

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 240

[Release No. 34-40164; File No. S7-7-98]

RIN 3235-AH36

Reports To Be Made by Certain Brokers and Dealers

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule; request for additional comments.

SUMMARY: The Securities and Exchange Commission ("Commission") is reopening the comment period with respect to its proposal that would have required broker-dealers to engage an independent public accountant to attest to specific assertions included in the broker-dealer's report on Year 2000 compliance. The attestation by independent public accountants was one amendment to Rule 17a-5 under the Securities Exchange Act of 1934 proposed by the Commission in Release No. 34-39724 which was published in the **Federal Register** on March 12, 1998 (63 FR 12056).

DATES: Comments should be received on or before August 12, 1998.

ADDRESSES: Comments should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission ("Commission"), 450 Fifth Street, NW, Washington, DC 20549. Comments also may be submitted electronically at the following E-mail address: rule=comments@sec.gov. Comment letters should refer to File No. S7-7-98; this file number should be included on the subject line if E-mail is used. All comments received will be available for public inspection and copying at the Commission's Public Reference Room, 450 Fifth Street, NW, Washington, DC 20549. Electronically submitted comment letters will be posted on the Commission's Internet web site (<http://www.sec.gov>).

FOR FURTHER INFORMATION CONTACT: Michael A. Macchiaroli, Associate Director, 202/942-0131; Thomas K. McGowan, Assistant Director, 202/942-4886; Lester Shapiro, Senior Accountant, 202/942-0757; or Christopher M. Salter, Staff Attorney, 202/942-0148, Division of Market Regulation, Securities and Exchange Commission, 450 Fifth Street, NW, Mail Stop 10-1, Washington, DC 20549.

SUPPLEMENTARY INFORMATION:

I. Introduction

At midnight on December 31, 1999, unless the proper modifications have

been made, the program logic in many of the world's computer systems will start to produce erroneous results because, among other things, the systems will incorrectly read the date "01/01/00" as being the year 1900 or another incorrect date. In addition, 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 millennium are entered into non-Year 2000 compliant programs.

The Commission views the Year 2000 problem as an extremely serious issue. A failure to assess properly the extent of the problem, remediate systems that are not Year 2000 compliant, and then test those systems could endanger the nation's capital markets and place at risk the assets of millions of investors. In light of this, both the broker-dealer industry and the Commission are working hard to address the industry's Year 2000 Problems.¹

In a companion release also issued today, the Commission is adopting amendments to Rule 17a-5² under the Securities Exchange Act³ that require certain broker-dealers to file reports with the Commission and their Designated Examining Authority ("DEA") regarding Year 2000 compliance.⁴

II. Year 2000 Reporting Requirements

The amendments to Rule 17a-5 included in the Adopting Release require broker-dealers with a minimum net capital requirement of \$5,000 or greater to file the new Form BD-Y2K. Part I of Form BD-Y2K is a check-the-box Year 2000 questionnaire. Each broker-dealer that is required to maintain net capital of \$100,000 or greater will also be required to file Part II of Form BD-Y2K, which requires a narrative discussion of its efforts to address Year 2000 Problems.

Generally, Form BD-Y2K requires each broker-dealer to discuss the steps it has taken to address Year 2000 Problems. Each broker-dealer, among other things, is required to (i) indicate whether its board of directors, or similar body, has approved and funded written Year 2000 remediation plans that

address all mission critical computer systems; (ii) describe its Year 2000 staffing efforts; (iii) discuss its progress on each stage of preparation for the Year 2000;⁵ (iv) indicate if it has written contingency plans to deal with Year 2000 problems that may occur; and (v) identify what levels of management are responsible for Year 2000 remediation efforts.⁶

III. Independent Public Accountant Review

The Commission originally proposed amendments to Rule 17a-5⁷ that would have required each broker-dealer to have an independent public accountant attest to several specific assertions included in its second Year 2000 report, now Part II of Form BD-Y2K.⁸ In response to the Proposing Release, the American Institute of Certified Public Accountants ("AICPA") commented that the required attestation report would be difficult for independent public accountants to provide.⁹ The AICPA said that some of the required broker-dealer assertions are not appropriate for accountant attestation because the assertions are not capable of reasonably consistent measurement against reasonable criteria. The AICPA stated that currently, there are no established criteria related to Year 2000 remediation efforts, and that the lack of

⁵ These stages are: (i) Awareness of potential Year 2000 Problems; (ii) assessment of what steps must be taken to avoid Year 2000 Problems; (iii) implementation of the steps needed to avoid Year 2000 Problems; (iv) internal testing of software designed to avoid Year 2000 Problems; (v) integrated or industry-wide testing of software designed to avoid Year 2000 Problems (including testing with other broker-dealers, other financial institutions, customers, and vendors); and (vi) implementation of tested software that will avoid Year 2000 Problems.

⁶ The Commission refers members of the public to the Adopting Release for more detailed information about the reporting requirements and Form BD-Y2K.

⁷ Release Nos. 34-39724; IC-23059; IA-1704, (March 5, 1998), 63 FR 12056 (March 12, 1998) ("Proposing Release").

⁸ As proposed, each broker-dealer would have been required to assert (i) whether it has developed written plans for preparing and testing its computer systems for potential Year 2000 Problems; (ii) whether the board of directors, or similar body, has approved these plans, and whether a member of the broker-dealer's board of directors, or similar body, is responsible for executing the plans; (iii) whether its Year 2000 remediation plans address all domestic and international operations, including the activities of its subsidiaries, affiliates, and divisions; (iv) whether it has assigned existing employees, hired new employees, or engaged third parties to execute its Year 2000 remediation plans; and (v) whether it has conducted internal and external testing of its Year 2000 solutions and whether the results of those tests indicate that the broker-dealer has modified its software to correct Year 2000 Problems.

⁹ This point was echoed by a number of other comment letters.

¹ The Proposing Release defined the term "Year 2000 Problem" to include any erroneous result caused by any computer software (i) incorrectly reading the date "01/01/00" or any year thereafter; (ii) incorrectly identifying a date in the year 1999 or any year thereafter; (iii) failing to detect that the Year 2000 is a leap year, and (iv) any other computer error that is directly or indirectly related to (i), (ii), or (iii) above.

² 17 CFR 240.17a-5.

³ 15 U.S.C 78a et seq.

⁴ Release No. 34-40162, (July 2, 1998) ("Adopting Release").

established criteria would likely result in significant variation in the examination procedures performed by independent public accountants and thus reduce the usefulness of the attestation reports. In addition, the AICPA expressed concern that the purpose and conclusions of the attestation report could be easily misunderstood. The AICPA was primarily concerned that uninformed users of the attestation reports would place undue reliance on them.

The AICPA suggested that an "agreed-upon procedures" engagement, instead of an attestation engagement, would more effectively meet the Commission's goals. Pursuant to such an engagement, a broker-dealer would engage an independent public accountant to perform and report on specific procedures designed to meet the Commission's objectives. This would eliminate the variability of examination procedures performed by independent public accountants and thus increase the consistency of the reports received by the Commission. The AICPA's letter outlined elements of an agreed-upon procedures report and offered to follow-up with the Commission staff regarding the development of specific procedures for a Year 2000 engagement.

In light of the above, the Commission has deferred consideration of the appropriate accountant's review of Part II of the second Form BD-Y2K that broker-dealers with a minimum net capital requirement of \$100,000 or greater will be required to file by April 30, 1999, reflecting the status of the broker-dealer's Year 2000 efforts as of March 15, 1999. Accordingly, the Commission is reopening the comment period to obtain additional views, including commentary on the feasibility and desirability of an agreed-upon procedures engagement. The public file (No. S7-7-98) contains the AICPA's comment letter received in the original comment period, the Commission's Initial Regulatory Flexibility Analysis, and will contain any subsequent letters submitted for the Commission's consideration.

Dated: July 2, 1998.

By the Commission.

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 240

[Release No. 34-40165; File No. S7-8-98]

RIN 3235-AH42

Year 2000 Readiness Reports To Be Made by Certain Transfer Agents

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule; request for additional comments.

SUMMARY: The Securities and Exchange Commission ("Commission") is reopening the comment period with respect to its proposal that would have required transfer agents to engage an independent public accountant to attest to specific assertions included in the transfer agent's report on Year 2000 compliance. The attestation by independent public accountants was one component of Rule 17Ad-18 under the Securities Exchange Act of 1934 proposed by the Commission in Release No. 34-39726, which was published in the **Federal Register** on March 12, 1998 (63 FR 12062).

DATES: Comments should be received on or before August 12, 1998.

ADDRESSES: Comments should be submitted in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission ("Commission"), 450 Fifth Street, NW, Washington, DC 20549. Comments also may be submitted electronically at the following E-mail address: rule-comments@sec.gov. Comment letters should refer to File No. S7-8-98; this file number should be included on the subject line if E-mail is used. All comments received will be available for public inspection and copying at the Commission's Public Reference Room, 450 Fifth Street, NW, Washington, DC 20549. Electronically submitted comment letters will be posted on the Commission's Internet web site (<http://www.sec.gov>).

FOR FURTHER INFORMATION CONTACT: Jerry W. Carpenter, Assistant Director, 202/942-4187; Thomas C. Etter, Jr., Special Counsel, 202/942-0178; or Jeffrey Mooney, Special Counsel, 202/942-4174, Division of Market Regulation, Securities and Exchange Commission, 450 Fifth Street, NW, Mail Stop 10-1, Washington, DC 20549.

SUPPLEMENTARY INFORMATION:

I. Introduction

At midnight on December 31, 1999, unless the proper modifications have been made, the program logic in many of the world's computer systems will

start to produce erroneous results because, among other things, the systems will incorrectly read the date "01/01/00" as being the year 1900 or another incorrect date. In addition, 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 millennium are entered into non-Year 2000 compliant programs.

The Commission views the Year 2000 problem as an extremely serious issue. A failure to assess properly the extent of the problem, remediate systems that are not Year 2000 compliant, and then test those systems could endanger the nation's capital markets and place at risk the assets of millions of investors. In light of this, both the transfer agent industry and the Commission are working hard to address the industry's Year 2000 problems.

In a companion release also issued today, the Commission is adopting Rule 17Ad-18¹ under the Securities Exchange Act² to require certain transfer agents to file reports with the Commission regarding Year 2000 compliance.³

II. Year 2000 Reporting Requirements

Rule 17Ad-18 requires new Form TA-Y2K to be filed by each transfer agents whose: (i) Appropriate regulatory agency, as that term is defined by 15 U.S.C. 78(c)(34)(B), is the Commission; but (ii) is not a savings association, as defined in Section 3 of the Federal Deposit Insurance Act, 12 U.S.C. 1813, which is regulated by the Office of Thrift Supervision. Part I of Form TA-Y2K is a check-the-box Year 2000 questionnaire. Each transfer agent that does not qualify for an exemption under Rule 17Ad-13(d)⁴ will also be required to file Part II of Form TA-Y2K, which requires a narrative discussion of its efforts to address Year 2000 Problems.

Generally, Form TA-Y2K requires each transfer agent to discuss the steps it has taken to address Year 2000 Problems. Each transfer agent is required, among other things, to (i) indicate whether its board of directors, or similar body, has approved and funded written Year 2000 remediation plans that address all mission critical computer systems; (ii) describe its Year 2000 staffing efforts; (iii) discuss its

¹ 17 CFR 240.17Ad-18.

² U.S.C. 78a *et seq.*

³ Release No. 34-XXXXX, (XXXX X, 1998), ("Adopting Release").

⁴ 17 CFR 240.17Ad-13(d). Generally, Rule 17Ad-13(d) exempts the following transfer agents from the rule's annual reporting requirements: issuer transfer agents, small transfer agents exempt under Rule 17Ad-4(b), and bank transfer agents.