other market risk sensitive instruments, positions, and transactions within the disclosures required under paragraphs 305(a) and 305(b). Such instruments, positions, and transactions might include commodity positions, derivative commodity instruments that are not permitted by contract or business custom to be settled in cash or with another financial instrument, cash flows from anticipated transactions, and certain financial instruments excluded under instruction 3.C.ii. of the General Instructions to Paragraphs 305(a) and 305(b).

B. Registrants that voluntarily include other market risk sensitive instruments, positions and transactions within their quantitative disclosures about market risk under the sensitivity analysis or value at risk disclosure alternatives are not required to provide separate market risk disclosures for any voluntarily selected instruments, positions, or transactions. Instead, registrants selecting the sensitivity analysis and value at risk disclosure alternatives are permitted to present comprehensive market risk disclosures, which reflect the combined market risk exposures inherent in both the required and any voluntarily selected instruments, position, or transactions. Registrants that choose the tabular presentation disclosure alternative should present voluntarily selected instruments, positions, or transactions in a manner consistent with the requirements in Item 305(a) for market risk sensitive instruments.

C. If a registrant elects to include voluntarily a particular type of instrument, position, or transaction in their quantitative disclosures about market risk, that registrant should include all, rather than some, of those instruments, positions, or transactions within those disclosures. For example, if a registrant holds in inventory a particular type of commodity position and elects to include that commodity position within their market risk disclosures, the registrant should include the entire commodity position, rather than only a portion thereof, in their quantitative disclosures about market risk.

5.A. Under paragraphs 305(a) and 305(b), a materiality assessment should be made for each market risk exposure category within the trading and other than trading portfolios.

B. For purposes of making the materiality assessment under instruction 5.A. of the General Instructions to Paragraphs 305(a) and 305(b), registrants should evaluate both:

i. The materiality of the fair values of derivative financial instruments, other financial instruments, and derivative commodity instruments outstanding as of the end of the latest fiscal year; and

ii. The materiality of potential, near-term losses in future earnings, fair values, and/or cash flows from reasonably possible near-term changes in market rates or prices.

iii. If either paragraphs B.i. or B.ii. in this instruction of the General Instructions to Paragraphs 305(a) and 305(b) are material, the registrant should disclose quantitative and qualitative information about market risk, if such market risk for the particular market risk exposure category is material.

C. For purposes of instruction 5.B.i. of the General Instructions to Paragraphs 305(a) and 305(b), registrants generally should not net fair values, except to the extent allowed under generally accepted accounting principles (see, *e.g., FASB Interpretation No. 39, ''Offsetting of Amounts Related to Certain Contracts''* (March 1992)). For example, under this instruction, the fair value of assets generally should not be netted with the fair value of liabilities.

D. For purposes of instruction 5.B.ii. of the General Instructions to Paragraphs 305(a) and 305(b), registrants should consider, among other things, the magnitude of:

i. Past market movements;

ii. Reasonably possible, near-term market movements; and

iii. Potential losses that may arise from leverage, option, and multiplier features.

E. For purposes of instructions 5.B.ii and 5.D.ii of the General Instructions to Paragraphs 305(a) and 305(b), the term *near term* means a period of time going forward up to one year from the date of the financial statements (see generally SOP 94–6, at paragraph 7 (December 30, 1994)).

F. For the purpose of instructions 5.B.ii. and 5.D.ii. of the General Instructions to Paragraphs 305(a) and 305(b), the term *reasonably possible* has the same meaning as defined by generally accepted accounting principles (see, *e.g.,* FAS 5, paragraph 3 (March 1975)).

6. For purposes of paragraphs 305(a) and 305(b), registrants should present the information outside of, and not incorporate the information into, the financial statements (including the footnotes to the financial statements). In addition, registrants are encouraged to provide the required information in one location. However, alternative presentation, such as inclusion of all or part of the information in Management's Discussion and Analysis, may be used at the discretion of the registrant. If information is disclosed in more than one location, registrants should provide cross-references to the locations of the related disclosures.

7. For purposes of the instructions to paragraphs 305(a) and 305(b), *trading purposes* has the same meaning as defined by generally accepted accounting principles (see, *e.g.,* FAS 119, paragraph 9a (October 1994)). In addition, *anticipated transactions* means transactions (other than transactions involving existing assets or liabilities or transactions necessitated by existing firm commitments) an enterprise expects, but is not obligated, to carry out in the normal course of business (see, *e.g.,* FASB, *Statement of Financial Accounting Standards No. 80, ''Accounting for Futures Contracts,''* paragraph 9, (August 1984)).

(c) *Interim periods.* If interim period financial statements are included or are required to be included by Article 3 of Regulation S–X (17 CFR 210), discussion and analysis shall be provided so as to enable the reader to assess the sources and effects of material changes in information that would be provided under Item 305 of Regulation S–K from the end of the preceding fiscal year to the date of the most recent interim balance sheet.

Instructions to Paragraph 305(c)

1. Information required under paragraph (c) of this Item 305 is not required until after the first fiscal year end in which this Item 305 is applicable.

(d) *Safe Harbor.* (1) The safe harbor provided in Section 27A of the Securities Act of 1933 (15 U.S.C. 77z–2) and Section 21E of the Securities Exchange Act of 1934 (15 U.S.C. 78u–5) (''statutory safe harbors'') shall apply, with respect to all types of issuers and transactions, to information provided pursuant to paragraphs (a), (b), and (c) of this Item 305, provided that the disclosure is made by: an issuer; a person acting on behalf of the issuer; an outside reviewer retained by the issuer making a statement on behalf of the issuer; or an underwriter, with respect to information provided by the issuer or information derived from information provided by the issuer.

(2) For purposes of paragraph (d) of this Item 305 only:

(i) All information required by paragraphs (a), (b)(1)(i), (b)(1)(iii), and (c) of this Item 305 is considered *forward looking statements* for purposes of the statutory safe harbors, except for historical facts such as the terms of particular contracts and the number of market risk sensitive instruments held during or at the end of the reporting period; and

(ii) With respect to paragraph (a) of this Item 305, the *meaningful cautionary statements* prong of the statutory safe harbors will be satisfied if a registrant satisfies all requirements of that same paragraph (a) of this Item 305.

(e) *Small business issuers.* Small business issuers, as defined in § 230.405 of this chapter and § 230.12b–2 of this chapter, need not provide the information required by this Item 305, whether or not they file on forms specially designated as small business issuer forms.

General Instructions to Paragraphs 305(a), 305(b), 305(c), 305(d), and 305(e)

1. Bank registrants, thrift registrants, and non-bank and non-thrift registrants with market capitalizations on January 28, 1997 in excess of $2.5 billion should provide Item 305 disclosures in filings with the Commission that include annual financial statements for fiscal years ending after June 15, 1997. Non-bank and non-thrift registrants with market capitalizations on January 28, 1997 of $2.5 billion or less should provide Item 305 disclosures in filings with the Commission that include financial statements for fiscal years ending after June 15, 1998.

2.A. For purposes of instruction 1. of the General Instructions to Paragraphs 305(a), 305(b), 305(c), 305(d), and 305(e), *bank registrants and thrift registrants* include any registrant which has control over a depository institution.

B. For purposes of instruction 2.A. of the General Instructions to Paragraphs 305(a), 305(b), 305(c), 305(d), and 305(e), a registrant has control over a depository institution if:

i. The registrant directly or indirectly or acting through one or more other persons owns, controls, or has power to vote 25% or more of any class of voting securities of the depository institution;

ii. The registrant controls in any manner the election of a majority of the directors or trustees of the depository institution; or

iii. The Federal Reserve Board or Office of Thrift Supervision determines, after notice and opportunity for hearing, that the registrant directly or indirectly exercises a controlling influence over the management or policies of the depository institution.

C. For purposes of instruction 2.B. of the General Instructions to Paragraphs 305(a), 305(b), 305(c), 305(d), and 305(e), a depository institution means any of the following:

i. An insured depository institution as defined in section 3(c)(2) of the Federal Deposit Insurance Act (12 U.S.C.A. Sec. 1813 (c));

ii. An institution organized under the laws of the United States, any State of the United States, the District of Columbia, any territory of the United States, Puerto Rico, Guam, American Somoa, or the Virgin Islands, which both accepts demand deposits or deposits that the depositor may withdraw by check or similar means for payment to third parties or others and is engaged in the business of making commercial loans.

D. For purposes of instruction 1. of the General Instructions to Paragraphs 305(a), 305(b), 305(c), 305(d) and 305(e), *market capitalization* is the aggregate market value of common equity as set forth in General Instruction I.B.1. of Form S–3; provided however, that common equity held by affiliates is included in the calculation of market capitalization; and provided further that instead of using the 60 day period prior to filing referenced in General Instruction I.B.1. of Form S–3, the measurement date is January 28, 1997.

Appendix to Item 305—Tabular Disclosures

The tables set forth below are illustrative of the format that might be used when a registrant elects to present the information required by paragraph (a)(1)(i)(A) of Item 305 regarding terms and information about derivative financial instruments, other financial instruments, and derivative commodity instruments. These examples are for illustrative purposes only. Registrants are not required to display the information in the specific format illustrated below. Alternative methods of display are permissible as long as the disclosure requirements of the section are satisfied. Furthermore, these examples were designed primarily to illustrate possible formats for presentation of the information required by the disclosure item and do not purport to illustrate the broad range of derivative financial instruments, other financial instruments, and derivative commodity instruments utilized by registrants.

Interest Rate Sensitivity

The table below provides information about the Company's derivative financial instruments and other financial instruments that are sensitive to changes in interest rates, including interest rate swaps and debt obligations. For debt obligations, the table presents principal cash flows and related weighted average interest rates by expected maturity dates. For interest rate swaps, the table presents notional amounts and weighted average interest rates by expected (contractual) maturity dates. Notional amounts are used to calculate the contractual payments to be exchanged under the contract. Weighted average variable rates are based on implied forward rates in the yield curve at the reporting date. The information is presented in U.S. dollar equivalents, which is the Company's reporting currency. The instrument's actual cash flows are denominated in both U.S. dollars ($US) and German deutschmarks (DM), as indicated in parentheses.

December 31, 19X1

	Expected maturity date							
	19X2	19X3	19X4	19X5	19X6	There-after	Total	Fair value
Liabilities	(US$ Equivalent in millions)							
Long-term Debt:								
Fixed Rate ($US)	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX
Average interest rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Fixed Rate (DM)	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX
Average interest rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Variable Rate ($US)	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX
Average interest rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Interest Rate Derivatives	(In millions)							
Interest Rate Swaps:								
Variable to Fixed ($US)	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX
Average pay rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Average receive rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Fixed to Variable ($US)	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX
Average pay rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Average receive rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	

Exchange Rate Sensitivity

The table below provides information about the Company's derivative financial instruments, other financial instruments, and firmly committed sales transactions by functional currency and presents such information in U.S. dollar equivalents.[1] The table summarizes information on instruments and transactions that are sensitive to foreign currency exchange rates, including foreign currency forward exchange agreements, deutschmark (DM)-denominated debt obligations, and firmly committed DM sales transactions. For debt obligations, the table presents principal cash flows and related weighted average interest rates by expected maturity dates. For firmly committed DM-sales transactions, sales amounts are presented by the expected transaction date, which are not expected to exceed two years. For foreign currency forward exchange agreements, the table presents the notional amounts and weighted average exchange rates by expected (contractual) maturity dates. These notional amounts generally are used to calculate the contractual payments to be exchanged under the contract.

December 31, 19X1

	Expected maturity date							
	19X2	19X3	19X4	19X5	19X6	There-after	Total	Fair value
On-Balance Sheet Financial Instruments	(US$ Equivalent in millions)							
$US Functional Currency[2]:								
Liabilities								
Long-Term Debt:								
Fixed Rate (DM)	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX
Average interest rate	X.X	X.X	X.X	X.X	X.X	X.X	X.X	....
Anticipated Transactions and Related Derivatives[3]	Expected maturity or transaction date (US$ Equivalent in millions)							
$US Functional Currency:								

[1] The information is presented in U.S. dollars because that is the registrant's reporting currency.

December 31, 19X1

	Expected maturity date							
	19X2	19X3	19X4	19X5	19X6	There-after	Total	Fair value
Firmly committed Sales Contracts (DM)	$XXX	$XXX	....	....	....	....	$XXX	$XXX
Forward Exchange Agreements (Receive $US/Pay DM):.								
Contract Amount	XXX	XXX	....	....	....	....	XXX	XXX
Average Contractual Exchange Rate	X.X	X.X	....	....	....	....	X.X	....

[2] Similar tabular information would be provided for other functional currencies.

[3] Pursuant to General Instruction 4. to Items 305(a) and 305(b) of Regulation S–K, registrants may include cash flows from anticipated transactions and operating cash flows resulting from non-financial and non-commodity instruments.

Commodity Price Sensitivity

The table below provides information about the Company's corn inventory and futures contracts that are sensitive to changes in commodity prices, specifically corn prices. For inventory, the table presents the carrying amount and fair value at December 31, 19x1. For the futures contracts the table presents the notional amounts in bushels, the weighted average contract prices, and the total dollar contract amount by expected maturity dates, the latest of which occurs one year from the reporting date. Contract amounts are used to calculate the contractual payments and quantity of corn to be exchanged under the futures contracts.

December 31, 19X1

	Carrying amount	Fair value
	(In millions)	
On Balance Sheet Commodity Position and Related Derivatives		
Corn Inventory [4]	$XXX	$XXX
	Expected maturity 1992	Fair value
Related Derivatives		
Futures Contracts (Short):		
Contract Volumes (100,000 bushels)	XXX	....
Weighted Average Price (Per 100,000 bushels)	$X.XX	....
Contract Amount ($US in millions)	$XXX	$XXX

[4] Pursuant to General Instruction 4. to Items 305(a) and 305(b) of Regulation S–K, registrants may include information on commodity positions, such as corn inventory.

PART 239—FORMS PRESCRIBED UNDER THE SECURITIES ACT OF 1933

8. The general authority citation for Part 239 is revised to read, in part, as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77z–2, 77sss, 78c, 78*l*, 78m, 78n, 78o(d), 78u–5, 78w(a), 78*ll*(d), 79e, 79f, 79g, 79j, 79*l*, 79m, 79n, 79q, 79t, 80a–8, 80a–29, 80a–30 and 80a–37, unless otherwise noted.

* * * * *

9. By amending Form S–1 (referenced in § 239.11) by redesignating Items 11(j) through 11(m) as Items 11(k) through 11(n) and adding Item 11(j) to read as follows:

Note—The text of Form S–1 does not, and this amendment will not, appear in the Code of Federal Regulations.

Form S–1—Registration Statement Under the Securities Act of 1933

* * * * *

Item 11. Information with Respect to the Registrant

* * * * *

(j) Information required by Item 305 of Regulation S–K (§ 229.305 of this chapter), quantitative and qualitative disclosures about market risk.

* * * * *

10. By amending Form S–2 (referenced in § 239.12) by adding paragraph (9) to Item 11(b), removing ''and'' at the end of Item 12(a)(3)(vii), removing the period at the end of Item 12(a)(3)(viii) and in its place adding ''; and'', and adding paragraph (ix) to Item 12(a)(3) to read as follows:

Note—The text of Form S–2 does not, and this amendment will not, appear in the Code of Federal Regulations.

Form S–2—Registration Statement Under the Securities Act of 1933

* * * * *

Item 11. Information with Respect to the Registrant

(a) * * *

(b) * * *

(9) Furnish quantitative and qualitative disclosures about market risk required by Item 305 of Regulation S–K (§ 229.305 of this chapter).

* * * * *

Item 12. Incorporation of Certain Information by Reference

(a) * * *

(3) * * *

(ix) quantitative and qualitative disclosures about market risk as required by Item 305 of Regulation S–K (§ 229.305 of this chapter).

* * * * *

11. By amending Form S–11 (referenced in § 239.18) to redesignate Items 30 through 36 as Items 31 through 37 and to add Item 30 to Part I to read as follows:

Note—The text of Form S–11 does not, and this amendment will not, appear in the Code of Federal Regulations.

Form S–11—Registration Statement Under the Securities Act of 1933

* * * * *

Item 30. Quantitative and Qualitative Disclosures About Market Risk

Furnish the information required by Item 305 of Regulation S–K (§ 229.305 of this chapter).

* * * * *

12. By amending Form S–4 (referenced in § 239.25) by removing ''and'' at the end of Item 12(b)(3)(v) and the period at the end of Item 12(b)(3)(vi) and in its place adding ''; and'', adding paragraph (vii) to Item 12(b)(3), removing ''and'' at the end of Item 13(a)(3)(v) and the period at the end of Item 13(a)(3)(vi) and in its place adding ''; and'', adding paragraph (vii) to Item 13(a)(3), removing ''and'' at the end of Item 14(h) and the period at the end of Item 14(i) and in its place adding ''; and'', adding paragraph (j) to Item 14, and adding paragraph (10) to Item 17(b) to read as follows:

Note—The text of Form S–4 does not, and this amendment will not, appear in the Code of Federal Regulations.

Form S–4—Registration Statement Under the Securities Act of 1933

* * * * *

Item 12. Information with Respect to S–2 or S–3 Registrants

* * * * *

(b) * * *

(3) * * *

(vii) Item 305 of Regulation S–K (§ 229.305 of this chapter), quantitative and qualitative disclosures about market risk.

* * * * *

Item 13. Incorporation of Certain Information by Reference

* * * * *

(a) * * *

(3) * * *

(vii) Item 305 of Regulation S–K (§ 229.305 of this chapter) quantitative and qualitative disclosures about market risk.

* * * * *

Item 14. Information with Respect to Registrants Other Than S–3 or S–2 Registrants

* * * * *

(j) Item 305 of Regulation S–K (§ 229.305 of this chapter), quantitative and qualitative disclosures about market risk.

* * * * *

Item 17. Information with Respect to Companies Other Than S–3 or S–2 Companies

* * * * *

(b) * * *

(10) Item 305 of Regulation S–K (§ 229.305 of this chapter), quantitative and qualitative disclosures about market risk.

* * * * *

13. By amending Form F–4 (referenced in § 239.34) to redesignate Item 12(b)(3)(vi) as Item 12(b)(3)(vi)(A), add paragraph (B) to Item 12(b)(3)(vi), redesignate Item 14(g) as Item 14(g)(1), add Item 14(g)(2), redesignate Item 17(b)(4) as Item 17(b)(4)(i), and add Item 17(b)(4)(ii) to read as follows:

Note—The text of Form F–4 does not, and this amendment will not, appear in the Code of Federal Regulations.

Form F–4—Registration Statement Under the Securities Act of 1933

* * * * *

Item 12. Information With Respect to F–2 or F–3 Registrants

* * * * *

(b) * * *

(3) * * *

(vi)(A) * * *

(B) Item 9A of Form 20–F, quantitative and qualitative disclosures of market risk.

* * * * *

Item 14. Information With Respect to Foreign Registrants Other Than F–2 or F–3 Registrants

* * * * *

(g)(1) * * *

(2) Item 9A of Form 20–F, quantitative and qualitative disclosures of market risk.

* * * * *

Item 17. Information With Respect to Foreign Companies Other Than F–2 or F–3 Companies

* * * * *

(b) * * *

(4)(i) * * *

(b)(4)(ii) Item 9A of Form 20–F, quantitative and qualitative disclosures of market risk.

* * * * *

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

14. The general authority citation for Part 240 is revised to read in part as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z–2, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78f, 78i, 78j, 78k, 78k–1, 78*l*, 78m, 78n, 78o, 78p, 78q, 78s, 78u–5, 78w, 78x, 78*ll*(d), 79q, 79t, 80a–20, 80a–23, 80a–29, 80a–37, 80b–3, 80b–4 and 80b–11, unless otherwise noted.

* * * * *

15. By amending § 240.14a-3 by adding paragraph (b)(5)(iii) to read as follows:

§ 240.14a–3 Information to be furnished to security holders.

* * * * *

(b) * * *

(5) * * *

(iii) The report shall contain the quantitative and qualitative disclosures about market risk required by Item 305 of Regulation S–K (§ 229.305 of this chapter).

* * * * *

16. By amending § 240.14a–101 to remove the word ''and'' at the end of Item 13(a)(4), redesignate Item 13(a)(5) as Item 13(a)(6), add Item 13(a)(5), add Instruction 6 to Item 13, remove ''and'' at the end of Item 14(b)(2)(i)(B)*(3)(vi)* and the period at the end of Item 14(b)(2)(i)(B)*(3)(vii)* and in its place add ''; and'', add paragraph *(viii)* to Item 14(b)(2)(i)(B)*(3)*, remove ''and'' at the end of Item 14(b)(2)(ii)(A)*(3)(v)* and the period at the end of Item 14(b)(2)(ii)(A)*(3)(vi)* and in its place add ''; and'', add paragraph *(vii)* to Item 14(b)(2)(ii)(A)*(3)*, remove ''and'' at the end of Item 14(b)(3)(i)(H) and the period at the end of Item 14(b)(3)(i)(I) and in its place add ''; and'', add paragraph (J) to Item 14(b)(3)(i), and add Instruction 8 to Item 14 to read as follows:

§ 240.14a–101 Schedule 14A. Information required in proxy statement.

* * * * *

Item 13. Financial and other information

(a) *Information required*. * * *

(5) Item 305 of Regulation S–K, quantitative and qualitative disclosures about market risk; and

* * * * *

Instructions to Item 13

* * * * *

6. A registered investment company need not comply with items (a)(2), (a)(3), and (a)(5) of this Item 13.

* * * * *

Item 14. Mergers, consolidations, acquisitions and similar matters

* * * * *

(b) Information about the registrant and the other person.

* * * * *

(2) Information with respect to S–2 or S–3 registrants.

(i) Information required to be furnished. * * *

(B) * * *

(3) * * *

(viii) Item 305 of Regulation S–K (§ 229.305 of this chapter), quantitative and qualitative disclosures about market risk.

(ii) *Incorporation of certain information by reference.* ***

(A) * * *

(3) * * *

(vii) Item 305 of Regulation S–K (§ 229.305 of this chapter), quantitative and qualitative disclosures about market risk.

* * * * *

(3) *Information with respect to registrants other than S–2 or S–3 registrants.*

(i) * * *

(J) Item 305 of Regulation S–K (§ 229.305 of this chapter), quantitative and qualitative disclosures about market risk.

* * * * *

Instructions to Item 14

* * * * *

8. A registered management investment company need not comply with items (A), (D), (F), (G), (H), and (J) of paragraph (b)(3)(i) of this Item 14.

* * * * *

PART 249—FORMS, SECURITIES EXCHANGE ACT OF 1934

17. The authority for Part 249 continues to read, in part, as follows:

Authority: 15 U.S.C. 78a, *et seq.*, unless otherwise noted;

18. By amending Form 10 (referenced in § 249.210) by revising Item 2 to read as follows:

Note—The text of Form 10 does not, and this amendment will not, appear in the Code of Federal Regulations.

Form 10—General Form for Registration of Securities

* * * * *

Item 2. Financial Information

Furnish the information required by Items 301, 303, and 305 of Regulation S–K (§§ 229.301, 229.303, and 229.305 of this chapter).

* * * * *

19. By amending Form 20-F (referenced in § 249.220f) by adding Item 9A to be inserted after Item 9 and before Item 10 in Part I to read as follows:

Note—The text of Form 20-F does not, and this amendment will not, appear in the Code of Federal Regulations.

Form 20–F—Registration Statement Pursuant to Section 12(b) or (g) of the Securities Exchange Act of 1934; or Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934; or Transaction Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

* * * * *

Part I

* * * * *

Item 9A. Quantitative and Qualitative Disclosures About Market Risk

(a) *Quantitative information about market risk.* (1) Registrants shall provide, in their reporting currency, quantitative information about market risk as of the end of the latest fiscal year, in accordance with one of the following three disclosure alternatives. In preparing this quantitative information, registrants shall categorize market risk sensitive instruments into instruments entered into for trading purposes and instruments entered into for purposes other than trading purposes. Within both the trading and other than trading portfolios, separate quantitative information shall be presented, to the extent material, for each market risk exposure category (*i.e.*, interest rate risk, foreign currency exchange rate risk, commodity price risk, and other relevant market risks, such as equity price risk). A registrant may use one of the three alternatives set forth below for all of the required quantitative disclosures about market risk. A registrant also may choose, from among the three alternatives, one disclosure alternative for market risk sensitive instruments entered into for trading purposes and another disclosure alternative for market risk sensitive instruments entered into for other than trading purposes. Alternatively, a registrant may choose any disclosure alternative, from among the three alternatives, for each risk exposure category within the trading and other than trading portfolios. The three disclosure alternatives are:

(i)(A)(*1*) Tabular presentation of information related to market risk sensitive instruments; such information shall include fair values of the market risk sensitive instruments and contract terms sufficient to determine future cash flows from those instruments, categorized by expected maturity dates.

(*2*) Tabular information relating to contract terms shall allow readers of the table to determine expected cash flows from the market risk sensitive instruments for each of the next five years. Comparable tabular information for any remaining years shall be displayed as an aggregate amount.

(*3*) Within each risk exposure category, the market risk sensitive instruments shall be grouped based on common characteristics. Within the foreign currency exchange rate risk category, the market risk sensitive instruments shall be grouped by functional currency and within the commodity price risk category, the market risk sensitive instruments shall be grouped by type of commodity.

(*4*) See the Appendix to this Item for a suggested format for presentation of this information; and

(B) Registrants shall provide a description of the contents of the table and any related assumptions necessary to understand the disclosures required under paragraph (a)(1)(i)(A) of this Item 9A; or

(ii)(A) Sensitivity analysis disclosures that express the potential loss in future earnings, fair values, or cash flows of market risk sensitive instruments resulting from one or more selected hypothetical changes in interest rates, foreign currency exchange rates, commodity prices, and other relevant market rates or prices over a selected period of time. The magnitude of selected hypothetical changes in rates or prices may differ among and within market risk exposure categories; and

(B) Registrants shall provide a description of the model, assumptions, and parameters, which are necessary to understand the disclosures required under paragraph (a)(1)(ii)(A) of this Item 9A; or

(iii)(A) Value at risk disclosures that express the potential loss in future earnings, fair values, or cash flows of market risk sensitive instruments over a selected period of time, with a selected likelihood of occurrence, from changes in interest rates, foreign currency exchange rates, commodity prices, and other relevant market rates or prices;

(B)(*1*) For each category for which value at risk disclosures are required under paragraph (a)(1)(iii)(A) of this Item 9A, provide either:

(*i*) The average, high and low amounts, or the distribution of the value at risk amounts for the reporting period; or

(*ii*) The average, high and low amounts, or the distribution of actual changes in fair values, earnings, or cash flows from the market risk sensitive instruments occurring during the reporting period; or

(*iii*) The percentage or number of times the actual changes in fair values, earnings, or cash flows from the market risk sensitive instruments exceeded the value at risk amounts during the reporting period;

(*2*) Information required under paragraph (a)(1)(iii)(B)(*1*) of this Item 9A is not required for the first fiscal year end in which a registrant must present Item 9A information; and

(C) Registrants shall provide a description of the model, assumptions, and parameters, which are necessary to understand the disclosures required under paragraphs (a)(1)(iii) (A) and (B) of this Item 9A.

(2) Registrants shall discuss material limitations that cause the information required under paragraph (a)(1) of this Item 9A not to reflect fully the net market risk exposures of the entity. This discussion shall include summarized descriptions of instruments, positions, and transactions omitted from the quantitative market risk disclosure information or the features of instruments, positions, and transactions that are included, but not reflected fully in the quantitative market risk disclosure information.

(3) Registrants shall present summarized market risk information for the preceding fiscal year. In addition, registrants shall discuss the reasons for material quantitative changes in market risk exposures between the current and preceding fiscal years. Information required by this paragraph (a)(3), however, is not required if disclosure is not required under paragraph (a)(1) of this Item 9A for the current fiscal year. Information required by this paragraph (a)(3) is not required for the first fiscal year end in which a registrant must present Item 9A information.

(4) If registrants change disclosure alternatives or key model characteristics, assumptions, and parameters used in providing quantitative information about market risk (*e.g.*, changing from tabular presentation to value at risk, changing the scope of instruments included in the model, or changing the definition of loss from fair values to earnings), and if the effects of any such change is material, the registrant shall:

(i) Explain the reasons for the change; and

(ii) Either provide summarized comparable information, under the new disclosure method, for the year preceding the current year or, in addition to providing disclosure for the current year under the new method, provide disclosures for the current year and preceding fiscal year under the method used in the preceding year.

Instructions to Item 9A(a)

1. Under Item 9A(a)(1):

A. For each market risk exposure category within the trading and other than trading portfolios, registrants may report the average, high, and low sensitivity analysis or value at risk amounts for the reporting period, as an alternative to reporting year-end amounts.

B. In determining the average, high, and low amounts for the fiscal year under instruction 1.A. of the Instructions to Item 9A(a), registrants should use sensitivity analysis or value at risk amounts relating to at least four equal time periods throughout the reporting period (*e.g.*, four quarter-end amounts, 12 month-end amounts, or 52 week-end amounts).

C. Functional currency means functional currency as defined by generally accepted accounting principles (see, *e.g.*, FASB, *Statement of Financial Accounting Standards No. 52*, ‘‘*Foreign Currency Translation*’’, (‘‘FAS 52’’) paragraph 20 (December 1981)).

D. Registrants using the sensitivity analysis and value at risk disclosure alternatives are encouraged, but not required, to provide quantitative amounts that reflect the aggregate market risk inherent in the trading and other than trading portfolios.

2. Under Item 9A(a)(1)(i):

A. Examples of contract terms sufficient to determine future cash flows from market risk sensitive instruments include, but are not limited to:

i. Debt instruments—principal amounts and weighted average effective interest rates;

ii. Forwards and futures—contract amounts and weighted average settlement prices;

iii. Options—contract amounts and weighted average strike prices;

iv. Swaps—notional amounts, weighted average pay rates or prices, and weighted average receive rates or prices; and

v. Complex instruments—likely to be a combination of the contract terms presented in 2.A.i. through iv. of this Instruction;

B. When grouping based on common characteristics, instruments should be categorized, at a minimum, by the following characteristics, when material:

i. Fixed rate or variable rate assets or liabilities;

ii. Long or short forwards and futures;

iii. Written or purchased put or call options with similar strike prices;

iv. Receive fixed and pay variable swaps, receive variable and pay fixed swaps, and receive variable and pay variable swaps;

v. The currency in which the instruments' cash flows are denominated;

vi. Financial instruments for which foreign currency transaction gains and losses are reported in the same manner as translation adjustments under generally accepted accounting principles (see, *e.g.*, FAS 52 paragraph 20 (December 1981)); and

vii. Derivatives used to manage risks inherent in anticipated transactions;

C. Registrants may aggregate information regarding functional currencies that are economically related, managed together for internal risk management purposes, and have statistical correlations of greater than 75% over each of the past three years;

D. Market risk sensitive instruments that are exposed to rate or price changes in more than one market risk exposure category should be presented within the tabular information for each of the risk exposure categories to which those instruments are exposed;

E. If a currency swap (see, *e.g.*, FAS 52 Appendix E for a definition of currency swap) eliminates all foreign currency exposures in the cash flows of a foreign currency denominated debt instrument, neither the currency swap nor the foreign currency denominated debt instrument are required to be disclosed in the foreign currency risk exposure category. However, both the currency swap and the foreign currency denominated debt instrument should be disclosed in the interest rate risk exposure category; and

F. The contents of the table and related assumptions that should be described include, but are not limited to:

i. The different amounts reported in the table for various categories of the market risk sensitive instruments (*e.g.*, principal amounts for debt, notional amounts for swaps, and contract amounts for options and futures);

ii. The different types of reported market rates or prices (*e.g.*, contractual rates or prices, spot rates or prices, forward rates or prices); and

iii. Key prepayment or reinvestment assumptions relating to the timing of reported amounts.

3. Under Item 9A(a)(1)(ii):

A. Registrants should select hypothetical changes in market rates or prices that are expected to reflect reasonably possible near-term changes in those rates and prices. In this regard, absent economic justification for the selection of a different amount, registrants should use changes that are not less than 10 percent of end of period market rates or prices;

B. For purposes of instruction 3.A. of the Instructions to Item 9A(a), the term *reasonably possible* has the same meaning as defined by generally accepted accounting principles (see, *e.g.*, FASB, *Statement of Financial Accounting Standards No. 5*, ''*Accounting for Contingencies*,'' (''FAS 5'') paragraph 3 (March 1975));

C. For purposes of instruction 3.A. of the Instructions to Item 9A(a), the term *near term* means a period of time going forward up to one year from the date of the financial statements (see generally AICPA, Statement of Position 94–6, ''*Disclosure of Certain Significant Risks and Uncertainties*,'' (''SOP 94–6'') at paragraph 7 (December 30, 1994));

D. Market risk sensitive instruments that are exposed to rate or price changes in more than one market risk exposure category should be included in the sensitivity analysis disclosures for each market risk category to which those instruments are exposed;

E. Registrants with multiple foreign currency exchange rate exposures should prepare foreign currency sensitivity analysis disclosures that measure the aggregate sensitivity to changes in all foreign currency exchange rate exposures, including the effects of changes in both transactional currency/functional currency exchange rate exposures and functional currency/reporting currency exchange rate exposures. For example, assume a French division of a registrant presenting its financial statements in U.S. dollars ($US) invests in a deutschmark(DM)-denominated debt security. In these circumstances, the $US is the reporting currency and the DM is the transactional currency. In addition, assume this division determines that the French franc (FF) is its functional currency according to FAS 52. In preparing the foreign currency sensitivity analysis disclosures, this registrant should report the aggregate potential loss from hypothetical changes in both the DM/FF exchange rate exposure and the FF/$US exchange rate exposure; and

F. Model, assumptions, and parameters that should be described include, but are not limited to, how *loss* is defined by the model (*e.g.*, loss in earnings, fair values, or cash flows), a general description of the modeling technique (*e.g.*, duration modeling, modeling that measures the change in net present values arising from selected hypothetical changes in market rates or prices, and a description as to how optionality is addressed by the model), the types of instruments covered by the model (*e.g.*, derivative financial instruments, other financial instruments, derivative commodity instruments, and whether other instruments are included voluntarily, such as certain commodity instruments and positions, cash flows from anticipated transactions, and certain financial instruments excluded under instruction 3.C.ii. of the General Instructions to Items 9A(a) and 9A(b)), and other relevant information about the model's assumptions and parameters (*e.g.*, the magnitude and timing of selected hypothetical changes in market rates or prices used, the method by which discount rates are determined, and key prepayment or reinvestment assumptions).

4. Under Item 9A(a)(1)(iii):

A. The confidence intervals selected should reflect reasonably possible near-term changes in market rates and prices. In this regard, absent economic justification for the selection of different confidence intervals, registrants should use intervals that are 95 percent or higher;

B. For purposes of instruction 4.A. of the Instructions to Item 9A(a), the term *reasonably possible* has the same meaning as defined by generally accepted accounting principles (see, *e.g.*, FAS 5, paragraph 3 (March 1975));

C. For purposes of instruction 4.A. of the Instructions to Item 9A(a), the term *near term* means a period of time going forward up to one year from the date of the financial statements (see generally SOP 94–6, at paragraph 7 (December 30, 1994));

D. Registrants with multiple foreign currency exchange rate exposures should prepare foreign currency value at risk analysis disclosures that measure the aggregate sensitivity to changes in all foreign currency exchange rate exposures, including the aggregate effects of changes in both transactional currency/functional currency exchange rate exposures and functional currency/reporting currency exchange rate exposures. For example, assume a French division of a registrant presenting its financial statements in U.S. dollars ($US) invests in a deutschmark(DM)-denominated debt security. In these circumstances, the $US is the reporting currency and the DM is the transactional currency. In addition, assume this division determines that the French franc (FF) is its functional currency according to FAS 52. In preparing the foreign currency value at risk disclosures, this registrant should report the aggregate potential loss from hypothetical changes in both the DM/FF exchange rate exposure and the FF/$US exchange rate exposure; and

E. Model, assumptions, and parameters that should be described include, but are not limited to, how *loss* is defined by the model (*e.g.*, loss in earnings, fair values, or cash flows), the type of model used (*e.g.*, variance/covariance, historical simulation, or Monte Carlo simulation and a description as to how optionality is addressed by the model), the types of instruments covered by the model (*e.g.*, derivative financial instruments, other financial instruments, derivative commodity instruments, and whether other instruments are included voluntarily, such as certain commodity instruments and positions, cash flows from anticipated transactions, and certain financial instruments excluded under instruction 3.C.ii. of the General Instructions to Items 9A(a) and 9A(b)), and other relevant information about the model's assumptions and parameters, (*e.g.*, holding periods, confidence intervals, and, when appropriate, the methods used for aggregating value at risk amounts across market risk exposure categories, such as by assuming perfect positive correlation, independence, or actual observed correlation).

5. Under Item 9A(a)(2), limitations that should be considered include, but are not limited to:

A. The exclusion of certain market risk sensitive instruments, positions, and transactions from the disclosures required under Item 9A(a)(1) (*e.g.*, derivative commodity instruments not permitted by contract or business custom to be settled in cash or with another financial instrument, commodity positions, cash flows from anticipated transactions, and certain financial instruments excluded under instruction 3.C.ii. of the General Instructions to Items 9A(a) and 9A(b)). Failure to include such instruments, positions, and transactions in preparing the disclosures under Item 9A(a)(1) may be a limitation because the resulting disclosures may not fully reflect the net market risk of a registrant; and

B. The ability of disclosures required under Item 9A(a)(1) to reflect fully the market risk that may be inherent in instruments with leverage, option, or prepayment features (*e.g.*, options, including written options, structured notes, collateralized mortgage obligations, leveraged swaps, and options embedded in swaps).

(b) *Qualitative information about market risk*. (1) To the extent material, describe:

(i) The registrant's primary market risk exposures;

(ii) How those exposures are managed. Such descriptions shall include, but not be limited to, a discussion of the objectives, general strategies, and instruments, if any, used to manage those exposures; and

(iii) Changes in either the registrant's primary market risk exposures or how those exposures are managed, when compared to what was in effect during the most recently completed fiscal year and what is known or expected to be in effect in future reporting periods.

(2) Qualitative information about market risk shall be presented separately for market risk sensitive instruments entered into for trading purposes and those entered into for purposes other than trading.

Instructions to Item 9A(b)

1. For purposes of disclosure under Item 9A(b), *primary market risk exposures* means:

A. The following categories of market risk: Interest rate risk, foreign currency exchange rate risk, commodity price risk, and other relevant market rate or price risks (*e.g.,* equity price risk); and

B. Within each of these categories, the particular markets that present the primary risk of loss to the registrant. For example, if a registrant has a material exposure to foreign currency exchange rate risk and, within this category of market risk, is most vulnerable to changes in dollar/yen, dollar/pound, and dollar/peso exchange rates, the registrant should disclose those exposures. Similarly, if a registrant has a material exposure to interest rate risk and, within this category of market risk, is most vulnerable to changes in short-term U.S. prime interest rates, it should disclose the existence of that exposure.

2. For purposes of disclosure under Item 9A(b), registrants should describe primary market risk exposures that exist as of the end of the latest fiscal year, and how those exposures are managed.

General Instructions to Items 9A(a) and 9A(b)

1. The disclosures called for by Items 9A(a) and 9A(b) are intended to clarify the registrant's exposures to market risk associated with activities in derivative financial instruments, other financial instruments, and derivative commodity instruments.

2. In preparing the disclosures under Items 9A(a) and 9A(b), registrants are required to include derivative financial instruments, other financial instruments, and derivative commodity instruments.

3. For purposes of Items 9A(a) and 9A(b), derivative financial instruments, other financial instruments, and derivative commodity instruments (collectively referred to as ''market risk sensitive instruments'') are defined as follows:

A. *Derivative financial instruments* has the same meaning as defined by generally accepted accounting principles (see, *e.g.,* FASB, *Statement of Financial Accounting Standards No. 119, ''Disclosure about Derivative Financial Instruments and Fair Value of Financial Instruments,''* (''FAS 119'') paragraphs 5–7 (October 1994)), and includes futures, forwards, swaps, options, and other financial instruments with similar characteristics;

B. *Other financial instruments* means all financial instruments as defined by generally accepted accounting principles for which fair value disclosures are required (*see, e.g.,* FASB, *Statement of Financial Accounting Standards No. 107, ''Disclosures about Fair Value of Financial Instruments,''* (''FAS 107'') paragraphs 3 and 8 (December 1991)), except for derivative financial instruments, as defined above;

C.i. Other financial instruments include, but are not limited to, trade accounts receivable, investments, loans, structured notes, mortgage-backed securities, trade accounts payable, indexed debt instruments, interest-only and principal-only obligations, deposits, and other debt obligations;

ii. Other financial instruments exclude employers' and plans' obligations for pension and other post-retirement benefits, substantively extinguished debt, insurance contracts, lease contracts, warranty obligations and rights, unconditional purchase obligations, investments accounted for under the equity method, minority interests in consolidated enterprises, and equity instruments issued by the registrant and classified in stockholders' equity in the statement of financial position (see, *e.g.,* FAS 107, paragraph 8 (December 1991)). For purposes of this item, trade accounts receivable and trade accounts payable need not be considered other financial instruments when their carrying amounts approximate fair value; and

D. *Derivative commodity instruments* include, to the extent such instruments are not derivative financial instruments, commodity futures, commodity forwards, commodity swaps, commodity options, and other commodity instruments with similar characteristics that are permitted by contract or business custom to be settled in cash or with another financial instrument. For purposes of this paragraph, settlement in cash includes settlement in cash of the net change in value of the derivative commodity instrument (*e.g.,* net cash settlement based on changes in the price of the underlying commodity).

4.A. In addition to providing required disclosures for the market risk sensitive instruments defined in instruction 2. of the General Instructions to Items 9A(a) and 9A(b), registrants are encouraged to include other market risk sensitive instruments, positions, and transactions within the disclosures required under Items 9A(a) and 9A(b). Such instruments, positions, and transactions might include commodity positions, derivative commodity instruments that are not permitted by contract or business custom to be settled in cash or with another financial instrument, cash flows from anticipated transactions, and certain financial instruments excluded under instruction 3.C.ii. of the General Instructions to Items 9A(a) and 9A(b).

B. Registrants that voluntarily include other market risk sensitive instruments, positions and transactions within their quantitative disclosures about market risk under the sensitivity analysis or value at risk disclosure alternatives are not required to provide separate market risk disclosures for any voluntarily selected instruments, positions, or transactions. Instead, registrants selecting the sensitivity analysis and value at risk disclosure alternatives are permitted to present comprehensive market risk disclosures, which reflect the combined market risk exposures inherent in both the required and any voluntarily selected instruments, position, or transactions. Registrants that choose the tabular presentation disclosure alternative should present voluntarily selected instruments, positions, or transactions in a manner consistent with the requirements in Item 9A(a) for market risk sensitive instruments.

C. If a registrant elects to include voluntarily a particular type of instrument, position, or transaction in their quantitative disclosures about market risk, that registrant should include all, rather than some, of those instruments, positions, or transactions within those disclosures. For example, if a registrant holds in inventory a particular type of commodity position and elects to include that commodity position within their market risk disclosures, the registrant should include the entire commodity position, rather than only a portion thereof, in their quantitative disclosures about market risk.

5.A. Under Items 9A(a) and 9A(b), a materiality assessment should be made for each market risk exposure category within the trading and other than trading portfolios.

B. For purposes of making the materiality assessment under instruction 5.A. of the General Instructions to Items 9A(a) and 9A(b), registrants should evaluate both:

i. The materiality of the fair values of derivative financial instruments, other financial instruments, and derivative commodity instruments outstanding as of the end of the latest fiscal year; and

ii. The materiality of potential, near-term losses in future earnings, fair values, and cash flows from reasonably possible near-term changes in market rates or prices.

iii. If either paragraphs B.i. or B.ii. in this instruction of the General Instructions to Items 9A(a) and 9A(b) are material, the registrant should disclose quantitative and qualitative information about market risk, if such market risk for the particular market risk exposure category is material.

C. For purposes of instruction 5.B.i. of the General Instructions to Items 9A(a) and 9A(b), registrants generally should not net fair values, except to the extent allowed under generally accepted accounting principles (see, *e.g., FASB Interpretation No. 39, ''Offsetting of Amounts Related to Certain Contracts''* (March 1992)). For example, under this instruction, the fair value of assets generally should not be netted with the fair value of liabilities.

D. For purposes of instruction 5.B.ii. of the General Instructions to Items 9A(a) and 9A(b), registrants should consider, among other things, the magnitude of:

i. Past market movements;

ii. Reasonably possible, near-term market movements; and

iii. Potential losses that may arise from leverage, option, and multiplier features.

E. For purposes of instructions 5.B.ii. and 5.D.ii. of the General Instructions to Items 9A(a) and 9A(b), the term *near term* means a period of time going forward up to one year from the date of the financial statements (see generally SOP 94–6, at paragraph 7 (December 30, 1994)).

F. For the purpose of instructions 5.B.ii. and 5.D.ii. of the General Instructions to Items 9A(a) and 9A(b), the term reasonably possible has the same meaning as defined by generally accepted accounting principles (see, *e.g.*, FAS 5, paragraph 3 (March 1975)).

6. For purposes of Items 9A(a) and 9A(b), registrants should present the information outside of, and not incorporate the information into, the financial statements (including the footnotes to the financial statements). In addition, registrants are encouraged to provide the required information in one location. However, alternative presentation, such as inclusion of all or part of the information in Management's Discussion and Analysis, may be used at the discretion of the registrant. If information is disclosed in more than one location, registrants should provide cross-references to the locations of the related disclosures.

7. For purposes of the instructions to Items 9A(a) and 9A(b), *trading purposes* has the same meaning as defined by generally accepted accounting principles (see, e.g., FAS 119, paragraph 9a (October 1994)). In addition, anticipated transactions means transactions (other than transactions involving existing assets or liabilities or transactions necessitated by existing firm commitments) an enterprise expects, but is not obligated, to carry out in the normal course of business (see, *e.g.,* FASB, *Statement of Financial Accounting Standards No. 80, ''Accounting for Futures Contracts,''* paragraph 9, (August 1984)).

(c) *Interim periods.* If interim period financial statements are included or are required to be included by Article 3 of Regulation S–X (17 CFR 210), discussion and analysis shall be provided so as to enable the reader to assess the sources and effects of material changes in information that would be provided under Item 9A of Form 20–F from the end of the preceding fiscal year to the date of the most recent interim balance sheet.

Instructions to Item 9A(c)

1. Information required by paragraph (c) of this Item 9A is not required until after the first fiscal year end in which this Item 9A is applicable.

(d) *Safe Harbor.* (1) The safe harbor provided in Section 27A of the Securities Act of 1933 (15 U.S.C. 77z-2) and Section 21E of the Securities Exchange Act of 1934 (15 U.S.C. 78u-5) (''statutory safe harbors'') shall apply, with respect to all types of issuers and transactions, to information provided pursuant to paragraphs (a), (b), and (c) of this Item 9A, provided that the disclosure is made by an issuer; a person acting on behalf of the issuer; an outside reviewer retained by the issuer making a statement on behalf of the issuer; or an underwriter, with respect to information provided by the issuer or information derived from information provided by the issuer.

(2) For purposes of this paragraph (d) of this Item 9A only:

(i) All information required by paragraphs (a), (b)(1)(i), (b)(1)(iii), and (c) of this Item 9A is considered *forward looking statements* for purposes of the statutory safe harbors, except for historical facts such as the terms of particular contracts and the number of market risk sensitive instruments held during or at the end of the reporting period; and

(ii) With respect to paragraph (a) of this Item 9A, the *meaningful cautionary statements* prong of the statutory safe harbors will be satisfied if a registrant satisfies all requirements of that same paragraph (a) of this Item 9A.

(e) *Small business issuers.* Small business issuers, as defined in § 230.405 of this chapter and § 240.12b-2 of this chapter, need not provide the information required by this Item 9A, whether or not they file on forms specially designated as small business issuer forms.

General Instructions to Items 9A(a), 9A(b), 9A(c), 9A(d), and 9A(e)

1. Bank registrants, thrift registrants, and non-bank and non-thrift registrants with market capitalizations on January 28, 1997 in excess of $2.5 billion should provide Item 9A disclosures in filings with the Commission that include annual financial statements for fiscal years ending after June 15, 1997. Non-bank and non-thrift registrants with market capitalizations on January 28, 1997 of $2.5 billion or less should provide Item 9A disclosures in filings with the Commission that include annual financial statements for fiscal years ending after June 15, 1998.

2.A. For purposes of instruction 1. of the General Instructions to Items 9A(a), 9A(b), 9A(c), 9A(d), and 9A(e), *bank registrants and thrift registrants* include any registrant which has control over a depository institution.

B. For purposes of instruction 2.A. of the General Instructions to Items 9A(a), 9A(b), 9A(c), 9A(d), and 9A(e), a registrant has control over a depository institution if:

i. The registrant directly or indirectly or acting through one or more other persons owns, controls, or has power to vote 25% or more of any class of voting securities of the depository institution;

ii. The registrant controls in any manner the election of a majority of the directors or trustees of the depository institution; or

ii. The Federal Reserve Board or Office of Thrift Supervision determines, after notice and opportunity for hearing, that the registrant directly or indirectly exercises a controlling influence over the management or policies of the depository institution;

C. For purposes of instruction 2.B. of the General Instructions to Items 9A(a), 9A(b), 9A(c), 9A(d), and 9A(e), a depository institution means any of the following:

i. An insured depository institution as defined in section 3(c)(2) of the Federal Deposit Insurance Act (12 U.S.C.A. Sec. 1813 (c));

ii. An institution organized under the laws of the United States, any State of the United States, the District of Columbia, any territory of the United States, Puerto Rico, Guam, American Somoa, or the Virgin Islands, which both accepts demand deposits or deposits that the depositor may withdraw by check or similar means for payment to third parties or others and is engaged in the business of making commercial loans.

D. For purposes of instruction 1. of the General Instructions to Items 9A(a), 9A(b), 9A(c), 9A(d), and 9A(e), *market capitalization* is the aggregate market value of common equity as set forth in General Instruction I.B.1. of Form S–3; provided however, that common equity held by affiliates is included in the calculation of market capitalization; and provided further that instead of using the 60 day period prior to filing referenced in General Instruction I.B.1. of Form S–3, the measurement date is January 28, 1997.

Appendix to Item 9A—Tabular Disclosures

The tables set forth below are illustrative of the format that might be used when a registrant elects to present the information required by paragraph (a)(1)(i)(A) of Item 9A regarding terms and information about derivative financial instruments, other financial instruments, and derivative commodity instruments. These examples are for illustrative purposes only. Registrants are not required to display the information in the specific format illustrated below. Alternative methods of display are permissible as long as the disclosure requirements of the section are satisfied. Furthermore, these examples were designed primarily to illustrate possible formats for presentation of the information required by the disclosure item and do not purport to illustrate the broad range of derivative financial instruments, other financial instruments, and derivative commodity instruments utilized by registrants.

Interest Rate Sensitivity

The table below provides information about the Company's derivative financial instruments and other financial instruments that are sensitive to changes in interest rates, including interest rate swaps and debt obligations. For debt obligations, the table presents principal cash flows and related weighted average interest rates by expected maturity dates. For interest rate swaps, the table presents notional amounts and weighted average interest rates by expected (contractual) maturity dates. Notional amounts are used to calculate the contractual payments to be exchanged under the contract. Weighted average variable rates are based on implied forward rates in the yield curve at the reporting date. The information is presented in U.S. dollar equivalents, which is the Company's reporting currency. The instrument's actual cash flows are denominated in both U.S. dollars ($US) and German deutschmarks (DM), as indicated in parentheses.

December 31, 19X1

	Expected maturity date							
	19X2	19X3	19X4	19X5	19X6	There-after	Total	Fair value
Liabilities	(US$ Equivalent in millions)							
Long-term Debt:								
Fixed Rate ($US)	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX
Average interest rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Fixed Rate (DM)	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX
Average interest rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Variable Rate ($US)	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX
Average interest rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Interest Rate Derivatives	(In millions)							
Interest Rate Swaps:								
Variable to Fixed ($US)	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX
Average pay rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Average receive rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Fixed to Variable ($US)	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX
Average pay rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Average receive rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	

Exchange Rate Sensitivity

The table below provides information about the Company's derivative financial instruments, other financial instruments, and firmly committed sales transactions by functional currency and presents such information in U.S. dollar equivalents.[1] The table summarizes information on instruments and transactions that are sensitive to foreign currency exchange rates, including foreign currency forward exchange agreements, deutschmark (DM)-denominated debt obligations, and firmly committed DM sales transactions. For debt obligations, the table presents principal cash flows and related weighted average interest rates by expected maturity dates. For firmly committed DM-sales transactions, sales amounts are presented by the expected transaction date, which are not expected to exceed two years. For foreign currency forward exchange agreements, the table presents the notional amounts and weighted average exchange rates by expected (contractual) maturity dates. These notional amounts generally are used to calculate the contractual payments to be exchanged under the contract.

[1] The information is presented in U.S. dollars because that is the registrant's reporting currency.

December 31, 19X1

	Expected maturity date							
	19X2	19X3	19X4	19X5	19X6	There-after	Total	Fair value
On-Balance Sheet Financial Instruments	(US$ Equivalent in millions)							
$US Functional Currency [2]:								
Liabilities.								
Long-Term Debt:.								
Fixed Rate (DM)	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX	$XXX
Average interest rate	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	X.X%	
Anticipated Transactions and Related Derivatives [3]	Expected maturity or transaction date (US$ Equivalent in millions)							
$US Functional Currency:								
Firmly committed Sales Contracts (DM)	$XXX	$XXX	....	....	....	....	$XXX	$XXX
Forward Exchange Agreements (Receive $US/Pay DM):								
Contract Amount	XXX	XXX	....	....	....	....	XXX	XXX
Average Contractual Exchange Rate	X.X%	X.X%	....	....	....	....	X.X%	....

[2] Similar tabular information would be provided for other functional currencies.
[3] Pursuant to General Instruction 4. to Items 9A(a) and 9A(b) of Form 20–F, registrants may include cash flows from anticipated transactions and operating cash flows resulting from non-financial and non-commodity instruments.

Commodity Price Sensitivity

The table below provides information about the Company's corn inventory and futures contracts that are sensitive to changes in commodity prices, specifically corn prices. For inventory, the table presents the carrying amount and fair value at December 31, 19x1. For the futures contracts the table presents the notional amounts in bushels, the weighted average contract prices, and the total dollar contract amount by expected maturity dates, the latest of which occurs one year from the reporting date. Contract amounts are used to calculate the contractual payments and quantity of corn to be exchanged under the futures contracts.

December 31, 19X1

	Carrying amount	Fair value
On Balance Sheet Commodity Position and Related Derivatives	(In millions)	
Corn Inventory [4]	$XXX	$XXX
	Expected maturity 1992	Fair value
Related Derivatives		
Futures Contracts (Short):		
Contract Volumes (100,000 bushels)	XXX	....
Weighted Average Price (Per 100,000 bushels)	$X.XX	....
Contract Amount ($US in millions)	$XXX	$XXX

[4] Pursuant to General Instruction 4. to Items 305(a) and 305(b) of Regulation S-K, registrants may include information on commodity positions, such as corn inventory.

20. By amending Form 10–Q (referenced in § 249.308a) by removing references to ''Items 1 and 2 of Part I of this form'' and adding in their place references to ''Items 1, 2, and 3 of Part I of this form'' in paragraphs 1 and 2 of General Instruction F, adding paragraph 2.c. to General Instruction H and Item 3 to Part I to read as follows:

Note—The text of Form 10–Q does not, and this amendment will not, appear in the Code of Federal Regulations.

Form 10–Q—Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934; or Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

* * * * *

General Instructions

* * * * *

H. Omission of Information by Certain Wholly-Owned Subsidiaries

* * * * *

2. * * * c. Such registrants may omit the information called for by Item 3 of Part I, Quantitative and Qualitative Disclosures About Market Risk.

* * * * *

Part I—Financial Information

* * * * *

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Furnish the information required by Item 305 of Regulation S-K (§ 229.305 of this chapter).

* * * * *

21. By amending Form 10–K (referenced in § 249.310) by adding Item 7A to be inserted after Item 7 and before Item 8 in Part II to read as follows:

Note—The text of Form 10–K does not, and this amendment will not, appear in the Code of Federal Regulations.

Form 10–K—Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934; or Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

* * * * *

Part II

* * * * *

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Furnish the information required by Item 305 of Regulation S-K (§ 229.305 of this chapter).

* * * * *

Dated: January 31, 1997.

By the Commission.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 97–2991 Filed 2–7–97; 8:45 am]

BILLING CODE 8010–01–P