NASD Notice to Members 97-16

NASD Updates Year 2000 Activities And Advises Members

Suggested Routing

- ■ Senior Management
- ☐ Advertising
- ☐ Corporate Finance
- ☐ Government Securities
- ☐ Institutional
- ■ Internal Audit
- ■ Legal & Compliance
- ☐ Municipal
- ☐ Mutual Fund
- ■ Operations
- ☐ Options
- ■ Registration
- ☐ Research
- ☐ Syndicate
- ■ Systems
- ■ Trading
- ☐ Training

Executive Summary

In 1996 there was an abundance of news and magazine articles, web pages, and special hearings in Congress designed to promote awareness of the Year 2000 (Y2K) challenge and to communicate information about the potential effect on computer systems brought about by the upcoming change in century. This trend is likely to continue in 1997 as businesses around the world work to ensure that automated processes with date-sensitive components will correctly identify "00" as 2000, rather than 1900, when the date changes to January 1, 2000.

The NASD® is committed to coordinating its efforts with the securities industry to meet the Y2K challenge. In early October 1996, NASD participated in the formation of the Y2K securities industry advisory group. Joining the NASD were representatives from the New York Stock Exchange (NYSE), the American Stock Exchange (AMEX), the National Securities Clearing Corporation (NSCC), the Depository Trust Company (DTC), and the Securities Industry Automation Corporation (SIAC). The purpose of the group was to establish inter-organizational data interchange guidelines and a plan for "street-wide" testing to ensure that exchanges, stock markets, clearing corporations, depositories, and securities firms perform data transfers and interfaces correctly when the millennium changes. Later, the group was expanded to include representatives from member firms, regional exchanges, and other similar organizations.

The NASD is continuing its work with the NYSE, AMEX, NSCC, DTC, SIAC, and member firms to establish an industry-wide Y2K test environment. It is envisioned that existing test facilities in the participating organizations will be connected in an integrated architecture to simulate an industry-wide production environment. This testing framework will allow members and "utility" organizations to test their data interfaces in an integrated manner. It will also facilitate the testing of securities transactions throughout their life cycle as they flow from one organization to the next (*e.g.*, a trade flows from a member firm to Nasdaq®/NASD, to NSCC, to DTC, and back again to the member firm). At this time, two committees have been established: a Steering Committee comprised of senior executives from the referenced organizations to provide overall guidance and support, and the Exchange and Utility Sub-Committee comprised of technology managers to develop technical and logistical details, and later, to oversee the day-to-day operations.

In addition, the NASD is participating in a number of other Y2K Committees formed by the Data Management Division of the Securities Industry Association, and is continuously communicating with other Y2K project teams in the industry to exchange ideas and relevant information.

NASD Regulation Year 2000 Compliance Project

In the July 1996 issue of *NASD Notices to Members*, it was announced that NASD had initiated an internal Y2K Compliance Project for the NASD and its subsidiaries, NASD Regulation, Inc., and The Nasdaq Stock Market, Inc. Subsequently, an Executive Steering Committee was established to oversee the project, facilitate communications throughout the NASD organization, and ensure that appropriate resources are available. The Executive Steering Committee is composed of three Executive Vice Presidents representing the three NASD entities and four Senior Vice Presidents/Vice Presidents representing Technology Services.

Phase 1 of the Project, Assessment and Planning, was completed in December. During that phase, the NASD accomplished the following: developed Y2K compliance standards for all new applications; amended its contracts to ensure all newly purchased hardware and software are Y2K compliant; inventoried all in-house developed applications and assessed the scope of the problem; did the same for computer and network hardware and off-the-shelf software; developed initial cost and effort estimates; developed an initial applications remediation plan; developed conversion methodology and testing guidelines; selected application analysis and conversion tools; and identified and began addressing legal issues related to Y2K.

In January 1997, the Project moved into Phase 2, Remediation, *i.e.*, conversion and/or testing of all NASD systems. This is a two-year effort that will extend through the end of 1998. In 1999 the Project will move into Phase 3, Monitoring, which will include the monitoring of all internal NASD systems through an entire business cycle, and performing "street-wide" (transaction life cycle) testing with members and other industry organizations (NSCC, DTC, NYSE, information vendors, etc.).

Year 2000 Member Readiness

The NASD strongly urges all its members, if they have not already done so, to initiate their own Y2K project. Every member has a responsibility to analyze the readiness of their internal computer systems for the Y2K challenge. In particular, *members who use automated programs to satisfy their regulatory and compliance responsibilities must ensure that those systems are able to function on and after January 1, 2000. Computer failures related to Y2K problems generally will be considered neither a defense to violations of firm's regulatory or compliance responsibilities nor a mitigation of sanctions for such violations. To that end, members must develop and implement an action plan to deal with any identified system coding changes required to achieve Y2K compliance. Also, members are urged to contact vendors of the software and hardware products they use to ensure they are addressing the Y2K issue. It is highly recommended that each firm accomplish all code changes by the end of 1998, so that 1999 can be used for monitoring the operations of all converted systems and performing quality assurance and interface tests with other organizations.*

Project Observations

So far, the NASD's Y2K Project has learned a few lessons worth sharing:

1. In preparation for the remediation phase, resources will be planned based on a schedule of the applications to be remediated and/or tested within a specific time period. It is important to recognize that the schedule will be revised whenever there is a valid business or technical reason to reschedule work on a particular application. Therefore, Y2K projects must anticipate that they will face a continuing challenge to: (1) maintain the pace of remediation activities and (2) anticipate changing resource demands as a result of the revisions to the work schedule.

2. Existing systems maintenance teams should have primary responsibility for code conversion because of their in-depth knowledge of the applications. Their knowledge will ensure that conversions are performed in the most efficient and effective manner. On the other hand, there should also be a strong Y2K central team to coordinate and monitor all Y2K activities, provide tools, contract resources, develop standards, and establish processes.

3. The Y2K arena resembles a minefield of hidden surprises. For example, contacting vendors for information about the Y2K compliance of their products and then verifying compliance will take much longer than anticipated. Constant and careful communications with suppliers is an absolute must because it is not unlikely that a vendor may reverse its position about whether it will or will not release a Y2K-compliant version of a particular product.

4. It is likely that unforeseen events will occur that may affect a Y2K project's ability to meet its January 1, 2000, deadline. Consequently, a contingency plan addressing possible "worst case scenarios" must be developed, preferably during the planning and assessment phase of the project.

Questions regarding these suggestions, the NASD's Y2K Project, or the Exchange and Utility Sub-Committee may be directed to Jack Samarias, Vice President, Office of Technology Services, at (301) 590-6633.