

assets of the Acquired Fund will be transferred to the Acquiring Fund.

4. Each Fund's board of trustees ("Board"), including a majority of the trustees who are not "interested persons," as defined in section 2(a)(19) of the Act, approved the Reorganization and concluded that the Reorganization was in the best interest of the respective Fund. In approving the Reorganization, each Board considered the Wells Fargo Position. To effect the Reorganization, a shareholder meeting of the Acquired Fund's shareholders will be held on or about January 31, 2002. A proxy statement soliciting shareholder approval, which discussed the Wells Fargo Position, was mailed in November, 2001.

#### Applicants' Legal Analysis

1. Section 12(d)(3) of the Act, in relevant part, prohibits a registered investment company from purchasing or otherwise acquiring any security issued by any person who is a broker, dealer, investment adviser, or engaged in the business of underwriting. Rule 12d3-1 under the Act exempts certain transactions from the prohibitions of section 12(d)(3) if specified conditions are met. Rule 12d3-1(c) provides that the exemption provided by the rule is not available when the issuer of the securities is the investment company's investment adviser, promoter, or principal underwriter, or an affiliated person thereof.

2. Applicants state that because Wells Fargo is an affiliated person of WFFM, the Acquiring Fund's investment adviser, the Transfer and the Acquiring Fund's continued holding of the Wells Fargo Position would not meet the conditions of rule 12d3-1(c).<sup>1</sup> Applicants request relief from section 12(d)(3) to permit the Acquiring Fund to effect the Transfer and the continued holding for up to two years of the Wells Fargo Position following the Reorganization in order to permit the Acquiring Fund to effect its orderly liquidation.

3. Section 6(c) of the Act authorizes the SEC to exempt persons or transactions from the provisions of the Act to the extent that the exemption is necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policies and provisions of the Act. Applicants state that the requested relief meets this standard.

4. Applicants state that the relief is warranted because none of the abuses

that section 12(d)(3) was intended to prevent are present in the instant situation and the two-year disposition period will permit the Acquiring Fund to maximize the realization of gain on the orderly sale of the Wells Fargo Position while minimizing the tax effects of the disposition. Applicants also state that the Acquired Fund obtained the Wells Fargo Position in compliance with the Act and the rules thereunder.

#### Applicants' Condition

Applicants agree that any order granting the requested relief will be subject to the following condition:

Applicants will seek to liquidate the Wells Fargo Position as soon as possible, consistent with the maximization of shareholder return and the best interests of the Acquiring Fund, and in any case, within two years of the date of the Reorganization.

For the Commission, by the Division of Investment Management, under delegated authority.

**Margaret H. McFarland,**  
*Deputy Secretary.*

[FR Doc. 02-1900 Filed 1-24-02; 8:45 am]

**BILLING CODE 8010-01-P**

#### SECURITIES AND EXCHANGE COMMISSION

##### Sunshine Act Meeting

Notice is hereby given, pursuant to the provisions of the Government in the Sunshine Act, Pub. L. 94-409, that the Securities and Exchange Commission will hold the following meeting during the week of January 28, 2002: a closed meeting will be held on Tuesday, January 29, 2002, at 10 a.m.

Commissioners, Counsel to the Commissioners, the Secretary to the Commission, and recording secretaries will attend the closed meeting. Certain staff members who have an interest in the matters may also be present.

The General Counsel of the Commission, or his designee, has certified that, in his opinion, one or more of the exemptions set forth in 5 U.S.C. 552b(c)(3), (5), (7), (9)(B), and (10) and 17 CFR 200.402(a)(3), (5), (7), 9(ii) and (10), permit consideration of the scheduled matters at the closed meetings.

The subject matters of the closed meeting scheduled for Tuesday, January 22, 2002, will be:

Institution and settlement of injunctive actions;

Institution and settlement of administrative proceedings of an enforcement nature; and

Formal orders of investigation.

At times, changes in Commission priorities require alterations in the scheduling of meeting items. For further information and to ascertain what, if any, matters have been added, deleted or postponed, please contact:

The Office of the Secretary at (202) 942-7070.

Dated: January 22, 2002.

**Jill M. Peterson,**  
*Assistant Secretary.*

[FR Doc. 02-1987 Filed 1-23-02; 11:57 am]

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#### SECURITIES AND EXCHANGE COMMISSION

[Release Nos. 33-8056; 34-45321; FR-61]

##### Commission Statement About Management's Discussion and Analysis of Financial Condition and Results of Operations

**AGENCY:** Securities and Exchange Commission ("Commission").

**ACTION:** Commission statement.

**SUMMARY:** The Commission today is issuing a statement regarding Management's Discussion and Analysis of Financial Condition and Results of Operations. The release sets forth certain views of the Commission regarding disclosure that should be considered by registrants. Disclosure matters addressed by the release are liquidity and capital resources including off-balance sheet arrangements; certain trading activities that include non-exchange traded contracts accounted for at fair value; and effects of transactions with related and certain other parties.

**FOR FURTHER INFORMATION CONTACT:** Questions about this statement should be referred to Jackson Day or Robert Bayless, Office of the Chief Accountant (202 942-4400) or Paula Dubberly, Division of Corporation Finance (202 942-2900), Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-1103.

##### SUPPLEMENTARY INFORMATION:

##### I. Background

On December 31, 2001, the Commission received a petition from the accounting firms of Arthur Andersen LLP, Deloitte and Touche LLP, Ernst & Young LLP, KPMG LLP, and PricewaterhouseCoopers LLP.<sup>1</sup> The petition, which was endorsed by the

<sup>1</sup> See Investment Company Act Release No. 3542. (Sep. 21, 1962).

<sup>1</sup> The petition is posted on the Commission's web page ([www.sec.gov](http://www.sec.gov)) under Regulatory Actions, Petitions for Rulemaking.

American Institute of Certified Public Accountants, requested that the Commission issue additional interpretive guidance regarding Item 303 of Regulation S-K, *Management's Discussion and Analysis of Financial Condition and Results of Operations*,<sup>2</sup> Item 303 of Regulation S-B, *Management's Discussion and Analysis of Plan of Operations*,<sup>3</sup> and Item 5 of Form 20-F, *Operating and Financial Review and Prospects*<sup>4</sup> (collectively, "MD&A" or "the MD&A rules").<sup>5</sup> The petition requested that additional guidance be provided to public companies preparing their annual reports for the fiscal year just ended.

The petition identified three areas of concern regarding disclosure in MD&A:

- Liquidity and capital resources, including off-balance sheet arrangements;
- Certain trading activities involving non-exchange traded contracts accounted for at fair value; and
- Relationships and transactions with persons or entities that derive benefits from their non-independent relationship with the registrant or the registrant's related parties.

Generally, we believe that the quality of information provided by public companies in the three areas identified in the petition should be improved. Because many companies are currently preparing disclosures for fiscal 2001 annual reports, the Commission believes it is appropriate to issue this statement so that public companies can consider the petition and this statement in preparing year-end and interim financial reports and other disclosures made after the issuance of this release.

While the Commission intends to consider rulemaking regarding the topics addressed in this statement and other topics covered by MD&A, the purpose of this statement is to suggest steps that issuers should consider in meeting their current disclosure obligations with respect to the topics described. This statement does not create new legal requirements, nor does it modify existing legal requirements.

<sup>2</sup> 17 CFR 229.303.

<sup>3</sup> 17 CFR 228.303.

<sup>4</sup> See 17 CFR 249.220f.

<sup>5</sup> The accounting profession has made previous petitions to improve MD&A disclosure. See, e.g., Securities Act Release No. 6711 (April 17, 1987), Concept Release on Management's Discussion and Analysis of Financial Condition and Results of Operations, 52 FR 13715; and Securities Act Release No. 6835 (May 18, 1989), Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, 54 FR 22427.

## II. Regulation S-K. Item 303. Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A)

Paragraph (a) of Item 303 of Regulation S-K identifies a basic and overriding requirement of MD&A: to "provide such other information that the registrant believes to be necessary to an understanding of its financial condition, changes in financial condition and results of operations." The Commission has explained this requirement on a number of occasions. In 1987, we said:

The Commission has long recognized the need for a narrative explanation of the financial statements, because numerical presentations and brief accompanying footnotes alone may be insufficient for an investor to judge the quality of earnings and the likelihood that past performance is indicative of future performance. MD&A is intended to give the investor an opportunity to look at the company through the eyes of management by providing both a short and long-term analysis of the business of the company.<sup>6</sup>

And, as we said in 1989, "[t]he MD&A requirements are intended to provide in one section of a filing, material historical and prospective textual disclosure enabling investors and other users to assess the financial condition and results of operations of the registrant, with particular emphasis on the registrant's prospects for the future."<sup>7</sup>

Disclosure is mandatory where there is a known trend or uncertainty that is reasonably likely to have a material effect on the registrant's financial condition or results of operations.<sup>8</sup> Accordingly, the development of MD&A disclosure should begin with management's identification and evaluation of what information, including the potential effects of known trends, commitments, events, and uncertainties, is important to providing

<sup>6</sup> Securities Act Release No. 6711 (April 17, 1987), Concept Release on Management's Discussion and Analysis of Financial Condition and Results of Operations, 52 FR 13715.

<sup>7</sup> Securities Act Release No. 6835 (May 18, 1989), Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, 54 FR 22427, 22438 (footnote omitted).

<sup>8</sup> Securities Act Release No. 6835 (May 18, 1989), Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, 54 FR 22427, 22429 ("Required disclosure is based on currently known trends, events, and uncertainties that are reasonably expected to have material effects. \* \* \* In contrast, optional forward-looking disclosure involves anticipating a future trend or event or anticipating a less predictable impact of a known event, trend or uncertainty.").

investors and others an accurate understanding of the company's current and prospective financial position and operating results.<sup>9</sup>

Investors have become increasingly concerned about the sufficiency of disclosure regarding liquidity risk, market price risks, and effects of "off-balance sheet" transaction structures. Also, many readers of financial statements have cited a lack of transparent disclosure about transactions with unconsolidated entities and other parties where that information appeared necessary to understand how significant aspects of the business were conducted.

Accordingly, the Commission is reminding companies of the requirements of MD&A as they relate to (1) liquidity and capital resources, including off-balance sheet arrangements; (2) certain trading activities involving non-exchange traded contracts accounted for at fair value; and (3) relationships and transactions on terms that would not be available from clearly independent third parties on an arm's-length basis. This statement suggests steps that companies should consider in meeting their disclosure obligations.

We also want to remind registrants that disclosure must be both useful and understandable. That is, management should provide the most relevant information and provide it using language and formats that investors can be expected to understand. Registrants should be aware also that investors will often find information relating to a particular matter more meaningful if it is disclosed in a single location, rather than presented in a fragmented manner throughout the filing.

### A. Disclosures Concerning Liquidity and Capital Resources, Including "Off-Balance Sheet" Arrangements

Paragraphs (a)(1) and (a)(2)(ii) of Item 303 of Regulation S-K set forth certain requirements for disclosures about "Liquidity" and "Capital Resources."

(1) *Liquidity*. Identify any known trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way.

\* \* \* \* \*

(2)(ii) *Capital Resources*. Describe any known material trends, favorable or

<sup>9</sup> See Instructions to Item 303 ("The discussion and analysis shall focus specifically on material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition.").

unfavorable, in the registrant's capital resources. Indicate any expected material changes in the mix and relative cost of such resources. The discussion shall consider changes between equity, debt and any off-balance sheet financing arrangements.

A registrant's liquidity and capital resources are closely aligned. Disclosures about each are likely to be affected by many of the same facts and circumstances. And off-balance sheet financing arrangements often are integral to both.<sup>10</sup> Management should consider all of these items together, as well as individually, when drafting disclosures responsive to the MD&A rules.

### 1. Liquidity Disclosures

MD&A disclosures should not be overly general. For example, disclosure that the registrant has sufficient short-term funding to meet its liquidity needs for the next year provides little useful information. Instead, registrants should consider describing the sources of short-term funding and the circumstances that are reasonably likely to affect those sources of liquidity.

For example, a registrant that identifies its principal source of liquidity as operating cash flows may need also to disclose the extent of the risk that a decrease in demand for the company's products would reduce the availability of funds. That risk might arise, to further the example, where customer demand is reasonably likely to fluctuate in response to rapid technological changes. Similarly, if commercial paper is a principal source of liquidity, the registrant should consider the need to disclose how this facility could be adversely affected by a debt rating downgrade or deterioration in certain of the company's financial ratios or other measures of financial performance. The discussion should be limited to material risks, and, as with MD&A generally, should be sufficiently detailed and tailored to the company's individual circumstances, rather than "boilerplate."

If the registrant's liquidity is dependent on the use of off-balance sheet financing arrangements, such as securitization of receivables or obtaining access to assets through special purpose entities, the registrant should consider disclosure of the factors that are reasonably likely to affect its ability to continue using those off-balance sheet

financing arrangements.<sup>11</sup> Registrants also should make informative disclosures about matters that could affect the extent of funds required within management's short- and long-term planning horizons.

Registrants are reminded that identification of circumstances that could materially affect liquidity is necessary if they are "reasonably likely" to occur. This disclosure threshold is lower than "more likely than not." Market price changes, economic downturns, defaults on guarantees, or contractions of operations that have material consequences for the registrant's financial position or operating results can be reasonably likely to occur under some conditions. Material effects on liquidity as a result of any reasonably likely changes should be disclosed pursuant to Item 303(a).

In 1989, the Commission identified two assessments management must make where a trend, demand, commitment, event or uncertainty is known:

1. Is the known trend, demand, commitment, event or uncertainty likely to come to fruition? If management determines that it is not reasonably likely to occur, no disclosure is required.

2. If management cannot make that determination, it must evaluate objectively the consequences of the known trend, demand, commitment, event or uncertainty, on the assumption that it will come to fruition. Disclosure is then required unless management determines that a material effect on the registrant's financial condition or results of operations is not reasonably likely to occur.<sup>12</sup>

The Commission further reminded registrants that each final determination resulting from the assessments made by management must be objectively reasonable, as viewed at the time the determination is made.<sup>13</sup>

To identify trends, demands, commitments, events and uncertainties that require disclosure, management should consider the following:

- Provisions in financial guarantees or commitments, debt or lease agreements or other arrangements that

could trigger a requirement for an early payment, additional collateral support, changes in terms, acceleration of maturity, or the creation of an additional financial obligation, such as adverse changes in the registrant's credit rating, financial ratios, earnings, cash flows, or stock price, or changes in the value of underlying, linked or indexed assets;

- Circumstances that could impair the registrant's ability to continue to engage in transactions that have been integral to historical operations or are financially or operationally essential, or that could render that activity commercially impracticable, such as the inability to maintain a specified investment grade credit rating, level of earnings, earnings per share, financial ratios, or collateral;

- Factors specific to the registrant and its markets that the registrant expects to be given significant weight in the determination of the registrant's credit rating or will otherwise affect the registrant's ability to raise short-term and long-term financing;

- Guarantees of debt or other commitments to third parties; and
- Written options on non-financial assets (for example, real estate puts).

### 2. Off-Balance Sheet Arrangements

Registrants should consider the need to provide disclosures concerning transactions, arrangements and other relationships with unconsolidated entities or other persons that are reasonably likely to affect materially liquidity or the availability of or requirements for capital resources. Specific disclosure may be necessary regarding relationships with unconsolidated entities that are contractually limited to narrow activities that facilitate the registrant's transfer of or access to assets. These entities are often referred to as structured finance or special purpose entities. These entities may be in the form of corporations, partnerships or limited liability companies, or trusts.

Material sources of liquidity and financing, including off-balance sheet arrangements and transactions with unconsolidated, limited purpose entities, should be discussed pursuant to Item 303(a).<sup>14</sup> The extent of the registrant's reliance on off-balance sheet arrangements should be described fully and clearly where those entities provide financing, liquidity, or market or credit risk support for the registrant; engage in

<sup>10</sup> See Securities Act Release No. 6835 (May 18, 1989), Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, 54 FR 22427, particularly Section III.C.

<sup>11</sup> "The scope of the discussion should thus address liquidity in the broadest sense, encompassing internal as well as external sources, current conditions as well as future commitments and known trends, changes in circumstances and uncertainties." [Securities Act Release No. 6349 (September 28, 1981)].

<sup>12</sup> Securities Act Release No. 6835 (May 18, 1989), Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, 54 FR 22427, 22430.

<sup>13</sup> *Id.*

<sup>14</sup> Securities Act Release No. 6835 (May 18, 1989), Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, 54 FR 22427, at III.C.

leasing, hedging, research and development services with the registrant; or expose the registrant to liability that is not reflected on the face of the financial statements. Where contingencies inherent in the arrangements are reasonably likely to affect the continued availability of a material historical source of liquidity and finance, registrants must disclose those uncertainties and their effects.

Registrants should consider the need to include information about the off-balance sheet arrangements such as: their business purposes and activities; their economic substance; the key terms and conditions of any commitments; the initial and ongoing relationships with the registrant and its affiliates; and the registrant's potential risk exposures resulting from its contractual or other commitments involving the off-balance sheet arrangements.

For example, a registrant may be economically or legally required or reasonably likely to fund losses of an unconsolidated, limited purpose entity, provide it with additional funding, issue securities pursuant to a call option held by that entity, purchase the entity's capital stock or assets, or the registrant otherwise may be financially affected by the performance or non-performance of an entity or counterparty to a transaction or arrangement. In those circumstances, the registrant may need to include information about the arrangements and exposures resulting from contractual or other commitments to provide investors with a clear understanding of the registrant's business activities, financial arrangements, and financial statements. Other disclosures that registrants should consider to explain the effects and risks of off-balance sheet arrangements include:

- Total amount of assets and obligations of the off-balance sheet entity, with a description of the nature of its assets and obligations, and identification of the class and amount of any debt or equity securities issued by the registrant;
  - The effects of the entity's termination if it has a finite life or it is reasonably likely that the registrant's arrangements with the entity may be discontinued in the foreseeable future;
  - Amounts receivable or payable, and revenues, expenses and cash flows resulting from the arrangements;
  - Extended payment terms of receivables, loans, and debt securities resulting from the arrangements, and any uncertainties as to realization, including repayment that is contingent upon the future operations or performance of any party;
  - The amounts and key terms and conditions of purchase and sale agreements between the registrant and the counterparties in any such arrangements; and
  - The amounts of any guarantees, lines of credit, standby letters of credit or commitments or take or pay contracts, throughput contracts or other similar types of arrangements, including tolling, capacity, or leasing arrangements, that could require the registrant to provide funding of any obligations under the arrangements, including guarantees of repayment of obligors of parties to the arrangements, make whole agreements, or value guarantees.
- Although disclosure regarding similar arrangements can be aggregated, important distinctions in terms and effects should not be lost in that process. The relative significance to the registrant's financial position and results of the arrangements with unconsolidated, non-independent,

limited purpose entities should be clear from the disclosures to the extent material. While legal opinions regarding "true sale" issues or other issues relating to whether a registrant has contingent, residual or other liability can play an important role in transactions involving such entities, they do not obviate the need for the registrant to consider whether disclosure is required. In addition, disclosure of these matters should be clear and individually tailored to describe the risks to the registrant, and should not consist merely of recitation of the transactions' legal terms or the relationships between the parties or similar boilerplate.

### 3. Disclosures About Contractual Obligations and Commercial Commitments

Accounting standards<sup>15</sup> require disclosure concerning a registrant's obligations and commitments to make future payments under contracts, such as debt and lease agreements, and under contingent commitments, such as debt guarantees. Disclosures responsive to these requirements usually are located in various parts of a registrant's filings. We believe investors would find it beneficial if aggregated information about contractual obligations and commercial commitments<sup>16</sup> were provided in a single location so that a total picture of obligations would be readily available. One aid to presenting the total picture of a registrant's liquidity and capital resources and the integral role of on- and off-balance sheet arrangements may be schedules of contractual obligations and commercial commitments as of the latest balance sheet date. Examples that could be adapted to the registrant's particular facts are presented below.

Contractual obligations	Payments due by period				
	Total	Less than 1 year	1-3 years	4-5 years	After 5 years
Long-Term Debt					
Capital Lease Obligations					
Operating Leases					
Unconditional Purchase Obligations					
Other Long-Term Obligations					
Total Contractual Cash Obligations					

The preceding table could be accompanied by footnotes to describe provisions that create, increase or accelerate liabilities, or other pertinent data.

<sup>15</sup> See, e.g., Statement of Financial Accounting Standards Nos. 5, *Accounting for Contingencies*, 13, *Accounting for Leases*, 47, *Disclosure of Long-Term*

*Obligations*, and 129, *Disclosure of Information about Capital Structure*."

<sup>16</sup> Commercial commitments are intended to include lines of credit, guarantees, and other

potential cash outflows resulting from a contingent event that requires registrant performance pursuant to a funding commitment.

Other commercial commitments	Total amounts committed	Amount of commitment expiration per period			
		Less than 1 year	1-3 years	4-5 years	Over 5 years
Lines of Credit					
Standby Letters of Credit					
Guarantees					
Standby Repurchase Obligations					
Other Commercial Commitments					
Total Commercial Commitments					

*B. Disclosures About Certain Trading Activities That Include Non-Exchange Traded Contracts Accounted for at Fair Value*

The Commission is concerned that there may be a lack of transparency and clarity with respect to the disclosure of trading activities involving commodity contracts that are accounted for at fair value but for which a lack of market price quotations necessitates the use of fair value estimation techniques. These contracts may be indexed to measures of weather, commodities prices, or quoted prices of service capacity, such as energy storage and bandwidth capacity contracts. Companies engaged to a material extent in trading activities<sup>17</sup> involving these contracts should consider providing disclosures in MD&A that supplement those required in the financial statements by applicable accounting standards. Investor understanding and financial reporting transparency may depend on additional statistical and other information about these business activities and transactions. That information should include any contracts that are derivatives involving the same commodities that are part of those trading activities (for example, energy derivatives that are part of energy trading activities<sup>18</sup>).

The Commission reminds registrants that accounting standards require disclosures in financial statements of material energy trading and risk management activities.<sup>19</sup> Discussion in MD&A of material trends and uncertainties arising from those activities is also required. Information about these trading activities, contracts and modeling methodologies, assumptions, variables and inputs, along with explanations of the different outcomes reasonably likely under different circumstances or measurement methods, should be considered for inclusion in management's discussion of how the activities affect reported results for the latest annual period and subsequent interim period and how financial position is affected as of the latest balance sheet date. The Commission recently issued cautionary advice encouraging companies to include in their MD&A full explanations, in plain English, of their "critical accounting policies," the judgments and uncertainties affecting the application of those policies, and the likelihood that materially different amounts would be reported under different conditions or using different assumptions.<sup>20</sup>

Consistent with that advice, registrants should consider the need to

furnish information, quantified to the extent practicable, that does the following:

- Disaggregates realized and unrealized changes in fair value;
- Identifies changes in fair value attributable to changes in valuation techniques;
- Disaggregates estimated fair values at the latest balance sheet date based on whether fair values are determined directly from quoted market prices or are estimated; and
- Indicates the maturities of contracts at the latest balance sheet date (e.g., within one year, within years one through three, within years four and five, and after five years).

An example of this disclosure in the form of a schedule is provided below.

Fair value of contracts outstanding at the beginning of the period—xxxxxx
Contracts realized or otherwise settled during the period—xxxxxx
Fair value of new contracts when entered into during the period—xxxxxx
Changes in fair values attributable to changes in valuation techniques and assumptions—xxxxxx
Other changes in fair values—xxxxxx
Fair value of contracts outstanding at the end of the period—xxxxxx

Source of fair value	Fair value of contracts at period-end				Total fair value
	Maturity less than 1 year	Maturity 1-3 years	Maturity 4-5 years	Maturity in excess of 5 years	
Prices actively quoted.					
Prices provided by other external sources.					
Prices based on models and other valuation methods.					

<sup>17</sup> Companies that may find the suggested disclosures particularly valuable are those engaged to a material extent in (a) energy trading activities as defined in Emerging Issues Task Force Issue 98-10 (EITF 98-10), *Accounting for Contracts Involved in Energy Trading and Risk Management Activities*, (b) weather trading activities as defined in Emerging Issues Task Force Issue No. 99-2, *Accounting for Weather Derivatives*, or (c) non-exchange traded commodity trading contracts that are marked to fair

value through earnings and are part of analogous trading activities (for example, nonderivative trading contracts on pulp, bandwidth, newsprint, and so on).

<sup>18</sup> Emerging Issues Task Force No. 98-10 (September 23, 1999) identifies factors that distinguish energy trading activities from other activities that involve the purchase or sale of energy.

<sup>19</sup> Emerging Issues Task Force Issue 98-10 (September 23, 1999), *Accounting for Contracts Involved in Energy Trading and Risk Management Activities*.

<sup>20</sup> Financial Reporting Release No. 60, *Cautionary Advice Regarding Disclosure About Critical Accounting Policies* (December 12, 2001) 66 FR 65013.

In addition, issuers should consider the need to disclose the fair value of net claims against counterparties that are reported as assets at the most recent balance sheet date, based on the credit quality of the contract counterparty (e.g., investment grade; noninvestment grade; and no external ratings).

Registrants should also consider their disclosure obligations regarding risk management in connection with the trading activities discussed above. Registrants should consider whether they should provide fuller disclosure regarding the management of risks related to, for example, changes in credit quality or market fluctuations of underlying, linked or indexed assets or liabilities, especially where such assets are illiquid or susceptible to material uncertainties in valuation.

### C. Disclosures About Effects of Transactions With Related and Certain Other Parties

Statement of Financial Accounting Standards No. 57 (FAS 57), *Related Party Disclosures*, sets forth the requirements under GAAP concerning transactions with related parties.<sup>21</sup> As noted in that standard, “[t]ransactions involving related parties cannot be presumed to be carried out on an arm’s length basis, as the requisite conditions of competitive, free-market dealings may not exist.”<sup>22</sup> Accordingly, where related party transactions are material, MD&A should include discussion of those transactions to the extent necessary for an understanding of the company’s current and prospective financial position and operating results. In addition, Item 404 of Regulation S–K and Item 404 of Regulation S–B require disclosure of certain relationships and transactions with related parties.<sup>23</sup>

<sup>21</sup> Statement of Financial Accounting Standard No. 57, *Related Party Disclosures* (March 1982). See also 17 CFR 210.4–08(k)(1), which states, “Related party transactions should be identified and the amounts stated on the face of the balance sheet, income statement, or statement of cash flows.”

<sup>22</sup> *Id.*, paragraph 3.

<sup>23</sup> 17 CFR 229.404 and 17 CFR 228.404, which require, with certain exceptions, disclosure of transactions or series of transactions in which the company was, or is to be, a party, the amount involved exceeds \$60,000, and a director, executive officer, nominee for election as director, security holder of more than five percent of any class of the company’s voting securities, or any member of the immediate family of any of such persons, had or will have a direct or indirect material interest. Required disclosures include the name of the person and the person’s relationship with the registrant, the nature of the person’s interest, the amount of the transaction(s), and, where practicable, the amount of the person’s interest in the transaction(s). In addition, section 10A of the Securities Exchange Act of 1934, 15 U.S.C. 78j–1, requires that each audit of financial statements

Registrants should consider whether investors would better understand financial statements in many circumstances if MD&A included descriptions of all material transactions involving related persons or entities, with clear discussion of arrangements that may involve transaction terms or other aspects that differ from those which would likely be negotiated with clearly independent parties.<sup>24</sup> Registrants should consider describing the elements of the transactions that are necessary for an understanding of the transactions’ business purpose and economic substance, their effects on the financial statements, and the special risks or contingencies arising from these transactions. Discussion of the following may be necessary:

- The business purpose of the arrangement;
- Identification of the related parties transacting business with the registrant;
- How transaction prices were determined by the parties;
- If disclosures represent that transactions have been evaluated for fairness, a description of how the evaluation was made; and
- Any ongoing contractual or other commitments as a result of the arrangement.

Registrants should also consider the need for disclosure about parties that fall outside the definition of “related parties,” but with whom the registrant or its related parties have a relationship that enables the parties to negotiate terms of material transactions that may not be available from other, more clearly independent, parties on an arm’s-length basis. For example, an entity may be established and operated by individuals that were former senior management of, or have some other current or former relationship with, a registrant. The purpose of the entity may be to own assets used by the registrant or provide financing or services to the registrant. Although former management or persons with other relationships may not meet the definition of a related party

pursuant to that Act include procedures designed to identify related party transactions that are material to the financial statements or that require disclosure. Statement on Auditing Standards No. 45, *Related Parties*, published by the Auditing Standards Board and effective for periods ended after September 30, 1983, provides guidance on auditing related party transactions.

<sup>24</sup> Audit committees may wish to include a review of such relationships and transactions in their discussions with management and auditors, including a review of their terms and internal corporate and Board actions involving the transactions, prior to their recommendation that the financial statements be included in the company’s Form 10–K. See generally, Regulation S–K Item 306, 17 CFR 229.306, and Regulation S–B Item 306, 17 CFR 228.306.

pursuant to FAS 57, the former management positions may result in negotiation of terms that are more or less favorable than those available on an arm’s-length basis from clearly independent third parties that are material to the registrant’s financial position or results of operations. In some cases, investors may be unable to understand the registrant’s reported results of operations without a clear explanation of these arrangements and relationships.

Dated: January 22, 2002.

By the Commission.

**Margaret H. McFarland,**

*Deputy Secretary.*

[FR Doc. 02–1899 Filed 1–24–02; 8:45 am]

**BILLING CODE 8010–01–U**

## SECURITIES AND EXCHANGE COMMISSION

### Tel-One, Inc., File No. 500–1; Order of Suspension of Trading

January 23, 2002.

It appears to the Securities and Exchange Commission that there is a lack of current and accurate information concerning the securities of Tel-One, Inc. (“Tel-One”), because of questions regarding the accuracy of assertions by Tel-One, and by others, in documents sent to and statements made to market makers of the stock of Tel-One, other broker-dealers, and investors concerning, among other things: (1) The company’s claims about its prospects in the video conferencing industry; (2) the future price of Tel-One’s stock; and (3) the involvement of persons in control of the operations and management of the company in efforts to tout, and inflate artificially the price of, Tel-One’s stock.

The Commission is of the opinion that the public interest and the protection of investors require a suspension of trading in the securities of the above-listed company.

Therefore, it is ordered, pursuant to section 12(k) of the Securities Exchange Act of 1934, that trading in the above-listed company is suspended for the period from 9:30 a.m. EST, January 23, 2002, through 11:59 p.m. EST, on February 5, 2002.

By the Commission.

**Jill M. Peterson,**

*Assistant Secretary.*

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