

**INVESTMENT DEALERS
ASSOCIATION OF CANADA –
PROPOSED REGULATION - YEAR
2000 NARRATIVE REPORT AND
SPECIFIED PROCEDURES**

I. EXECUTIVE SUMMARY

The IDA has required its Members to file surveys and management representations with respect to their Year 2000 preparation efforts. The IDA has also modified its examination programs to include a review of Members' Year 2000 plans and preparations. To date, there has been no other third party review of Members' Year 2000 plans. IDA staff have discussed this situation with representatives of the Canadian Securities Administrators ("CSA") and agree with them that a further independent review of Members' Year 2000 plans is desirable. On January 11, 1999, the Ontario Securities Commission sent the IDA a letter requesting the IDA to implement:

1. Emergency Amendments to Form 1 requiring Members with regulatory capital equal to or greater than \$5 million to file with the IDA, the securities regulators with which the Member is registered and the Canadian Investor Protection Fund ("CIPF") by May 15, 1999
 - (a) a Narrative Report on Year 2000 Preparations prepared by management of the Member with information current to March 31, 1999; and
 - (b) a report by a public accountant on the results of applying specified procedures relating to the narrative report.

The OSC have also indicated that they and other members of the CSA intend to make these reports available to the public.

II. DETAILED ANALYSIS

At midnight on December 31, 1999, unless the proper modifications have been made, the program logic in some of the world's computer systems will start to produce erroneous results. Primarily this will be the result of computer systems incorrectly reading the date "01/01/00" as being the year 1900 or another incorrect date. In addition, computer systems may fail to detect that the Year 2000 is a leap year.

Problems can also arise earlier than January 1, 2000 as dates in the next millenium are entered into non-Year 2000 compliant programs. For example, firms operating in the securities industry could experience the following Year 2000 Implications:

- Computer programs not accepting settlement dates in the Year 2000;
- Various computational models, such as those used for risk analysis, hedging, and derivative pricing and trading, being inaccurate or unworkable;
- Difficulty in calculating interest payments and maturity dates for debt instruments that mature in the Year 2000 and thereafter.

These problems could have negative repercussions throughout the world's financial systems because of the extensive interrelationship and information sharing between Canadian investment firms and foreign financial firms and markets.

Because accurate output from computer programs is vital to investment firms record keeping and operations, all IDA member firms should be taking steps to avoid the Year 2000 implications.

IDA Bylaw 17.2 states that *"every Member shall keep and maintain at all times a proper systems of books and records"*. Given that records of a Member firm are date sensitive and in order for SROs to better assess and prepare for SRO contingency planning in regards to Member firm's failure to adequately plan for Year 2000 readiness, amendments to the IDA Bylaws are

required. These amendments are necessary to ensure that Member firms maintain an adequate system of books and records at all times.

The proposed amendments are very similar to regulations recently implemented in the United States. Staff of the other Participating Institutions of the CIPF have indicated that they intend to implement similar changes.

VI. PROPOSAL

It is recommended that the Joint Regulatory Financial Questionnaire and Report be amended to require Members with Capital Employed equal to or greater than \$5 million, as at March 31, 1999, to file with the IDA, the securities regulators with which the Member is registered and the Canadian Investor Protection Fund ("CIPF") by May 15, 1999:

1. a Narrative Report on Year 2000 Preparations prepared by management of the Member with information current to March 31, 1999; and
2. a report by a public accountant on the results of applying specified procedures relating to the narrative report.

Copies of these reports are enclosed. It is recommended that this change be made on an emergency basis.

The specified procedures will be attached to an Accountant's Report on Applying Specified Procedures, to be signed by the public accountant performing the specified procedures. Both the Narrative Report on Year 2000 Preparations and the report by a public accountant on the results of applying specified procedures will be public filings which may be posted on the websites of regulators with which a Member is registered.

V. COMMENTARY

These recommendations are supported by the serious implications that the Year 2000

presents to the investing public in the event that any Member firm that handles customer monies or securities fails to take necessary actions to maintain an adequate system of books and records.

For Members, particularly larger Members whose operations have a significant impact on the operation of the securities industry as a whole, it is desirable to have a third party review of the Member's Year 2000 Plans. The recommendation accomplishes this by requiring a public accountant to conduct specified procedures relating to the Narrative Report on Year 2000 Preparations prepared by the Member.

The Accountant's Report on Applying Specified Procedures will be prepared in accordance with a Guideline to be published by the Canadian Institute of Chartered Accountants.

There will be a cost associated with having a public accountant perform these specified procedures. We believe that the additional cost is warranted by the benefits to be obtained by this change. However, these costs will be decreased by only having Members with Capital Employed greater than or equal to five million dollars complete these reports.

VI. SOURCES

- IDA Rule Book.

These rule amendments were approved at a meeting of the IDA Board on January 13, 1999. The IDA believes that pursuant to sub-paragraph 14 (b)(ii) of the IDA Recognition Criteria [(1995) 18 OSCB 2671], there is an urgent need for the above-noted rule changes and that without changes, there is substantial risk of material harm to investors, clients, creditors, Members, CIPF or the IDA.

Narrative Report on Year 2000 Preparations

Firm Name:

Firm Address:

Identify a specific person or persons that are responsible for your Year 2000 project and are available to discuss the contents of this report.

Name:

Title:

Business Address:

Respond to each of the following questions in narrative form.

- (A) Has the registrant's board of directors (or similar body) approved and funded plans for assessing, remediating, replacing and testing its computer systems for the Year 2000 Problem?¹ Your response shall include the specific budget allocation for each of fiscal years 1998, 1999 and 2000.
- (B) Do the registrant's plans for preparing and testing its computer systems for the Year 2000 Problem exist in writing and do the plans address all of the registrant's mission critical computer systems, physical facilities and communications systems wherever located throughout the world?
- (C) Do the registrant's plans address external interfaces with third party systems that communicate with its systems?
- (D) Has the registrant identified which mission critical systems are not currently Year 2000 compliant?

¹ CSA National Instrument 33-106: Year 2000 Preparation Reporting interprets the term "Year 2000 Problem" as including problems arising from any of the following:

- (a) computer software incorrectly reading the date "01/01/00" as being the year 1900 or another incorrect year;
- (b) computer software incorrectly identifying a date in the year 1999 or any year thereafter;
- (c) computer software failing to detect that the year 2000 is a leap year;
- (d) any other computer software error that is directly or indirectly caused by the problems set out in clauses (a), (b) or (c).

- (E) Has the registrant assigned existing employees, hired new employees, or engaged third parties to provide assistance in addressing the Year 2000 Problem? If so, provide a description of the work that these groups of individuals have performed as of the date of this report.
- (F) What is the registrant's current progress on each stage of preparation for potential problems caused by the Year 2000 Problem for both its mission critical and non-mission critical systems? These stages are:
- (1) Awareness of the Year 2000 Problem (including designating individuals responsible for Year 2000 compliance, presentations to the Board, management and employees, and contacting third parties);
 - (2) Assessment of what steps the registrant must take to address the Year 2000 Problem (including preparing an inventory of computer systems affected by the Year 2000 Problem);
 - (3) Implementation of the steps needed to address the Year 2000 Problem;
 - (4) Internal testing of systems designed to address the Year 2000 Problem including the number and a description of the material exceptions resulting from such testing that are unresolved as of the reporting date;
 - (5) Point-to-point or industry wide testing of systems designed to address the Year 2000 Problem (including testing with other registrants, other financial institutions, suppliers and customers), including the number and a description of the material exceptions resulting from such testing that are unresolved as of the reporting date;
 - (6) Implementation of tested systems that will address the Year 2000 Problem.
- (G) Has the registrant identified and contacted all third parties (including clearing firms, utilities, vendors, service providers, counterparties) who provide mission critical systems and has any such third party declined or failed to provide assurances that it is taking the necessary steps to prepare for the Year 2000?
- (H) Does the registrant have written contingency plans that have been approved by the board of directors (or similar body) in the event that after December 31, 1999, it has problems caused by the Year 2000 Problem? Does the contingency plan account for third parties whose systems may fail after December 31, 1999?
- (I) What levels of management of the registrant are responsible for addressing potential problems caused by the Year 2000 Problem? Provide a description of the responsibilities for each level of management regarding the Year 2000 Problem.
- (J) Provide any additional material information concerning the registrant's management of the Year 2000 Problem that will help the regulators, self-regulatory organizations, and the Canadian Investor Protection Fund assess the readiness of the registrant for the Year 2000.

Name and Title - Type

Signature

Chief Executive Officer

Chief Financial Officer

Designated Year 2000 person responsible

Chairman of Year 2000 Board Committee

[date]

	<u>Findings</u>		
	<u>N/A</u>	<u>No Exception</u>	<u>Exception</u>
<u>Procedure</u>			
1. We read the entity's written plans for preparing and testing the entity's computer systems for potential year 2000 problems ⁱ ("year 2000 project plans") and-	_____	_____	_____
(a) Determined, by comparison to organization charts (or similar corporate documents) and the entity's most recently filed "risk adjusted capital calculation" that the year 2000 project plans include all divisions and branches of the registered entity and any company that has been consolidated in accordance with Note 3 of the General Notes and Definitions. ⁱⁱ	_____	_____	_____
(b) Obtained written representation from the entity's chief operating officer (or equivalent) that the organization charts (or similar corporate documents) used in performing this procedure were complete, accurate, and current.	_____	_____	_____
(c) Obtained written representation from the entity's chief operating officer (or equivalent) that the entity's most recently filed "risk adjusted capital calculation" includes any company that has been consolidated in accordance with Note 3 of the General Notes and Definitions.	_____	_____	_____
(d) Compared the organizational information in the year 2000 project plans (see item 1a) with the corresponding information in the Narrative Report on Year 2000 Preparations and found them to be in agreement.	_____	_____	_____
2. We read the entity's year 2000 project plans, and determined that the plans include each of the elements listed below. In performing this procedure, we did not evaluate the completeness or accuracy of the information contained within each element of the written document nor did we evaluate whether the year 2000 project plans will achieve the objectives set forth therein.	_____	_____	_____

Assessment

Mission-critical systems

<u>Procedure</u>	<u>Findings</u>	
	<u>N/A</u>	<u>No Exception</u>
(a) The entity’s definition of mission-critical systems. (In defining “mission-critical”, the entity included, as applicable, systems whether developed and maintained in-house or by an outside service organization related to clearing and settlement, customer segregation, risk adjusted capital calculation, financial reporting and payroll, among other things.)	_____	_____
(b) Process for identifying and actual identification of systems (including affected software and hardware) that the entity has determined are mission-critical systems.	_____	_____
(c) Process for identifying and actual identification of mission-critical systems that the entity has determined present a potential year 2000 problem (hereinafter referred to as “non-compliant”).	_____	_____
<i>Vendors, service providers and counterpartiesⁱⁱⁱ</i>		
(d) Process for identifying and actual identification of vendors, service providers and counterparties (hereinafter collectively referred to as “third parties”) that the entity has determined to be significant (as defined by the entity) in the context of the entity’s potential year 2000 problems.	_____	_____
(e) Process for identifying and actual identification of significant third parties with respect to which the entity has determined either (1) the third party’s lack of year 2000 readiness is expected to result in its inability to continue to provide goods and services or perform in the time and manner required, or (2) insufficient information is available to the entity to make an assessment as to the significant third party’s year 2000 readiness.	_____	_____
Electronic Interfaces		
(f) Process for identifying and actual identification of internal and external electronic interfaces (hereinafter collectively referred to as “interfaces”) that the entity has determined to be significant (as defined by the entity) in the context of the entity’s potential year 2000 problems.	_____	_____
(g) Process for identifying and actual identification of significant interfaces that the entity has determined are non-compliant.	_____	_____

Remediation strategy

Mission-critical systems

- (h) Plans for repairing or replacing each non-compliant mission-critical system (including affected hardware and software). _____
- (i) The date by which each non-compliant mission-critical system is expected to be year 2000 ready and either (1) a determination by the entity that such date is prior to the date that the entity expects the mission-critical system to fail, or (2) plans for resolving situations where mission-critical systems are not expected to be year 2000 ready before failure. _____

Third Parties

- (j) Plans for resolving situations where either (1) a significant third party's assessed lack of year 2000 readiness is expected to result in its inability to provide goods and services or perform in the time and manner required, or (2) insufficient information is available to the entity to make an assessment as to the significant third party's year 2000 readiness. _____

Interfaces

- (k) Plans for repairing or replacing each significant non-compliant interface (including affected hardware and software). _____
- (l) The date by which each significant non-compliant interface is expected to be year 2000 ready and either (1) a determination by the entity that such date is prior to the date that the entity expects the significant interfaces to fail, or (2) plans for addressing situations in which significant interfaces are not expected to be year 2000 ready before failure. _____

Staffing

- (m) Identification of staff resources needed, including assignment of existing employees and/or hiring of new employees or contractors to implement the year 2000 project plans. _____
- (n) Process to evaluate staffing requirements on an ongoing basis throughout the term of the project. _____

Testing

- (o) Plans for testing year 2000 project efforts relating to each mission-critical system and significant interface (including affected hardware and software) as follows:
 - 1) Internal testing _____
 - 2) Point-to-point testing _____
- (p) Process for reporting results of testing (including exceptions) identified in item o above to members of management assigned oversight responsibility for the implementation of the year 2000 project plans (see item s below). _____

Contingency Plans

- (q) Plans for addressing unexpected failures or unsuccessful remediation efforts of mission-critical systems or significant interfaces and unexpected inability of significant third parties to continue to provide goods and services or perform in the time and manner required due to lack of year 2000 readiness.

Timetable

- (r) Timetable with milestones for completion of the key elements (assessment, implementation of remediation strategy, staffing, testing and contingency planning) of the entity's year 2000 project plans.

Management Oversight

- (s) Specific identification of the member(s) of management who have been assigned oversight responsibility for the implementation of the year 2000 project plans.

Monitoring

- (t) Procedures for reporting the progress of the year 2000 project efforts to members of management assigned oversight responsibility for the implementation of the year 2000 project plans (see items above).
- (u) Procedures for reporting the progress of the year 2000 project efforts, including the results of testing, to the board of directors.^{iv}
- (v) Procedures for evaluating the progress of the year 2000 project efforts, including testing thereof, and making revisions to the year 2000 project plans as necessary.
3. We compared the information described in items 2a to 2v with the corresponding information in the Narrative Report on Year 2000 Preparations and found it to be in agreement.
4. We read minutes of meetings of the board of directors or made inquiries of individuals in attendance at meetings of the board of directors and noted that the board of directors of the entity approved the year 2000 project plans. We compared this information with the corresponding information in the Narrative Report on Year 2000 Preparations and found it to be in agreement.
5. We read minutes of the meetings of the board of directors or made inquiries of individuals in attendance at meetings of the board of directors and noted that the board of directors has approved the commitment of financial resources determined by management to be sufficient to accomplish the objectives of the entity's year 2000 project plans. We compared this information with the corresponding information in the Narrative Report on Year 2000 Preparations and found it to be in agreement. In performing this procedure, we did not evaluate the adequacy of the resources determined by management to be sufficient to accomplish the objectives of the year 2000 project plans.

6. We obtained from management a list of business units^v _____ considered by the entity to be significant and performed the following procedures: _____

Assessment

- (a) We inquired of management of five randomly selected _____ [or 100% if less than five] significant business units _____ (see list below), and obtained written representation therefrom, as to whether the identification of mission-critical systems included in the entity's year 2000 project plans included all systems that they considered critical to the continuation of operations in their respective business unit (see item 2b above). An exception would be reported if, as a result of this procedure, management of a significant business unit identified systems that they considered critical to the continuation of operations in their respective business unit that are not included in the entity's year 2000 project plans.

[List the five business units here.]

- (b) We inquired of management of five randomly selected _____ [or 100% if less than five] significant business units _____ (see list below), and obtained written representation therefrom, as to whether the identification of significant third parties included in the entity's year 2000 project plans included all third parties that they considered critical to the continuation of operations in their respective business unit (see item 2d above). An exception would be reported if, as a result of this procedure, management of a significant business unit identified significant third parties that they considered critical to the continuation of operations in their respective business unit that are not included in the entity's year 2000 project plans.

[List the five business units here.]

- (c) We inquired of information technology management of _____
 five randomly selected [or 100% if less than five] _____
 significant business units (see list below), and obtained _____
 written representation therefrom, as to whether the _____
 identification of interfaces included in the entity's year _____
 2000 project plans included all interfaces that they _____
 considered critical to the continuation of operations in _____
 their respective business unit (see item 2f above). An _____
 exception would be reported if, as a result of this _____
 procedure, information technology management of a _____
 significant business unit identified interfaces that they _____
 considered critical to the continuation of operations in _____
 their respective business unit that are not included in _____
 the entity's year 2000 project plans.

[List the five business units here.]

Staffing

- (d) We read reports to or summaries of meetings attended _____
 by the individual(s) of the management team with _____
 oversight responsibility for the execution of the year _____
 2000 project plans indicating that implementation of _____
 staffing plans, as set forth in the year 2000 project _____
 plans, are being tracked and deviations from the year _____
 2000 project plans are being identified.
- (e) We read contracts or other written evidence of _____
 engagements with five randomly selected [or 100% if _____
 less than five] individuals (not employees) or entities _____
 that were contracted to implement year 2000 project _____
 activities. We compared this information with the _____
 corresponding information in the year 2000 project _____
 plans and found them to be in agreement.

Testing

- (f) We read reports to or summaries of meetings attended _____
 by the individual(s) of the management team with _____
 oversight responsibility for the execution of the year _____
 2000 project plans indicating that the status of testing _____
 of mission-critical systems and significant interfaces is _____
 being tracked and any delays in schedule are being _____
 identified.
- (g) We obtained written representation from the _____
 individual(s) of the management team with oversight _____
 responsibility for the execution of the year 2000 _____
 project plans that the status of testing of mission- _____
 critical systems and significant interfaces is being _____
 tracked and any delays in schedule are being identified.

Monitoring

- (h) We read minutes of meetings of the board of directors _____ or made inquires of individuals in attendance at meetings of the board of directors and noted that, as called for in the year 2000 project plans, the board of directors is receiving periodic updates of the status of the implementation progress of the year 2000 project plans.
- (i) We read reports to or summaries of meetings attended _____ by the individual(s) of the management team with oversight responsibility for executing the year 2000 project plans indicating that modifications to the year 2000 project plans that they have determined are necessary, including those found to be necessary as a result of testing, or delays in schedule, have been made.
- (j) We obtained written representation from the _____ individual(s) of the management team with oversight responsibility for executing the year 2000 project plans that modifications to the year 2000 project plans that they have determined are necessary, including those found to be necessary as a result of testing, or delays in schedule, have been made.
7. We compared the information described in items 6a to 6j _____ with the corresponding information in the Narrative Report on Year 2000 Preparations and found it to be in agreement. (Include description of any exceptions.)

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ⁱ CSA National Instrument 33-106: Year 2000 Preparation Reporting interprets the term “Year 2000 Problem” as including problems arising from any of the following:

- computer software incorrectly reading the date "01/01/00" as being the year 1900 or another incorrect year;
- computer software incorrectly identifying a date in the year 1999 or any year thereafter;
- computer software failing to detect that the year 2000 is a leap year;
- any other computer software error that is directly or indirectly caused by the problems set out in clauses (a), (b) or (c).

ⁱⁱ See the Joint Regulatory Financial Questionnaire and Report.

ⁱⁱⁱ For purposes of this report, vendors, service providers and counterparties may include affiliated entities.

^{iv} As used in this report, "board of directors" refers to the board of directors, its designee committee for addressing year 2000 matters, or group equivalent to the board of directors or designee committee

^v The entity's list of significant business units includes profit centers as well as support units such as treasury, accounting, payroll and human resources, order entry and trade execution, clearance and settlement, and regulatory reporting.