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Financial accounting and reporting by investment companies, April 15, 1977 : proposal to Financial Accounting Standards Board to amend AICPA Industry audit guide on audits of investment companies; Statement of position 77-1;

American Institute of Certified Public Accountants. Accounting Standards Division

Statement of Position on

77-1

Financial Accounting and Reporting by Investment Companies

April 15, 1977

Proposal to Financial Accounting Standards Board to Amend AICPA Industry Audit Guide on Audits of Investment Companies

Issued by
Accounting Standards Division

American Institute of
Certified Public Accountants

AICPA

NOTES

The American Institute of Certified Public Accountants has issued a series of industry-oriented Audit Guides that present recommendations on auditing procedures and auditors' reports and in some instances on accounting principles, and a series of Accounting Guides that present recommendations on accounting principles. Based on experience in the application of these Guides, AICPA Task Forces may from time to time conclude that it is desirable to change a Guide. A Statement of Position is used to revise or clarify certain of the recommendations in the Guide to which it relates. A Statement of Position represents the considered judgment of the responsible AICPA Task Force.

To the extent that a Statement of Position is concerned with auditing procedures and auditors' reports, its degree of authority is the same as that of the Audit Guide to which it relates. As to such matters, members should be aware that they may be called upon to justify departures from the recommendations of the Task Force.

To the extent that a Statement of Position relates to standards of financial accounting or reporting (accounting principles), the recommendations of the Task Force are subject to ultimate disposition by the Financial Accounting Standards Board. The recommendations are made for the purpose of urging the FASB to promulgate standards that the Task Force believes would be in the public interest.

Accounting Standards Task Force
on Investment Companies

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April 15, 1977

Marshall S. Armstrong, CPA
Chairman
Financial Accounting Standards Board
High Ridge Park
Stamford, Connecticut 06905

Dear Mr. Armstrong:

The accompanying Statement of Position of the Accounting Standards Division proposes changes to the AICPA Industry Audit Guide on Audits of Investment Companies to give effect to developments that have taken place since the Guide was published in 1973. It was prepared on behalf of the Division by the Accounting Standards Task Force on Investment Companies for consideration by the Financial Accounting Standards Board and for such action as the Board deems appropriate.

The Statement includes a section on money-market funds, which were not discussed specifically in the Guide. This section suggests reporting formats suitable for reporting the changes in net assets of money-market funds and provides guidance with respect to the presentation of the per-share data included in the financial statements as "Supplementary Information." In addition, the section contains recommendations on accounting and reporting for gains and losses on short-term investments.

The advent of listed options has increased trading volume significantly, and substantive procedural changes in the mechanics of the options market system have been codified and implemented. Accordingly, the Statement recommends that the sections of the Guide dealing with put and call options should be superseded. The Statement includes an expanded glossary, a discussion of industry practices, and recommendations on appropriate accounting and disclosure.

In recent years, a significant number of no-load funds, particularly money-market funds, have borne their own organization expenses. The Statement concludes, among other things, that expenses incurred by a newly organized open-end investment company in preparing its initial registration statement and obtaining clearance of such registration statement by the SEC should be considered part of its organization expense and accounted for as such. Expenses incurred after that registration statement has been declared effective by the SEC, such as printing a supply of prospectuses to be used for sales purposes, are not organization expenses. The Statement also contains recommendations with respect to the amortization of costs deferred by an investment company.

Finally, the Statement proposes an amendment to the discussion in the Guide of the valuation of short-term investments to make it clear that all investments, including short-term investments (money-market instruments), should be carried at amounts that approximate market or fair value.

Members of the Task Force will be glad to meet with you or your representatives to discuss this proposal. The Task Force would also appreciate being advised as to the Board's proposed action on the recommendations set forth in this Statement of Position.

Sincerely yours,

James H. Muller

James H. Muller
Chairman
Accounting Standards Task Force on
Investment Companies

cc: Securities and Exchange Commission

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Introduction

The AICPA Industry Audit Guide, *Audits of Investment Companies,* notes that "changes in the rules, regulations, practices, and procedures of the investment company industry have been frequent and extensive in recent years" and that "further changes are under consideration." A number of changes and new developments have taken place since the Guide was published in 1973 which the Accounting Standards Division believes should be reflected in an amendment to the Guide.

This proposed amendment presents the Division's views on the following matters:

- Money-market funds (an addition to the Guide)
- Put and call options (supersedes discussion in the Guide)
- Expenses during the development stage (an addition to the Guide)
- Amortization of deferred costs (an addition to the Guide)
- Valuation of short-term investments (an amendment to the Guide)

The Guide includes collective trust funds within its general definition of investment companies, but has no discussion of regulatory and tax matters specifically applicable to such funds. Although collective trust funds are not investment companies within the definition of the Investment Company Act of 1940 and are not regulated under the Securities Acts, the accounting and auditing discussions in the Guide are applicable to such funds, where relevant. In addition, the auditor should be familiar with Regulation 9 of the Comptroller of the Currency, which is the regulatory standard for most collective funds operated by banks, and Subchapter H of the Internal Revenue Code, which contains rules for the specialized tax treatment of collective funds.

Money-Market Funds

Background

Money-market funds are open-end management investment companies that invest principally in money-market instruments (short-term government obligations, commercial paper, bankers' acceptances, certificates of deposit, and so forth) with the objective of preserving capital, maintaining liquidity, and obtaining current income. As such, money-market funds are subject to the provisions of the AICPA Industry Audit Guide, *Audits of Investment Companies*.

At the time the Guide was published in October 1973, only a few money-market funds were in operation, and the Guide did not discuss such funds specifically. However, many more have commenced operations since that date, and the Division believes that specific guidance for money-market funds is now desirable.

Distribution Policies

Many money-market funds declare dividends daily, thereby maintaining net asset value per share at or near a fixed amount, depending on which of the following distribution policies is adopted.

Distribution Policy	*Effect on Net Asset Value per Share*
(a) Define income for dividend purposes as the sum of net investment income, net realized gain (loss), and net unrealized appreciation (depreciation). If income, as defined, is a negative amount for any day, that amount is first offset against undistributed dividends accrued during the month in each	Net asset value remains fixed.

Distribution Policy	*Effect on Net Asset Value per Share*
shareholder's account. If a negative amount remains in a shareholder's account, outstanding shares are reduced by treating each such shareholder as having contributed shares to the fund to the extent of such negative amount.	
(b) Define income as in (a) above, but take no action for any day in which such income is a negative amount.	Net asset value remains fixed unless income, as defined, is a negative amount, in which case net asset value will be less than the fixed amount until restored to the fixed amount through subsequent income, as defined.
(c) Define income for dividend purposes as the sum of net investment income and net realized gain (loss).	Net asset value varies from the fixed amount to the extent of unrealized appreciation or depreciation. Also, it is reduced if income, as defined, is a negative amount that is not offset by unrealized appreciation (net realized loss exceeds net investment income and unrealized appreciation).
(d) Declare daily dividends from net investment income only; distribute net realized gain annually.	Net asset value varies from the fixed amount to the extent of the sum of undistributed realized gain (loss) and unrealized appreciation (depreciation).

Long-term capital gains, as defined in the Internal Revenue Code, may be distributed only once every 12 months unless a

[1] Section 19(b) and Rule 19b-1 of the Investment Company Act of 1940.

specific exemption is obtained.[1] Therefore, a fund that expects to realize long-term gains and that wishes to follow distribution policy (a), (b), or (c) will need to request exemption from Section 19(b) of the 1940 Act to avoid adverse consequences.

See page 19 of this Statement for a discussion of the valuation of short-term investments.

Statement of Changes in Net Assets

A modification of the format suggested in the Guide for the Statement of Changes in Net Assets is required to report clearly the effects of following one of the distribution policies described in (a), (b), or (c) in the preceding section.

A fund that follows distribution policy (a) or (b) should include a subtotal for net investment income and net realized gain (loss) and unrealized appreciation (depreciation) in the Statement of Changes in Net Assets. This subtotal represents income as defined for dividend purposes.

The following format is appropriate for the Statement of Changes in Net Assets (shown in part) of a money-market fund that has adopted distribution policy (a) or (b).

From Investment Activities	19X1	19X0
Net investment income	$100,000	$80,000
Net realized gain (loss) on investments	2,000	(1,000)
Increase (decrease) in unrealized appreciation of investments	(3,000)	1,000
Total available for distribution	$ 99,000	$80,000
Dividends declared	99,500	80,000
Decrease in assets derived from investment activities[2]	$ (500)	–

The following format is suggested for the Statement of Changes in Net Assets (shown in part) of a money-market fund that follows distribution policy (c); that is, it distributes the sum of net investment income and net realized gain or loss daily.

[2] A decrease in net assets derived from investment activities would be reported by a company following distribution policy (b) only if the company incurred a net loss (realized and unrealized) on investments that was not offset by net investment income and net gains (realized and unrealized) prior to the end of the reporting period.

From Investment Activities	19X1	19X0
Net investment income	$100,000	$80,000
Net realized gain (loss) on investments	2,000	(1,000)
Total available for distribution	$102,000	$79,000
Dividends declared	(102,000)	(79,000)
Increase (decrease) in unrealized appreciation of investments	(3,000)	1,000
Increase (decrease) in net assets derived from investment activities	$ (3,000)	$ 1,000

Money-market funds that follow distribution policy (d), or that do not declare dividends daily, should follow the presentation on page 101 of the Guide.

Supplementary Information

The per-share data included in the financial statements as "Supplementary Information" should be presented on a basis consistent with the presentation of the Statement of Changes in Net Assets, as illustrated or discussed above.[3] A fund that follows distribution policy (a) and that has treated each shareholder as having contributed shares to the fund when income, as defined, is a negative amount, should include an additional line item in the per-share data to show the effect of such action.

The investment policies of money-market funds are such that gains and losses, whether realized or unrealized, are usually incidental to the realization of investment income. Also, the dividend policy adopted by a fund should have no effect on the reported ratio of income to average net assets, because the purpose of the ratio is to indicate the effective rate of earnings, regardless of when the earnings are distributed. Accordingly, the most significant ratio for a money-market fund to report is the ratio of net investment income, plus or minus realized and unrealized gains or losses, to average daily net assets. When supplementary infor-

[3] Income (as defined) per share should be based on the per-share dividends declared during the period and prorated by components based on the amounts shown in the Statement of Operations. For example, a fund following distribution policy (a) or (b) would apportion its per-share income (as defined) between net investment income and realized and unrealized gain (loss).

mation is provided by a money-market fund, this ratio should be reported instead of the ratio of net investment income to average net assets, which is included in the illustration of "Supplementary Information" in the Guide.

It may be appropriate for a fund that distributes only net investment income (distribution policy (d)) to provide a breakdown of the ratio, in a footnote or parenthetically, indicating the portion applicable to realized and unrealized gains or losses, if they are significant.

When yield information is presented as "Supplementary Information" or elsewhere in the financial statements, a description of the method of computation should be provided.

Reporting Gains and Losses

When short-term investments, including discounted instruments, are sold prior to maturity, realized gains and losses should be recorded as such, based on the difference between the proceeds from sale and cost (amortized cost in the case of discounted instruments). However, net realized gains or losses are ordinarily not significant in relation to the total dollar amount of sales of money-market instruments. Further, such gains or losses are rarely significant in relation to the results of operations of a money-market fund. Accordingly, except in unusual circumstances, a money-market fund need not report the proceeds from sales and the cost of securities sold in the Statement of Operations; it need report therein only the amount of net realized gain or loss.

Changes in unrealized appreciation or depreciation should be reported following the presentation on page 100 of the Guide.

Federal Income Taxes

A fund that includes unrealized appreciation or depreciation in dividends may have distributed more or less than its taxable income in a particular year. Accordingly, a fund that follows such a policy should pay particular attention to the provisions of the Internal Revenue Code relating to the distribution of taxable income, as discussed more fully in chapter 5 of the Guide.

Put and Call Options

Background

An active public market has been developed in listed call options, and trading in listed put options is expected in early 1977. Although there has been an over-the-counter market in options for many years and the public has participated to some degree, the advent of listed options has increased trading volume significantly, and substantive procedural changes in the mechanics of the options market system have been codified and implemented. Accordingly, the Division believes that the sections of *Audits of Investment Companies* covering options should be amended to give appropriate guidance with respect to an investment company that purchases or sells options. This Statement of Position supersedes the following sections of the Guide:

- Valuation of Put and Call Options Purchased (chapter 3, "Investment Accounts," page 37)
- Valuation of Put and Call Option Contracts Written by the Investment Company (chapter 3, "Investment Accounts," page 38)
- Put and Call Options (chapter 5, "Taxes," page 69)

Option Trading

The following glossary of terms should be helpful in understanding the mechanics of option trading.

Exchange-Traded Option. A put or call option traded on an exchange and settled through the facilities of an exchange. It gives the buyer of the option ("holder") the right to sell to (put) or buy from (call) the seller ("writer") the number of shares or other units of the underlying security covered by the option at the stated exercise price prior to the fixed expiration date of the option. The designation of an option includes the underlying security, the expiration month, and the exercise price; for example, "XYZ July 50" means that a unit of trading (typically 100 shares) of XYZ stock may be sold or purchased at $50 per share until the option expires on the expiration date in July. Options of like designation are said to be of the same "series."

Underlying Security. The security subject to sale or purchase upon the exercise of the option.

Unit of Trading. The number of units of the underlying security designated as the subject of a single option. In the absense of any other designation, the unit of trading for a common stock is 100 shares.

Exercise Price. The price per share or other unit at which the holder of an option may sell or purchase the underlying security upon exercise. The exercise price is sometimes called the "striking price."

Expiration Date. The last day on which an option may be exercised.

Premium. The aggregate price of an option agreed upon between the buyer and writer or their agents.

Opening Purchase Transaction. A transaction in which an investor becomes the holder of an exchange-traded option.

Opening Sale Transaction. A transaction in which one becomes the writer of an exchange-traded option.

Closing Purchase Transaction. A transaction in which a writer of an exchange-traded option liquidates his position as a writer by "purchasing," in a transaction designated as a closing purchase transaction, an option having the same terms as the option previously written. Such a transaction has the effect, upon payment of the premium, of canceling the writer's pre-existing position instead of resulting in the issuance of an option.

Closing Sale Transaction. A transaction by which a holder of an option liquidates his position as a holder by "selling," in a transaction designated as a closing sale transaction, an option having the same terms as the option previously purchased. Such a transaction has the effect of liquidating the holder's pre-existing position instead of resulting in the holder's assuming the obligation of a writer.

Covered Writer. A writer of a call option who, as long as he remains a writer, owns the shares or other units of the underlying security covered by the option. The writer of a put is "covered" only when he purchases an option on the same underlying security with an exercise price equal to or greater than that of the option written.

Uncovered Writer. A writer of an option who is not a covered writer; sometimes referred to as "naked."

Option Writing

As consideration for the rights and obligations represented by an option, the buyer pays, and the writer receives, a premium. The premium is determined in the exchanges' option markets on the basis of supply and demand, reflecting factors such as the duration of the option, the difference between the exercise price and the market price of the underlying security, and the price volatility and other characteristics of the underlying security. A covered writer of a call option gives up, in return for the premium, the opportunity for profit from an increase in the price of the underlying security above the exercise price as long as the option obligation continues, but he retains the risk of loss should the price of the security decline. Since the option holder may exercise the option and purchase the securities at the designated price at any time prior to the expiration date of the option, the option writer has no control over the date of sale.

An uncovered writer of a call option assumes, in return for the premium, the obligation to provide the option holder with the underlying securities upon exercise of the option. The uncovered writer, therefore, may have a substantial risk of loss should the price of the security increase, but he has no risk of loss should the price of the security decrease.

As long as a secondary market in options remains available on each of the exchanges, the writer of an option traded on an exchange is able to liquidate his position prior to the exercise of such option by entering into a closing purchase transaction. Such a transaction has the effect of canceling the writer's pre-existing position. The cost of such a liquidating purchase, however, can be greater than the premium received upon writing the original option.

Because the purchaser or writer has the ability to enter into a closing transaction, the option originally written may never be exercised. The exercise of an exchange-traded option takes place only through the Options Clearing Corporation (OCC), which is the obligor on every option, by the timely submission of an exercise notice by the clearing broker acting on behalf of the exercising holder. The exercise notice is then "assigned" by the OCC to a clearing broker acting on behalf of a writer of an option of the same series as the exercised option. This broker is then obligated to deliver the underlying security against payment of the aggregate exercise price. The assigned broker is randomly selected from clearing members having accounts with the OCC with options outstanding of the same series as the option being exercised.

Most investment companies deposit securities underlying the options written in order to guarantee delivery in the event the option is exercised.

Accounting

Portfolio securities underlying call options should be reported at value, determined in accordance with the provisions of the Guide, and reflected in net asset value accordingly. Premiums received by an investment company from the sale of outstanding call options should be included in the liability section of the Statement of Assets and Liabilities as a deferred credit and subsequently adjusted to the current market value (marked-to-market) of the option written. For example, if the current market value of the option exceeded the premium received (which should be shown parenthetically in the Statement of Assets and Liabilities), the excess would be an unrealized loss and, conversely, if the premium exceeded the current market value, such excess would be an unrealized gain. Current market value of exchange-traded options should be the last sales price or, in the absence of a transaction, the mean between the closing bid and ask prices, or the ask prices, in accordance with the valuation policy followed by the fund. The change in unrealized depreciation or appreciation resulting from the mark-to-market may be included with unrealized gains or losses on the portfolio in the Statement of Operations and Statement of Changes in Net Assets, with disclosure as to the amount, or it may be reported as a separate line item.

With respect to covered options, disclosure, summarized by security, should be made of the description and number of shares of portfolio securities covering outstanding options and the market value of the options. Disclosure should also be made of the aggregate market value of the securities or other assets deposited as collateral. With respect to uncovered options, disclosure should be made of the description and quantity of securities under option, the expiration dates and exercise prices, the current market prices of the securities covered by the options, and the assets deposited in escrow with respect to such options.

Subsequent to the sale of a call option, any one of three events may occur: the option may expire on its stipulated expiration date; the writer may enter into a closing transaction; or the option holder may exercise his right to call the security. Either of the first two events results in a realized gain (or loss if the cost of the closing transaction exceeds the premium received when the option was sold) for the investment company option writer and should be accounted for as such. The third possible event results, in the case of a covered writer, in the sale of the underlying securities, unless the writer purchases like securities for delivery to the exercising holder. The proceeds should be increased by the amount of premium originally received, and realized gains or losses resulting from such sales should be accounted for in the conventional manner. If an uncovered option is exercised, the writer must purchase the underlying securities in order to meet his obligation to the option holder. In such situations, the writer's realized loss resulting from the simultaneous purchase and sale of the securities should be reduced by the premium originally received, and the net realized loss (or gain) should be accounted for in the conventional manner.

The foregoing describes the accounting for the sale of call options. The same principles are applicable to the sale of put options.

Actively traded put and call options purchased by an investment company should be accounted for in the same manner as marketable portfolio securities. The cost of portfolio securities acquired through the exercise of call options should be increased by the premium paid to purchase the call. The proceeds from securities sold through the exercise of put options should be decreased by the premium paid to purchase the put.

Transactions in options not listed on a national exchange or not actively traded should be accounted for as described in the foregoing paragraphs, except that the determination of unrealized gain or loss during the contract period of the option must be based on the fair value of the option as determined by the investment company's board of directors. Among the many factors to be considered in the determination of fair value are the price of the underlying securities, the liquidity of the market, and the time remaining prior to expiration date.

Federal Income Taxes

The following paragraphs are intended to supersede only that portion of chapter 5 of the Guide ("Taxes") dealing with put and call options. Reference to that chapter should be made for other information pertinent to the taxation of investment companies.

For federal income tax purposes, premium income from the sale of options is deferred until expiration or exercise of the option, or until a closing purchase transaction takes place. If the option expires, the premium constitutes a short-term capital gain. If the option is exercised and the underlying securities are sold, the premium is added to the proceeds from the sale of the securities in determining capital gain or loss. Such gain or loss is short-term or long-term depending upon the holding period of the underlying securities. If the option is closed in a closing purchase transaction, the difference between the amount paid for the option purchased and the premium received on the original sale is a short-term capital gain or loss.[4]

Under the Internal Revenue Code, an investment company cannot qualify as a regulated investment company unless, among other things, less than 30 percent of its gross income is derived from gains from the sale or other disposition of securities held for less than three months ("30 percent rule"). Therefore, in order to be taxable as a regulated investment company, its ability to write

[4] The termination of a writing position that was established on or before September 1, 1976, by lapse of the option or by a closing purchase transaction, will produce ordinary income or loss.

options with exercise periods of less than three months or to effect closing purchase transactions within three months of writing options is restricted. For purposes of meeting this "three-month test," the holding period for the sale of an option commences on the day it is written.

An investment company must derive at least 90 percent of its gross income from dividends, interest, and gain from the sale or other disposition of stock or securities ("investment income"), in order to qualify as a regulated investment company in any taxable year. For tax purposes, income received from expired call options and from profits in executing closing purchase transactions for amounts less than the call premiums received qualifies as investment income.

Expenses During the Development Stage

The standards of financial accounting and reporting set forth in FASB Statement No. 7, *Accounting and Reporting by Development Stage Enterprises,* are applicable to financial statements issued by investment companies that are in the development stage, as defined in the FASB Statement. The following paragraphs in this section discuss certain expenses that may be incurred by an investment company that is in the development stage.

A newly formed investment company will incur organization expenses unless it is sponsored by a management company that has agreed to absorb these expenses. Organization expenses consist of expenses incurred in order to establish the company and legally equip it to engage in business. In recent years, a significant number of no-load funds, particularly money-market funds, have borne their own organization expenses.

An open-end investment company, which is organized to offer shares of capital stock to the public continuously and to invest the proceeds from sale of such capital stock, cannot be considered to be organized until it has registered securities with the Securities and Exchange Commission. Therefore, expenses incurred by a newly organized open-end investment company in preparing its initial registration statement and obtaining clearance of such registration statement by the SEC should be considered part of its organization expenses; expenses incurred after that registration statement has been declared effective by the SEC, such as printing a supply of prospectuses to be used for sales purposes, are not organization expenses.

As stated in *Audits of Investment Companies,* "closed-end companies charge all registration fees against paid-in capital at the time the shares are sold." This Statement of Position does not modify that requirement.

Once an investment company has been organized to do business, it usually engages immediately in its planned principal operations, that is, sales of capital stock and investment of funds. The training of employees, development of markets for the sale of capital stock, and similar activities are usually performed by the investment adviser or other agent, and in such cases the costs of these activities are not borne directly by the investment company. However, an investment company (particularly one that does not employ agents to manage its portfolio and perform other essential functions) may engage for a period of time in such activities, and may bear those costs directly during its development stage.

As stated above, an investment company that is in the development stage is subject to the provisions of FASB Statement No. 7. Paragraph 10 of the FASB Statement notes that "generally accepted accounting principles that apply to established operating enterprises . . . shall determine whether a cost incurred by a development stage enterprise is to be charged to expense when incurred or is to be capitalized or deferred." Accordingly, the costs and expenses discussed in the preceding paragraphs should be accounted for in accordance with the generally accepted accounting principles that apply to established operating enterprises. Organization expenses of investment companies are usually deferred and amortized in financial statements prepared in conformity with generally accepted accounting principles.

Amortization of Deferred Costs

Costs deferred by an investment company should be subject to the same assessment of recoverability that would be applicable to any established operating company. Such costs should be amortized to income over the period during which it is expected that a benefit will be realized. That period may vary according to the type of expense. Several costs are listed below.

Organization Expenses. Generally such expenses are amortized over a period of not more than 60 months from the date of commencement of operations. Straight-line or other acceptable methods of amortization may be utilized.

If such expenses are amortized on the basis of assets expected to be managed over the period selected, the projected growth rate initially used as the basis for establishing an amortization table should be reviewed frequently and adjusted, if necessary, to reflect actual experience.

Cost of Printing Prospectuses. Costs deferred in connection with printing a supply of prospectuses for sales purposes should be amortized, generally on a straight-line basis, over the period during which the prospectus may be used, which is limited to a period ending 16 months after the date of the latest audited financial statements. If during this period it becomes evident that the prospectus will be effective for a shorter period than originally anticipated, amortization should be accelerated so that no costs remain deferred at the end of such shorter period.

Registration Fees. Deferred SEC and state registration fees should be written off as the registered shares of stock are sold (but over not more than 60 months).

The summary in the financial statements describing an investment company's significant accounting policies should cover the company's accounting for deferred costs.

Valuation of Short-Term Investments

The discusssion of the valuation of short-term investments on page 39 of the Guide states that "original cost plus amortized discount or accrued interest . . . usually approximates market value." This statement was made when holdings of short-term investments generally constituted a small portion of an investment company's portfolio. It was not intended to modify the principle that "all investment companies should report their securities portfolio at value." In all cases, the board of directors should be satisfied that investments, including short-term investments (money-market instruments), are carried at amounts that approximate market or fair value. Accordingly, the Division believes that the discussion entitled Short-Term Investments on page 39 of the Guide should be amended by the addition of the following paragraph:

> Although the amortized cost of money-market instruments that mature within a relatively short period of time ordinarily approximates market value, it must be recognized that unusual events, such as the impairment of the credit standing of the issuer, can significantly affect the value of short-term investments regardless of the number of days to maturity. Changes in interest rates can also have a significant effect on the value of money-market instruments with longer terms to maturity. In such cases, amortized cost might not approximate the value of these investments. When amortized cost does not approximate value, the investments should be valued on the basis of quoted sales prices, bid and asked prices, or fair value based upon appraisals furnished by market makers or other appropriate evidence.