

**SECURITIES AND EXCHANGE COMMISSION ISSUES INTERPRETIVE
RELEASE CONCERNING YEAR 2000 DISCLOSURE ISSUES**

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AUGUST 4, 1998

The Securities and Exchange Commission ("SEC") has issued an interpretive release (the "Release") setting forth guidance for public companies, investment advisors, investment companies and municipal securities issuers regarding their disclosure obligations concerning Year 2000 disclosure issues.* The Release provides guidance to public companies so that they can determine whether their Year 2000 issues are known material events, trends or uncertainties that should be disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") sections of disclosure documents. The Release also sets forth guidance regarding specific matters for companies to discuss in their MD&A Year 2000 disclosure and highlights issues to consider in connection with other SEC rules and the preparation of financial statements. The Release became effective on August 4, 1998 and supersedes revised Staff Legal Bulletin No. 5.

WHETHER TO DISCLOSE YEAR 2000 ISSUES

The Release states that a company must provide Year 2000 disclosure if:

- (i) its assessment of its Year 2000 issues is not complete; or
- (ii) management determines that the consequences of its Year 2000 issues would have a material effect on the company's business, results of operations or financial condition, without taking into account the company's efforts to avoid those consequences.

This two-part test is substantially similar to the test contained in revised Staff Legal Bulletin No. 5.

Under the first test, a company's assessment should take into account whether third parties with whom a company has a material relationship are Year 2000 compliant. For example, for vendors and suppliers, the relationship is material if there would be a material effect on the company if they do not timely become Year 2000 compliant. A similar analysis should be made for significant customers whose Year 2000 readiness could cause a loss of business that might be material to the company. The company should also consider its potential liability to third parties if its systems are not Year 2000 compliant. The Release states

* Release Nos. 33-7558; 34-40277; IA-738; IC 23366; International Series Release No. 1149.

that a company's Year 2000 assessment is not complete until it considers third-party issues and takes reasonable steps to verify the Year 2000 readiness of any third party that could cause a material impact on the company.

Under the second test, companies must determine whether they have a Year 2000 disclosure obligation by evaluating their Year 2000 issues on a "gross" basis. This test means that, in the absence of clear evidence of readiness, a company must assume that it will not be Year 2000 compliant and weigh the likely results. As part of this analysis, the company must assume that material third parties will not be ready either unless they have delivered written assurances that they expect to be Year 2000 compliant in time. The test is driven by measuring the consequences if the company is not prepared, rather than the amount of money the company spent, or plans to spend, to address Year 2000 issues.

WHAT TO DISCLOSE ABOUT YEAR 2000 ISSUES

Once a company determines that it has Year 2000 disclosure obligations, it must decide what to disclose about Year 2000 issues. The Release states that companies should address the following four categories of information:

State of Readiness

A company should describe its Year 2000 issues in sufficient detail to allow investors to understand the challenges that the company faces. The Release states that a description will generally include, at the very least, the following three elements. First, the description should address both information technology ("IT") and non-IT systems, such as elevators and the like. Second, for both their IT and non-IT systems, the company should disclose where they are in the process of becoming ready for the Year 2000. The status of the company's progress identified by phase, including the estimated timetable, should be disclosed. Third, the company should describe its Year 2000 issues relating to the third parties with whom it has a material relationship. The Release cites the example that if a telecommunications company discloses that it may have a business interruption, this disclosure may require other companies to disclose that, as a result, they too may have a business interruption.

Costs to Address Year 2000 Issues

Companies should disclose material historical and estimated costs. These include costs directly related to fixing Year 2000 issues, such as modifying software and hiring solution providers. The replacement cost of a non-compliant IT system should be disclosed as a Year 2000 estimated cost even if the company had planned to replace the system and merely accelerated the replacement date. On the other hand, a company does not need to include the replacement cost as a Year 2000 cost if it did not accelerate replacement.

Risks of Year 2000 Issues

Companies should include a reasonable description of their most reasonable likely worst-case Year 2000 scenarios. If a company does not know the answer, this uncertainty should be disclosed, as well as the efforts made to analyze the uncertainty. For example, companies should disclose estimated material lost revenues due to Year 2000 issues, if known.

Contingency Plans

Companies should describe how they are prepared to handle the most reasonable likely worst-case scenarios. Under this category, the company must describe its contingency plans. If the company has not yet established a contingency plan, the company should disclose that it does not have a contingency plan, whether it intends to create one and the timetable for doing so.

SUGGESTED ADDITIONAL DISCLOSURES

The Release states that providing the minimum level of Year 2000 disclosure set forth in the four categories of information above may not be sufficient to meet disclosure obligations and makes suggestions to help companies meet their obligations. While acknowledging that not all may be relevant to every company, the SEC suggests the following:

- (i) Disclose historical and estimated costs, even if disclosure is not required because the amounts are not material.
- (ii) As of the end of each reporting period, disclose how much of the total estimated Year 2000 project costs have already been incurred.
- (iii) Identify the source of funds, including percentage of the IT budget used for remediation.
- (iv) Explain if other IT projects have been deferred due to Year 2000 efforts and the effects of this delay.
- (v) Describe the use of any independent verification and validation processes.
- (vi) Use a chart to provide Year 2000 disclosure to help investors track a company's progress over time, as it is updated, and make peer comparisons.
- (vii) Include a breakdown of the costs, such as disclosure of cost to repair software and problems to replace problem systems and equipment.

FORWARD-LOOKING INFORMATION

The Release notes that almost all of the required MD&A disclosures concerning Year 2000 software problems contain forward-looking statements. For example, a projection of capital expenses or other financial items is a forward-looking statement because it anticipates how remediation and testing will proceed in the future. Similarly, a statement regarding estimated future costs due to business disruption caused by vendors, suppliers or customers typically would be a statement of future economic performance. Contingency plans that assess which scenarios are most likely would be forward-looking statements of plans and objectives. In contrast, some disclosure will be simply statements of historical fact and not forward-looking. For example, historical costs and whether a company has a contingency plan at all would be a matter of fact as well as whether a company actually has performed an assessment. Similar statements identifying the remediation phase that a company is in would be a matter of fact but timetables for implementation of future phases would be forward-looking. For the statutory safe harbors to apply, forward-looking statements must be accompanied by meaningful cautionary statements.

FINANCIAL STATEMENT CONSIDERATIONS

The Release contains a list of matters that companies and auditors should consider concerning accounting and related disclosure issues and the Year 2000. These include: (i) cost of modifying software (charged to expense as incurred), (ii) cost of failure (resulting operating losses recognized as incurred), (iii) disclosure of commitments (payments to be made under commitments to remediate Year 2000 problems or potential for debt acceleration due to Year 2000 related covenant defaults), (iv) revenue and loss recognition (in particular relating to software and product returns); (v) allowance for loan losses (if a borrower fails to comply with covenants regarding Year 2000 issues); (vi) losses from breach of contract; (vii) impairment of assets and (viii) disclosure of risks and uncertainties.

OTHER SEC REGULATIONS

In addition to MD&A and financial statements, other SEC rules and regulations may require disclosure. These include Regulation S-K relating to description of business, legal proceedings, material contracts and risk factors and Form 8-K.

GUIDANCE FOR INVESTMENT ADVISORS AND INVESTMENT COMPANIES

The Release provides guidance to investment advisors and investment companies for meeting their obligations under the Investment Advisors Act of 1940 and the Investment Company Act of 1940.

The anti-fraud provisions of the Investment Advisors Act of 1940 generally impose on investment advisors an affirmative duty to disclose to clients material facts concerning

advisory relationships. If the failure to address the Year 2000 issue could materially affect the advisory service provided to clients, an advisor that will not be able to, or is uncertain about its ability to, address Year 2000 issues, must disclose that information to clients.

For investment companies, whether Year 2000 issues are material depends upon the facts and circumstances of each company. Consideration should be given, for example, to whether Year 2000 issues affect an investment company's own operations, and its ability to obtain and use services provided by third parties, or its portfolio investments. Investment companies could face difficulties, among other things, performing various functions such as calculating net asset value, redeeming shares, delivering account statements and providing other information to shareholders. Because many investment company operations are performed by external service providers, the SEC expects that investment companies would, as a matter of course, discuss Year 2000 issues with their service providers and seek reasonable assurance from these service providers that they will address Year 2000 issues so as to allow the continuation of the provided services without interruption.

GUIDANCE FOR MUNICIPAL ISSUERS

The Release also contains guidance for municipalities. Although municipal securities offerings are exempt from registration and municipal securities issuers are exempt from the reporting provisions of the federal securities laws, they are not exempt from the anti-fraud provisions. The Release contains a discussion of various types of Year 2000 issues that municipal issuers may face.

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For additional information concerning the matters discussed in this memorandum, please contact Raymond W. Wagner ((212) 455-2568).

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