

AUDITOR OF STATE BULLETIN 98-010
NOVEMBER 16, 1998

TO: ALL COUNTY AUDITORS
ALL CITY AUDITORS, FINANCE DIRECTORS & TREASURERS
ALL VILLAGE FISCAL OFFICERS
ALL SCHOOL DISTRICT TREASURERS
ALL EDUCATIONAL SERVICE CENTER TREASURERS
ALL PUBLIC EMPLOYEE RETIREMENT SYSTEM FISCAL OFFICERS
ALL PUBLIC UNIVERSITY FISCAL OFFICERS
ALL COMMUNITY COLLEGE TREASURERS
ALL TECHNICAL COLLEGE DISTRICT TREASURERS
ALL TOWNSHIP CLERKS
ALL LIBRARY CLERKS/TREASURERS
ALL JOINT FIRE DISTRICT FISCAL OFFICERS
ALL JOINT RECREATION DISTRICT FISCAL OFFICERS
ALL JOINT ADAMH FISCAL OFFICERS
ALL JOINT AMBULANCE DISTRICT FISCAL OFFICERS
ALL JOINT AMBULANCE AND FIRE DISTRICT FISCAL OFFICERS
ALL UNION CEMETERY DISTRICT FISCAL OFFICERS
ALL DRAINAGE IMPROVEMENT DISTRICT FISCAL OFFICERS
ALL JOINT EMERGENCY MEDICAL DISTRICT FISCAL OFFICERS
ALL TOWNSHIP POLICE DISTRICT FISCAL OFFICERS
ALL TOWNSHIP FIRE DISTRICT FISCAL OFFICERS
ALL TRANSIT AUTHORITY FISCAL OFFICERS
ALL PORT AUTHORITY FISCAL OFFICERS
ALL METROPOLITAN HOUSING AUTHORITY FISCAL OFFICERS
ALL AIRPORT AUTHORITY FISCAL OFFICERS
ALL HOSPITAL FISCAL OFFICERS
ALL TOWNSHIP ROAD DISTRICT FISCAL OFFICERS
ALL WATER AND SEWER DISTRICT FISCAL OFFICERS
ALL TOWNSHIP WASTE DISPOSAL DISTRICT FISCAL OFFICERS
ALL INDEPENDENT PUBLIC ACCOUNTANTS

SUBJECT: FINANCIAL STATEMENT DISCLOSURES - YEAR 2000 ISSUE

The purpose of this Bulletin is to provide financial statement preparers and auditors with information on the recent pronouncements related to the "Year 2000" (Y2K) problem by the Governmental Accounting Standards Board (GASB), American Institute of Certified Public Accountants (AICPA), and U.S. Securities and Exchange Commission (SEC).

☛ *The Auditor of State has determined that these pronouncements will apply equally to entities that prepare statements in accordance with generally accepted accounting principles and other comprehensive bases of accounting, including the **cash**-basis of accounting.*

☛ **Independent public accountants note** - financial statements for which audit reports are dated on or after November 1, 1998 must contain one of the following:

- the disclosures required by GASB TB 98-1;
- a qualified auditor's report indicating that the required disclosures were omitted by the government.

If for some reason the disclosures do not apply to the entity (as determined by the client and agreed to by the IPA), a statement to that effect by the IPA should be made in a separate letter upon submission of reports to the Auditor of State for review. Reports will be returned for reissuance if these requirements are not met.¹

Background - Significance of the Year 2000 Issue

As recently noted by the U.S. Securities and Exchange Commission²:

As the end of this century nears, there is worldwide concern that Year 2000 technology problems may wreak havoc on global economies. No country, government, business, or person is immune from the potential far-reaching effects of Year 2000 problems. [The] President ...recently stated that "all told, the worldwide cost will run into the tens, perhaps the hundreds of billions of dollars, and that's the cost of fixing the problem, not the cost if something actually goes wrong." Some estimates that include not only software and hardware costs, but also costs related to business interruptions, litigation, and liability, run in the hundreds of billions of dollars.

Only one thing is certain about the impact of the Year 2000 -- it is difficult to predict with certainty what truly will happen after December 31, 1999. To reduce the impact of this potentially serious, widespread problem, many public officials and private commentators have spoken out about the need to plan properly now.

The problem is caused by computer systems and embedded computer chips that use two-digit representations for the year part of date fields ("6/30/99" for June 30, 1999, for example). Besides financial systems and mainframe computers, "Y2K" problems can disable personal computers, operating systems, and other equipment.

The GASB, AICPA, and SEC have considered what responses preparers and auditors of governmental financial statements should make to this problem:

¹ Certain members and staff of the Auditing Standards Board of the American Institute of Certified Public Accountants have issued a document entitled *AICPA ILLUSTRATIVE REPORTING GUIDANCE ON YEAR 2000 DISCLOSURES MADE UNDER GASB TB 98-1*. This document provides sample language independent auditors may wish to use in their reports on governmental financial statements. Independent public accountants' reports which substantially conform with these illustrations will be accepted by the Auditor of State.

² SEC Release #s 33-7558 & 34-40277

- ❑ The GASB now requires certain additional financial statement disclosures.
- ❑ The AICPA has issued guidance for evaluating if the auditor must modify the report on the financial statements.
- ❑ The SEC has issued guidance for disclosures by governmental securities issuers.

Each of these is discussed below.

GASB Technical Bulletin 98-1

GASB TB 98-1³ requires that governments describe their “Y2K” issues, and any “significant resources committed - contracted amounts at the end of the government’s reporting period - to make (“mission-critical”) computer systems and other equipment year 2000 compliant”.

The GASB TB also requires that the “stage of work” on the government’s Y2K project(s) be disclosed. The following stages of work for disclosures concerning the Y2K problem for mission-critical systems have been identified:

▶ Awareness

This stage encompasses establishing a budget and project plan for dealing with the Y2K issue.

▶ Assessment

This stage is when the government identifies all of its systems and individual components of the systems. In this stage, at least all “mission-critical” systems (systems and equipment critical to conducting governmental operations) should be identified.⁴

▶ Remediation⁵

In this stage, the government makes the changes to the systems and equipment.

▶ Validation/Testing

³ GASB Technical Bulletin 98-1, effective for financial statements on which the auditor’s report is dated after October 31, 1998. The TB can be purchased from the GASB, and also may be obtained from the GASB Web site at “www.gasb.org”.

⁴ In this stage, it may be possible to identify that the system reasonably could be considered to be Y2K compliant.

⁵ It is possible for a mission-critical system to be considered in the remediation stage, even though one or more of the components of that system may be having unit testing.

In this stage, the government validates and tests the changes made during conversion or upgrading of the systems and equipment. If errors occur, further changes are made.

The stages were adopted from the U.S. Securities and Exchange Commission Division of Market Regulation Year 2000 Work Program (January, 1998).

Guidance for determining the stages of the Year 2000 project

It is management's responsibility to both assess and remediate any Year 2000 issues the government may have and to develop the disclosures required by GASB TB 98-1. Attached as Appendix B to this Bulletin are guidelines developed by the Auditor of State to assist governments with both of these responsibilities. Appendix B provides considerations for management and auditors to determine what mission-critical systems might need to be assessed. In general, management should look at mission-critical:

- ✓ Software applications, including significant sub-applications (e.g., the Financial Accounting Software, which in turn has a general ledger subsystem, a payroll subsystem, a purchasing subsystem, and a revenue subsystem)⁶;
- ✓ System software (e.g., Windows, DEC VMS, UNIX, MVS, DOS, etc);
- ✓ Hardware; and
- ✓ Embedded chips.

The Auditor of State's Sample Disclosures

In addition to performing Y2K assessments, remediation, and testing, governments should prepare the disclosures about:

- ▶ the stages of work in process or completed as of the end of the government's reporting period to make computer systems and other electronic equipment year 2000 compliant; and the
- ▶ committed resources.

A *sample* set of disclosures developed by the Auditor of State is attached to this Bulletin as Appendix A. Notes specific to the government's particular situation(s) should be developed by management and submitted to the auditors in a timely fashion for review.

⁶ This category also includes PC end-user software. This would include Groupwise, Quattro Pro, Excel, Microsoft Word, Word Perfect etc. For those vendor applications, it's just a matter of the software's ability to retain a 4 digit year.

These sample notes to the financial statements encompass 3 major situations:

- ▶ Where a government uses outside vendors (“off-the-shelf” software);
- ▶ Where a government uses an outside service organization; and
- ▶ Where a government uses in-house staff for all or most of its significant Y2K impacted operations.

A recent SEC report notes:

[I]t is not, and will not, be possible for (a government) to represent that it has achieved complete Year 2000 compliance and thus to guarantee its remediation efforts.

• *Disclosures related to Y2K therefore should not claim that the entity is Year 2000 compliant, and auditors should not attest to such a claim, either in their audit reports or in the related working papers. If individual systems reasonably are deemed to be compliant, then factual statements to that effect may be made, e.g.:*

All mission-critical systems have been remediated and tested for Year 2000 compliance.

The City engaged MiDi Engineering to assess the Year 2000 compliancy of mission-critical building efficiency systems. The vendor’s report indicates that these systems are compliant.

The City uses a general ledger software package developed by ICU Com. ICU has certified to the City that this package is Year 2000 compliant.

The Auditor of State requires the Year 2000 note to contain the following disclaimer language:

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]’s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

If this language is omitted, the note should be marked as “unaudited”; the Auditor of State will express a qualified opinion on the financial statements.

Other auditing considerations

Auditing standards currently require auditors to determine if disclosures in the financial statements are reasonably adequate. The Auditor of State has developed an audit program designed to validate management’s assertions about the various disclosures required by GASB TB 98-1. Management should

document :

- ▶ the stages of work in process or completed as of the end of the government’s reporting period to make its computer systems and other electronic equipment critical to operations year 2000 compliant; and the
- ▶ committed resources.

If any other disclosures are made beyond the TB 98-1 requirements, adequate documentation supporting these disclosures also should be available for the auditors’ inspection.

The GASB TB 98-1 disclosures should be adequate to inform the reader of the financial statements of the potential impact of Y2K issues on the level of service that can be provided by the government and its ability to meet its obligations as they come due. Disclosures may be general, and systems and related subsystems can be aggregated for purposes of these disclosures.

If (in the auditor’s opinion) those disclosures are *not* adequate, the auditor is to modify the opinion on the financial statements.

In addition, certain other auditing standards require auditors to comment on internal control weaknesses identified in the audit. The Auditor of State has adopted the following guidelines we will follow in determining under what circumstances the audit reports will be modified and\or internal control comments will be made for Y2K deficiencies other than inadequate disclosure:^{7 8}:

<i>Opinion</i>	<i>Management Letter/ Internal Control Report</i>	<i>Auditor’s Opinion dated prior to January 1, 1999</i>	<i>Auditor’s Opinion dated on or after January 1, 1999</i>
Unqualified	None	Mission critical systems believed to be year 2000 compliant	Mission critical systems believed to be year 2000 compliant
Unqualified	Management letter	Unit in remediation stage with mission critical systems not year 2000 compliant but reasonably expected to be year 2000 compliant	Unit in testing/validation stage with mission critical systems not year 2000 compliant but reasonably expected to be year 2000 compliant

⁷ If the entity has a viable contingency plan, generally the auditor will not need to modify the audit opinions or issue reportable conditions/material weaknesses.

⁸ Expectations and beliefs in this table are those of the auditor after evaluating the entity’s documentation.

<i>Opinion</i>	<i>Management Letter/ Internal Control Report</i>	<i>Auditor's Opinion dated prior to January 1, 1999</i>	<i>Auditor's Opinion dated on or after January 1, 1999</i>
Unqualified	Reportable condition	Unit in remediation stage with mission critical systems that are reasonably possible will not be year 2000 compliant	Unit in testing/validation stage with mission critical systems that are reasonably possible will not be year 2000 compliant
Unqualified	Material weakness	Unit in assessment stage with mission critical systems that are reasonably possible will not be year 2000 compliant	Unit in remediation stage with mission critical systems that are reasonably possible will not be year 2000 compliant
Emphasis of matter modification	Material weakness	Unit not in assessment stage	Unit in remediation stage with mission critical systems that have probability not to be year 2000 compliant
Going concern modification	Material weakness	Unit not in awareness stage, probability that year 2000 compliance cannot be met based on auditor knowledge of multiple systems such that critical mission cannot be accomplished or that financial integrity is compromised.	Unit not in awareness stage with mission critical systems Unit not in awareness stage, probability that year 2000 compliance cannot be met based on auditor knowledge of multiple systems such that critical mission cannot be accomplished or that financial integrity is compromised.

Updating the Disclosures

The GASB TB 98-1 disclosures are required to be made as of the government's fiscal year end. If the government wants to update the information to some later date close to the end of the auditor's planned field-work completion date, arrangements should be made between the government and the auditors at the start of the audit so the work necessary to examine the assertions in the note can be performed in a timely and effective manner.

We understand that the Government Finance Officers' Association Certificate of Excellence Program will not deny a certificate to an entity which receives a qualified auditor's report for a scope limitation in relation to the entity's Y2K note; the Certificate will be affected only if the entity receives a qualified auditor's report for not disclosing its Y2K issues in conformity with GASB TB 98-1. You may wish to contact the GFOA Certificate program if you have any questions about this matter.

AICPA Guidance

The AICPA has issued guidance to auditors⁹ for evaluating if a government has sufficiently considered whether Y2K conditions and events cause substantial doubt about a government's ability to continue to function starting in the year 2000. A government usually is thought of as enjoying a life in perpetuity, however, it still might not be a "going concern" as defined in AICPA standards.

If an auditor believes there are potentially significant adverse effects from the Y2K problem, the auditor considers management's plans for dealing with it. If the auditor concludes that substantial doubt about the government's viability as a "going concern" is not alleviated, the auditor will report that conclusion in an "explanatory paragraph" in the auditor's report on the financial statements.

Further, if the auditor concludes that the government's financial statement *disclosures* relating to the issue are not adequate, then a qualified or adverse opinion because of a GAAP departure on those financial statements might be issued.

SEC Requirements

Governments that issue debt that is traded on public exchanges (known as "municipal" securities even if issued by entities that are not municipalities) are subject to the SEC's "anti-fraud" provisions. As noted in the SEC Releases:

The Securities and Exchange Commission... is publishing guidance for... municipal securities issuers regarding their disclosure obligations about Year 2000 issues.... [W]e remind municipal securities issuers...that the anti-fraud provisions of the federal securities laws apply to disclosure about the Year 2000 issue.

Attached as Appendix C to this Bulletin are excerpts from the SEC's Release¹⁰ concerning "municipal" securities issuances and disclosures. The SEC notes:

Municipal securities issuers, like other organizations, have Year 2000 issues. Year 2000 problems may affect their operations, creditworthiness, and ability to make timely payment on their indebtedness. We

⁹ Interpretation of SAS 59, AU § 9341, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*

¹⁰ SEC Release #s 33-7558 & 34-40277

[i.e., the SEC] encourage municipal securities issuers and persons who assist in preparing their disclosure documents to consider whether Year 2000 issues may be material to investors. If material, the disclosure documents used by municipal issuers should contain a discussion of Year 2000 issues to avoid misleading statements or omissions that could violate the anti-fraud provisions.

Year 2000 issues should be considered in preparing all disclosure documents, whether in the context of an official statement, continuing disclosure provided in compliance with a disclosure covenant, or other information that is reasonably expected to reach investors and the trading markets.

The “disclosure documents” are not further defined in the SEC Release. However, the Auditor of State believes that governments should follow the SEC’s Y2K disclosure requirements in at least the following situations involving publicly traded debt:

- Upon initial issuance (usually in the form of an Official Statement); and
- For disclosures to the NRMSIRs and the SID.¹¹

It is unknown if the SEC release is intended to apply to regular financial statement disclosures in the context of “...other information that is reasonably expected to reach investors and the trading markets.” Governments with significant debt to be issued or outstanding should contact their bond/legal counsel for advice on complying with this SEC release. The Auditor of State will not provide advice on these matters.

The SEC disclosures generally are not subject to audit. If, however, the government’s bond/legal counsel advises the government to disclose the information in the government’s financial statements, then contact your auditor. *The Auditor of State generally will not provide audit assurance on this information and will require any SEC Release disclosures in the financial statements to be marked “unaudited”.*

*

Governmental entities should note that these new requirements, some of which require audit corroboration, may result in increased auditing fees. Auditor of State regional offices, and independent public accounting firms with the approval of the Auditor, will estimate the additional fees for performing this work and issue a revised engagement memorandum as necessary.

If you have any questions about this bulletin, please contact Accounting & Auditing Support at (800) 282-0370.

¹¹ For a discussion of these requirements, see the Auditor of State’s *Ohio Compliance Supplement (3/98)*, Compliance Requirement 3-5.

Appendix A

Sample Year 2000 Disclosures

- ❑ The Auditor of State of Ohio has prepared the following *Sample Y2K Financial Statement Notes*. This guidance represents the views of the Auditor of State of Ohio. While these Sample Notes have been reviewed and commented upon by certain members of the GASB staff, they have not been approved, disapproved, or otherwise acted upon by the GASB.
- ❑ Comments in **bold** illustrate GASB TB 98-1 minimum disclosures. Comments in regular, non-bold, typeface are not necessary to comply with the Technical Bulletin, but might serve as additional useful information.
- ❑ GASB staff has suggested to the Auditor of State that the following paragraph, or something similar, be added to the required disclosures:

“The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government’s operations as early as fiscal 1999.”

- ❑ Certain members and staff of the Auditing Standards Board of the American Institute of Certified Public Accountants have issued a document entitled *AICPA ILLUSTRATIVE REPORTING GUIDANCE ON YEAR 2000 DISCLOSURES MADE UNDER GASB TB 98-1*. This document illustrates disclosures independent auditors may wish to make in their reports on governmental financial statements. The Auditor of State has adopted, and modified, a portion of these suggested disclosures in the Sample Y2K Financial Statement Notes, as follows:

“Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]’s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.”

Example 1

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government’s operations as early as fiscal 1999.

Harrison Township has completed an inventory of computer systems and other equipment necessary to conducting Township operations. Based on this inventory, the Township is in the remediation stage in that bid specifications have been drawn up to purchase, from outside vendors, hardware and software believed

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to be year 2000 compliant **for the financial reporting systems; contracts totaling \$460,000 have been let as of December 31, 1998. Testing and validation of the systems will need to be completed** after the hardware and software are installed.

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]'s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Example 2

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government's operations as early as fiscal 1999.

Grant Township has completed an inventory of computer systems and other electronic equipment necessary to conducting Township operations:

- # The Township leases the Auditor of State's Uniform Accounting Network (UAN) system for its financial operations. The Auditor of State is responsible for remediating these systems and is solely responsible for any costs associated with this project.
- # Tax collection for the Township is handled by Buchanan County. The County is responsible for remediating this system, and is solely responsible for any costs associated with this project.
- # **The Township also owns a building with efficient power¹², heating, and air-conditioning systems. An external vendor was engaged to remediate the efficiency systems. The vendor has tested and validated these systems.**

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]'s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

¹² In this sample note, it is assumed that the entity has decided that a failure of the power systems could have a sufficiently significant effect on operations that it is necessary for it to be discussed; information on the heating and air conditioning systems probably is not necessary, but it can be disclosed if the entity wishes to.

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Example 3

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government's operations as early as fiscal 1999.

Harding Township has not inventoried computer systems and other equipment necessary to conducting Township operations. It is unknown as of June 30, 1998, what effects, if any, failing to remediate any such systems will have upon Township operations and financial reporting.

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]'s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Example 4a

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government's operations as early as fiscal 1999.

McKinley City has completed an inventory of computer systems and other equipment necessary to conducting City operations. The City has identified the following systems requiring year 2000 remediation:

- ***Financial reporting, tax collection, payroll and employee benefit systems.*** The City is currently remediating its financial reporting, tax collection, payroll and employee benefit systems. Validation and testing of these systems have yet to be completed. Remaining contracted amounts of \$700,000 are committed to this project as of December 31, 1998.
- ***A 911 police and fire emergency reporting system.*** The City has completed all testing and validation on its portion of the 911 police and fire reporting system. The 911 police and fire reporting system has data interchanges with several other such systems, some of which have not been tested and validated.
- ***A traffic control system.*** A vendor is currently remediating the traffic control system. Validation and testing of this system have yet to be completed. Remaining contracted amounts of \$325,000 are committed to this project as of December 31, 1998.

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- ***An electrical distribution system.*** Another vendor is remediating the electrical distribution system. Validation and testing of portions of this system have also been completed, however, validation and testing of certain parts of the system have yet to be completed. Remaining contracted amounts of \$1.2 million are committed to this project as of December 31, 1998. The electrical distribution system purchases electricity from a commercial supplier which is responsible for remediating the wholesale power system and is solely responsible for any costs associated with this project.
- ***A municipal hospital.*** The municipal hospital is operated by a component unit which reports all of its computer systems and other electronic equipment critical to conducting operations have been tested and validated.
- **The City has completed testing and validation on all electronic equipment it identified as necessary to conducting City operations.**

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]'s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Example 4b (tabular format)

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government's operations as early as fiscal 1999.

McKinley City has completed an inventory of computer systems and other equipment necessary to conducting City operations. The City has identified the following systems requiring year 2000 remediation:

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<i>Systems</i> <i>Completed</i>	Awareness	Assessment	Remediation	Validation & Testing	Contracted Amounts as of 12/31/98
	C	C	C	C	
<i>Financial reporting, tax collection, payroll and employee benefit systems</i>		✓			\$700,000
<i>911 police and fire emergency reporting system</i>				✓ ¹³	
<i>Traffic control system</i>		✓			\$325,000
<i>Electrical distribution system</i>		✓			\$1.2 million
<i>Electronic equipment identified as necessary to conducting City operations.</i>				✓	

¹³

The 911 police and fire reporting system has data interchanges with several other such systems, some of which have not been tested and validated.

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Sample Year 2000 Disclosures

<i>Systems</i>	Awareness	Assessment	Remediation	Validation & Testing	Contracted Amounts as of 12/31/98
<i>Completed</i>	C	C	C	C	
<i>Municipal hospital</i>				✓ ¹⁴	

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]'s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Example 4c - Client has updated the note to a current period

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government's operations as early as fiscal 1999.

McKinley City has completed an inventory of computer systems and other equipment necessary to conducting City operations. The City has identified the following systems requiring year 2000 remediation:

- ***Financial reporting, tax collection, payroll and employee benefit systems. The City is currently remediating its financial reporting, tax collection, payroll and employee benefit systems. Validation and testing of these systems were yet to be completed as of December 31, 1998; however, validation and testing was completed July 20, 1999. Remaining contracted amounts of \$700,000 were committed to this project as of December 31, 1998; this amount was spent by July***

¹⁴

The municipal hospital is operated by a component unit which reports all of its computer systems and other electronic equipment critical to conducting operations systems have been tested and validated.

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20, 1999.

- ***A 911 police and fire emergency reporting system.*** The City has completed all testing and validation on its portion of the 911 police and fire reporting system. The 911 police and fire reporting system has data interchanges with several other such systems, some of which had not been tested and validated as of December 31, 1998. As of July 20, 1999, these systems remain to be tested and validated.
- ***A traffic control system.*** A vendor was remediating the traffic control system at December 31, 1998; validation and testing of this system were yet to be completed as of December 31, 1998. Remaining contracted amounts of \$325,000 were committed to this project as of December 31, 1998. As of July 20, 1999, remediation of this system was completed and testing and validation were in process.
- ***An electrical distribution system.*** Another vendor is remediating the electrical distribution system. Validation and testing of portions of this system have also been completed, however, validation and testing of certain parts of the system have yet to be completed. Remaining contracted amounts of \$1.2 million are committed to this project as of December 31, 1998. The electrical distribution system purchases electricity from a commercial supplier which is responsible for remediating the wholesale power system and is solely responsible for any costs associated with this project.
- ***A municipal hospital.*** The municipal hospital is operated by a component unit which reports all of its computer systems and other electronic equipment critical to conducting operations have been tested and validated.
- **The City has completed testing and validation on all electronic equipment it identified as necessary to conducting City operations.**

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]'s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Example 4d - component unit has differing system

(Rest of sample note 4 except the discussion of the hospital is the same as one of the above. Hospital component unit is as follows):

A municipal hospital. The municipal hospital is operated by a component unit. The Hospital has identified the following systems requiring year 2000 remediation: *financial reporting, payroll and*

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employee benefit systems. **The Hospital is currently remediating these systems. Validation and testing of these systems were yet to be completed as of December 31, 1998;** however, validation and testing were completed June 15, 1999. **Remaining contracted amounts of \$250,000 were committed to this project as of December 31, 1998;** this amount was spent by June 15, 1999.

Example 5

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government's operations as early as fiscal 1999.

Hayes County has completed an inventory of computer systems and other equipment necessary to conducting County operations. The County has identified the following systems requiring year 2000 remediation:

- G The County has a financial reporting and tax collection system.** The County currently uses in-house staff for both of these systems. **Staff is developing a new financial reporting system and is mainly in the remediation phase of the project, however, certain subsystems, such as utility billing, are being tested and validated. The County currently has contracted with a vendor who is performing remediation work on the tax collection system. Testing and validation have yet to be completed for the tax collection system.**

- G The County also operates a regional 911 reporting system for police and fire emergencies and a water system serving unincorporated areas within the county. The County currently is assessing the need for system changes in its regional 911 police and fire reporting system and water distribution system. Some remediation is occurring during the assessment of these systems. Additional remediation is anticipated in these systems after completion of assessment. Testing and validation will occur after remediation of these systems is completed.**

Remaining contracted amounts of \$2.05 million are committed to this project as of December 31, 1998.

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]'s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Example 6

Note 10 - Year 2000 Issue

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The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government's operations as early as fiscal 1999.

Garfield County has completed an inventory of computer systems and other equipment necessary to conducting County operations. The County has identified the following systems requiring year 2000 remediation:

- **The County has a financial reporting system and a tax collection system. All testing and validation of the financial reporting system currently being used by the county has been completed. The County has developed a new tax collection system which has been tested and validated.**

- **The County also operates a regional 911 reporting system for police and fire emergencies and a water system serving unincorporated areas within the county. The County currently has completed assessing the need for system changes in its regional 911 police and fire reporting system. Some remediation is occurring during the assessments of this system. The County is in the remediation stage with respect to its water distribution system. However, as of December 31, 1998, the County has been unable to find electronic replacement chips which are year 2000 compliant for its system.**

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]'s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Example 7

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government's operations as early as fiscal 1999.

Tyler School District has completed an inventory of computer systems and other equipment necessary to conducting District operations and has identified such systems as being financial reporting, payroll, and grant reporting.

- ▶ **The financial reporting system has been assessed, remediated, and tested and validated.**

- ▶ **The payroll system is currently being remediated by a vendor. Testing and validation will have**

Appendix A

Sample Year 2000 Disclosures

to occur prior to the system being used for payroll processing.

- ▶ **The District's grant reporting system, including federal and state grants, currently is being assessed.**¹⁵

Tyler County collects property taxes for distribution to the Tyler School District. Tyler County is responsible for remediating the tax collection system.

The State of Ohio distributes a substantial sum of money to the District in the form of "Foundation" and federal and state grants payments. Further, the State processes a significant amount of financial and non-financial information about the District through the State's Education Management and Information System (EMIS). The State is responsible for remediating these systems.

Remaining contracted amounts of \$40,000 are committed to this project as of December 31, 1998.

The County is solely responsible for any costs associated with the tax collection system project. The State is solely responsible for any costs associated with the Foundation processing and EMIS systems.

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]'s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Example 8

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government's operations as early as fiscal 1999.

Polk School District has completed an inventory of computer systems and other equipment necessary to conducting District operations and has identified such systems as being financial reporting, payroll and employee benefits, and educational statistics reporting (through the State's Education Management and Information System (EMIS)). The District has seven school buildings with power systems which have extensive efficiency utilization measures within the systems.

¹⁵ The federal Office of Management and Budget has requested that all recipients and subrecipients of federal funding notify their grantor agencies if they anticipate Y2K issues that could significantly affect the grantee's ability to process grant transactions and prepare accurate required grant reports.

Appendix A

Sample Year 2000 Disclosures

The District uses the State of Ohio Uniform School Accounting System software for its financial reporting, and the State of Ohio Uniform Staff Payroll System software for its payroll and employee benefits. The State is responsible for remediating these systems.

The State of Ohio distributes a substantial sum of money to the District in the form of “Foundation” and federal and state grant payments. Further, the State processes a significant amount of financial and non-financial information about the District through EMIS. The State is responsible for remediating these systems.

The School District currently is assessing the changes needed in the power systems. Systems may have to be remediated, and tested and validated.

The Polk School District has contracted with outside vendors for \$720,000 for assessment, remediation, purchases, and testing and validation, all of which remains committed as of the end of the fiscal year.

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]’s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Example 9

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government’s operations as early as fiscal 1999.

Taylor School District has completed an inventory of computer systems and other equipment necessary to conducting District operations and has identified such systems as being financial reporting, payroll and employee benefits. The District has seven school buildings with power systems which have extensive efficiency utilization measures within the systems.

The financial reporting system has been assessed, remediated and tested and validated.

The District utilizes an external service organization for its payroll and employee benefit system. The external service organization is responsible for remediating these systems. The external service organization reports that it is doubtful that the payroll and employee benefit system can be remediated prior to December 1999 and the external service organization currently is negotiating to merge with another service organization.

Taylor County collects property taxes for distribution to the District. Taylor County is responsible for

Appendix A

Sample Year 2000 Disclosures

remediating its tax collection system.

The State of Ohio distributes a substantial sum of money to the District in the form of “Foundation” and federal and state grant payments. Further, the State processes a significant amount of financial and non-financial information about the District through EMIS. The State is responsible for remediating these systems.

The District has completed assessing the changes needed in the power systems. Four buildings contained systems for which the District plans no changes. Two other buildings were found to require remediation which is currently under way; testing and validation will follow. One building was found to require remediation but the original vendor for the electronic chips is out of business. A vendor currently is attempting to remediate the systems in this building to accept new electronic chips for controls.

Remaining contracted amounts of \$980,000 are committed to this project as of December 31, 1998.

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]’s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Example 10

Note 10 - Year 2000 Issue

The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government’s operations as early as fiscal 1999.

Fillmore County has identified 13 computer systems and other equipment necessary to conducting County operations. All of these systems and equipment except for financial accounting and reporting are in the remediation phase; those 12 systems must still be tested and validated. The financial accounting and reporting system is in the validation\testing phase. All of the systems are to be remediated by in-house staff, therefore there are no outside contracted amounts for this project as of December 31, 1998.

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]’s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready.

Appendix A
Sample Year 2000 Disclosures

Appendix B
Auditor of State of Ohio
Year 2000 Analysis Program & Disclosure Checklist

Directions for Completion

1. Complete **Part 1-- Mission-Critical¹⁶ Systems and Equipment**. This should list automated systems and other equipment (e.g., embedded chips), the failures of which would significantly adversely affect a government's financial reporting, ability to collect material revenue sources or make disbursements, provide mission-critical services or continue operation as a going concern. Consider the following criteria in classifying a system or equipment as "mission critical" :

a.) Would the improper operation of the system or equipment *significantly* affect the delivery of essential consumer services or public safety?

For example, the improper operation of certain hospital equipment could cause injury or even death to some patients. Improper record keeping at prisons could cause dangerous felons to be released, or could even "open the doors" of the prison, allowing escapes. The failure of communications equipment could prevent police or fire departments from responding to emergencies. Conversely, the failure of traffic signals to operate in a small village would be an inconvenience, but might not significantly affect public safety.

b.) Would the improper operation of the system or equipment *significantly* affect a government's ability to generate material revenue sources or make payments when due?

For example, the failure of embedded chips at a water system may prevent water from being pumped. Beyond being an essential public service (and a public safety factor), the water utility would have no services to bill and no revenue. A failure to pay bonded debt when due could result in events of default, requiring acceleration of scheduled payments. Conversely, an inability to collect cash for dog licenses might affect appropriations for animal control, but might not be material to a county as a whole.

2. Complete **Part 1(b)-- External organizations providing critical functions**— This section should document entities *outside* the primary government that provide services that directly affect the primary government's ability to fulfill its mission or process revenue or payment transactions. Examples of external entities providing critical functions include:

–Virtually all governments have a financial institution that processes deposits (often including EFTs) and checking account transactions. A Y2K failure on its part would disrupt the government's ability to collect revenue and make payments.

– Service organizations may similarly affect the ability to process certain accounting transactions.

¹⁶ GASB TB 98-1 uses the term "necessary for the continued and uninterrupted operations of a government"; for the purpose of this checklist, these terms are synonymous.

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- The failure of the county that bills, collects and remits property taxes to the government client could materially affect revenue.

- The failure of the entity that collects and remits income taxes to the government client could materially affect revenue.

- Y2K issues adversely affecting state agencies that, for example, pass through material federal financial assistance could affect the program.

- Other entities with automated systems or equipment that provide critical services.

3. Append an addendum to the Summary which briefly documents support for Part 1 conclusions (i.e., why management determined that certain systems/equipment were or were not mission critical).

4. For each mission-critical system and equipment identified in Part 1, complete a copy of **Part 2-- Documentation of Other GTB 98-1 Stages:**

GASB Technical Bulletin 98-1 requires classifying the entity's mission-critical systems and equipment into one of four stages: (1) awareness, (2) assessment, (3) remediation, and/or (4) validation/testing. In determining the stage of work, note that an entity could have differing assessments for different systems. For example, an entity could be in the "validation/testing" stage for accounting-related systems, but be in the "remediation stage" for its 911 emergency system. Since the disclosure should address the stage for each mission-critical system, you should complete a separate part 2 for all mission critical systems and equipment identified in part 1.

Begin by completing the steps for the stage management believes the entity is in. For example, if the entity system is in the remediation stage, complete only the remediation stage steps. In this example, completing the assessment stage for that system would not be needed, unless results from completing the remediation stage suggest that the system does not meet the remediation stage classification.

The completed Part 2 provides support for disclosure of the state of completion for that system.

5. Complete **Part 3 -- Required GTB 98-1 Disclosures.**

The GASB TB 98-1 disclosures are required to be made as of the government's fiscal year end. If the government wants to update the information to some later date close to the end of the auditor's planned field-work completion date, arrangements should be made between the government and the auditors at the start of the audit so the work necessary to examine the assertions in the note can be performed in a timely and effective manner.

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Going Concern Considerations

Judgment is required in determining whether a likely failure to achieve Y2K remediation requires a “going concern” consideration. Consider the following:

- 1) Would a Y2K failure materially affect the entity’s ability to collect revenue or pay bills?

Such evaluation should consider the entity’s contingency plans. For example, if an automated billing system failed, could the entity generate bills manually?

An inability to make payments could result from (1) a lack of financial resources or (2) an inability to process payments.

- 2) Would an inability to provide basic services or assure public safety likely result in severe adverse consequences?

For example, the failure of a 911 system could result in death or injury to citizens. We should consider the likelihood of litigation from such deaths or injury and the probability that a materially unfavorable outcome of litigation would result in severe adverse consequences? However, if legal counsel advised us that the entity would prevail against claims of negligence, it is unlikely that the substantial doubt about the entity’s ability to continue as a going concern criteria would be met.

Effective Date

GTB 98 -1 disclosures apply to financial statements with audit opinions dated after October 31, 1998, and terminate for financial statement periods ending after December 31, 1999, unless mission-critical systems and other equipment are not year 2000-compliant as of the balance sheet date.

“Best Practices”

The Auditor of State has compiled a listing of “best practices” to help Ohio governments address the Year 2000 computer problem. Potential policies, procedures and techniques are listed in the appropriate sections below.

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**Part 1a, Mission-Critical Systems and Equipment
Summary**

Systems & Equipment	Does the entity operate, use, or contract for this?	Significant to conducting critical operations? **	Significant to collecting revenue or making payments? **	Person Responsible for Assuring Risk Remediation
1). All systems and hardware and software related to the following financial applications :				
— Accounting & financial reporting systems.				
— Systems used to summarize budget vs. actual activity (are often integrated into the accounting & financial reporting system described above).				
— Payroll				
— Billing & collection systems for utilities, taxes and other revenue sources.				
— Grant accounting & reporting systems.				
—Other financially significant applications.				
— Systems used to record payment & eligibility information for human services programs.				
— Systems used by courts to record & allocate receipts, disbursements, case records.				
2). Utilities, such as water, sewer and electric.				
3). Telecommunications systems (including police and fire 911 systems, radio systems, burglar and fire reporting).				
4). Traffic control.				

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Systems & Equipment	Does the entity operate, use, or contract for this?	Significant to conducting critical operations? **	Significant to collecting revenue or making payments? **	Person Responsible for Assuring Risk Remediation
5).Transportation (bus, subway, handicap movement)				
6). Systems used for building operations (leased or operated), including security systems, heating/air conditioning, etc. The entity should consider these matters for each significant building it owns or operates:				
-- Administrative / office buildings				
-- Medical facilities				
-- Courts				
-- Prisons				
-- Other				
7). Component Units				

** Note: A “yes” answer to **either** “significant to conducting critical operations?” or “significant to collecting revenue or making payments?” should result in classifying the system or equipment as mission critical. For each of the above services the government operates, append a brief summary supporting the conclusions above (i.e., why the service is or is not significant to its critical operations, collecting revenue or making payments).

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Part 1(b), Mission-Critical Systems and Equipment
Summary– External Entities

Systems & Equipment	Does the entity operate, use, or contract for this?	Significant to conducting critical operations? **	Significant to collecting revenue or making payments? **	Any information suggesting significant Y2K remediation problems?
1. Entities that make material intergovernmental payments to this government.				
2.) Service organizations (As defined in Auditing Standard No. 70).				
3). Financial institutions that process material transactions for this entity (e.g., a bank processing our checking account).				
4.) Electronic interfaces with suppliers and other vendors. Examples include Electronic Funds Transfers, Electronic Data Interchange (EDI) of purchase order data and related wire payment information.				
5.) Systems used by “external” courts to record & allocate receipts, disbursements and to maintain case records.				

** Note: A “yes” answer to **either** “significant to conducting critical operations?” or “significant to collecting revenue or making payments?” should result in classifying the system or equipment as mission critical. For each of the above services the government operates, append a brief summary supporting the conclusions above (i.e., why the service is or is not significant to its critical operations, collecting revenue or making payments).

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Part 2
Documentation of Other GTB 98-1 Stages
Mission Critical System or Equipment Documented Below: _____

A copy of Part 2 should be completed for each Mission Critical System or equipment identified in **Part 1**.

Awareness Stage Steps		Yes	No
1.	Does the organization have a Y2K plan to remediate this system?		
2.	Has the entity appropriated resources for this project? <i>– If the system is to be remediated by in-house programmers, the appropriation may be for their salaries.</i>		
Awareness Stage Summary Based on the preponderance of evidence documented above, briefly describe below whether management believes the entity has met the “awareness” stage of the Y2K project.			

Assessment Stage Steps		Yes	No	N/A
1.	Has the entity assigned a person (or persons) with overall responsibility for remediating this system or equipment? (List their name on the Part 1 Summary. If no one has been assigned, it is questionable whether the entity has completed the awareness stage for this system or equipment.)			
2.	Has each element (mission critical system component - application, hardware, embedded chips or system software) been separately identified, assessed and their planned remediation defined?			
3.	Has the entity obtained written representations from <i>critical</i> suppliers or vendors that their products (computer applications, hardware, system software and embedded chips) are Year 2000 compliant? Such suppliers and vendors would include the entity's banking or other financial institutions, entities that supply water or electricity to a utility, etc.			
4.	Has the entity obtained written representations from their SAS 70 service organizations, financial institutions and entities with which our entity has electronic data interchanges that they will be Year 2000 compliant?			

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	Assessment Stage Steps	Yes	No	N/A
5.	If internal programmers are used, has an assessment been made identifying whether entity personnel (data processing staff, engineer staff) have sufficient skills to undertake and complete Year 2000 Plans, including validation testing, in the required time or whether outside resources are required to complete the Year 2000 Plan?			
6.	Does the entity have sufficient appropriable resources to pay for the employees (including overtime), outside consultants or other required costs?			
7.	Has the entity outlined a contingency plan should the system not be remediated in time or if the system was not remediated properly? -- Such plans might include, for example, provisions for temporary manual processing of accounting transactions. -- If contingency plans are the primary intended means of temporary remediation, the contingency plan should be in reasonable detail and be achievable.			
Assessment Stage Summary Based on the preponderance of evidence documented above, briefly describe below whether management believes the entity has met the "assessment" stage of the Y2K project.				

Best Practices - Assessment:

Dedicate A Year 2000 Project Manager. Because of the breadth of the Y2K problem and complexities of overall solutions, governments should assign a project manager. This person should have executive sponsorship, carry the authority of the highest ranking government official and have equal access to all departments.

Establish an Internal and External Awareness Program. Every facet of a government should be familiar with the nature and importance of the Year 2000 problem, including its potential for business disaster. An external campaign on Y2K activities is equally important. An informed public is more likely to support the necessary changes, and accept a certain level of inconvenience in dealing with Y2K issues.

Mission Critical Prioritization. Due to the limited timeline before 2000, governments should prioritize the system upgrades or replacements according to their missions and basic operating needs. Most organizations prioritize based on "life-health-safety" issues such as utilities and payroll. Governments should reevaluate priorities throughout the project as Year 2000 approaches.

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	Remediation Stage Steps	Yes	No	N/A
1.	Is any outside required assistance already under contract?			
2.	Have appropriate Y2K compliant hardware/microchips been ordered/received or installed?			
3.	Has all Y2K compliant systems software (operating system, security software, etc.) been ordered/received or installed?			
4.	Are embedded chips being recoded to become Y2K compliant or have new Y2K compliant embedded chips been ordered/received or installed?			
5.	Has the installation of new software, or the review of existing coding begun?			
6.	Does compliant vendor software currently exist, and has it been tested by the vendor? <i>-- For example, if critical software is still under development, an entity should probably not be classified in the remediation stage.</i>			
7.	Have any necessary data bridges and filters been developed, or are under development? <i>-- Data bridges and filters convert nonconforming data received from outside entities into the proper date format for internal use.</i>			
Remediation Stage Summary Based on the preponderance of evidence documented above, briefly describe below whether management believes the entity has met the "remediation" stage of the Y2K project.				

Best Practices - Remediation:

Contingency and Business Recovery Planning. A government should develop an effective contingency plan should certain systems fail. Such planning should also take life-health-safety issues into consideration and prioritize the business recovery along the expected failure and crisis need at the time. An effective plan should include a "go/no-go" date for employing the contingency solution.

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Validation/Testing Stage Steps		<u>Yes</u>	<u>No</u>	<u>N/A</u>
Mission Critical System or Equipment Documented Herein:				
Answer questions 1 - 3 for vendor-remediated software:				
1.	Has vendor-acquired software been installed?			
2.	Has the vendor supplied some form of written assurance that the upgraded software is Y2K compliant? <i>A vendor need not "guarantee" that software is Y2K compliant, but should provide a written statement that the vendor believes the software is compliant. This can be in the form of a certification, a warranty to repair any defects resulting from Y2K problems, or simply a statement of compliance in a list of enhancements associated with the latest upgrade.</i>			
3.	Has the remediated software been tested using the entity's hardware platform and operating systems?			
Answer questions 4 - 7 for software remediated by in-house programmers:				
4.	For each converted or replaced Y2K compliant application or system component, embedded chip(s), etc., has the entity developed and documented test and compliance plans and schedules?			
5.	Does the test plan for this mission-critical system or equipment component include:			
a.	Unit Testing <i>– Unit testing verifies that the smallest defined module (one application date field or hardware component or system software or embedded chip(s)) is operating as intended. Unit testing is usually performed by the software engineer or programmer who modified the module.</i>			
b.	Integration Testing <i>– Integration testing is performed to verify that the units (application or component), when combined, work together as intended. Because the units being integrated have already been tested successfully, integration testing focuses on ensuring that the interfaces work correctly and that the integrated software meets specified requirements.</i>			
c.	Acceptance Testing <i>– The purpose of system acceptance testing is to verify that the complete system satisfies specified requirements and is acceptable to end users.</i>			
d.	End-to-End Testing <i>– End-to-End testing verifies that a defined set of interrelated systems which collectively support an organizational core business area or function, interoperate as intended in an operational environment.</i>			

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Validation/Testing Stage Steps Mission Critical System or Equipment Documented Herein:		<u>Yes</u>	<u>No</u>	<u>N/A</u>
6.	Has the following testing of each application or system component been completed:			
a.	Unit Testing			
b.	Integration Testing			
c.	Acceptance Testing			
d.	End-to-End Testing			
7.	Have coding modifications been completed such that the revised software is operable?			
Validation/Testing Stage Summary – Based on the preponderance of evidence documented above, briefly describe below whether management believes the entity has met the “validation/testing” stage of the Y2K project.				
Dates for which the entity tested the system/equipment:				
<u>Critical Date</u>	<u>Did entity test run software/equipment for these dates?</u>	<u>Comments</u>		
9/9/99				
1/1/00				
Last day of week ending 1/7/00				
End of first month (Jan. '00)				
2/29/00				
Month/quarter/year end processing for '99				

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Best Practices - Validation\Testing:

Develop Robust Testing Environment. Y2K testing reviews more areas and business rules than most organizations expect, and existing processes often fall short of requirements. Testing must ensure all date-related calculations are correct and the data is forwarded in the proper formats. Leap year and aging calculations pose particular problems for the year 2000.

Part 3
Required GTB 98-1 Disclosures

GTB 98-1 and SEC Release Disclosure Information	
	Disclosure requirement
1.	A general description of the year 2000 issue as it relates to the organization. -- See AOSAM Bulletin 98-?? for examples. (GTB 98-1, ¶ PAR. 7)
2.	Disclose amounts of resources contractually committed but not yet spent or payable for the project. (GTB 98-1, ¶ 6)
3.	The disclosure should describe the stage(s) of work in process or completed and yet to be completed for mission-critical systems and equipment. (GTB 98-1, ¶ 8) -- <i>Many entities will have more than one mission critical system. If the stages of work differ between systems & equipment, multiple descriptions are required.</i> -- <i>Work done to complete Part 2 should be sufficient to support this portion of the disclosure.</i>
4.	The Auditor of State requires the Year 2000 note to contain the following disclaimer language: Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the [Government] is or will be Year 2000 ready, that the [Government]'s remediation efforts will be successful in whole or in part, or that parties with whom the [Government] does business will be year 2000 ready. If this language is omitted, the note should be marked as "unaudited"
5.	The following paragraph, or something similar, should be added to the required disclosures: The year 2000 issue is the result of shortcomings in many electronic data processing systems and other equipment that may adversely affect the government's operations as early as fiscal 1999.

6.	Governments with significant debt outstanding or to be issued should contact their bond/legal counsel for advice on complying with the SEC release requirements. If the government's bond/legal counsel advises the government to disclose the information in the government's <u>financial statements</u> , then these disclosures in the financial statements should be marked "unaudited".
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Appendix C
Excerpts from the SEC Release entitled, in part:
STATEMENT OF THE COMMISSION REGARDING
YEAR 2000 ISSUES...

I. C. Municipal Issuers

Municipal issuers also have disclosure obligations. Our [i.e., the SEC's] regulatory authority over disclosure by issuers of municipal securities is not as broad as our authority over disclosure by public and investment companies. Generally, municipal securities offerings are, by statute, exempt from registration and municipal securities issuers are exempt from the reporting provisions of the federal securities laws, including line-item disclosure rules.

Municipal securities issuers, and persons participating in the preparation of municipal securities issuers' disclosure, however, are subject to the anti-fraud provisions of the federal securities laws. Approximately 50,000 state and local governments have over \$1.3 trillion in municipal securities outstanding. Municipal securities issuers, like other organizations, have Year 2000 issues. Year 2000 problems may affect their operations, creditworthiness, and ability to make timely payment on their indebtedness. We encourage municipal securities issuers and persons who assist in preparing their disclosure documents to consider whether Year 2000 issues may be material to investors. If material, the disclosure documents used by municipal issuers should contain a discussion of Year 2000 issues to avoid misleading statements or omissions that could violate the anti-fraud provisions. In Section III. E [excerpted in the next section] , we [the SEC] provide guidance to municipal issuers, and persons assisting in the preparation of their disclosures, regarding Year 2000 disclosure.

...

III. E. Guidance for Year 2000 Disclosure for Municipal Issuers

Generally, municipal securities offerings are exempt from registration and municipal securities issuers are exempt from the reporting provisions of the federal securities laws, including line-item disclosure rules. However, they are not exempt from the anti-fraud provisions. Disclosure documents used by municipal issuers are subject to the prohibition against false or misleading statements of material facts, including the omission of material facts necessary to make the statements made, in light of the circumstances in which they are made, not misleading.

Issuers of municipal securities and persons assisting in preparing municipal issuer disclosures are encouraged to consider whether such disclosures should contain a discussion of Year 2000 issues. Persons, including "obligated persons" as defined in Rule 15c2-12¹⁷, who provide information for use in disclosure documents or in ongoing disclosure to the market, are urged to consider their own Year 2000 issues. Year 2000 issues should be considered in preparing all disclosure documents, whether in the context of an official statement, continuing disclosure provided in compliance with a disclosure covenant, or other information that is reasonably expected to reach investors and the trading markets.

¹⁷ See Auditor of State Bulletin 95-018 for a discussion of SEC Rule 15c2-12

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Whether Year 2000 issues are material depends upon the particular facts and circumstances for each municipal issuer. Consideration may be given, for example, to whether Year 2000 issues affect internal operations of an issuer or affect an issuer's ability to provide services and meet its obligations, including timely payment of its indebtedness.

Because of the varieties of municipal issuers and of municipal securities, the examples provided below may or may not apply to a particular issuer and an issuer may be subject to facts and circumstances requiring disclosure not described below. Issuers and the persons assisting in disclosure preparation should give careful consideration to Year 2000 issues within the context of the facts and circumstances applicable to the disclosing issuer or the securities.

Examples of Potential Year 2000 Problems

For municipal issuers, Year 2000 issues may be divided into three categories:

- ▶ Internal;
- ▶ External; and
- ▶ Mechanical.

Internal Year 2000 issues may arise from an issuer's own operations and materially affect its creditworthiness and ability to make timely payment of its obligations.

External Year 2000 issues may arise from parties, other than an issuer, that provide payments that support the debt service on an issuer's municipal securities. Such payments may include, for example, health care reimbursement payments and payments under housing and student loan programs, as well as payments made by an obligated person under a lease, loan or installment sale agreement in a conduit financing.

Mechanical Year 2000 issues may arise if Year 2000 problems disrupt the actual mechanical process used to send payments to bondholders. For example, many municipal securities pay interest semiannually on January 1 and July 1 of each year, or have periodic sinking fund installments due to an indenture trustee or fiscal agent. Issuers may wish to determine whether Year 2000 issues affect their ability to identify and meet such obligations in a timely manner and to disclose any measures that will be undertaken if an issuer determines it will not be able to meet such obligations.

Issuers of general obligation debt may wish to consider, for example, the adverse effects, if any, Year 2000 issues may pose to their ability to assess and collect ad valorem taxes and allocate receipts and disbursements to proper funds in a timely manner to make debt service payments when due. In addition, while Year 2000 issues may not directly affect an issuer's ability to pay debt service, they may affect an issuer's general

Appendix C
Excerpts from the SEC Release entitled, in part:
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accounting and payment functions, which may be material to investors.

Revenue bond issuers may wish to consider, for example, any adverse effects Year 2000 issues may have on their ability to collect and administer the revenue stream securing their bonds and their ability to make timely payment of principal and interest on their obligations, as well as adverse effects to general accounting and payment functions, which may be material to investors.

Conduit borrowers, such as hospitals, universities and others, may wish to consider, for example, any adverse effects Year 2000 issues may have on their ability to deliver services, collect revenue and make timely payment on their obligations, including the obligation to pay debt service relating to municipal securities, which may be material to investors.

All issuers and conduit borrowers also may wish to consider the impact of Year 2000 problems facing third parties on their own ability to satisfy their responsibilities.

Other examples of suggested disclosure for consideration include, but are not limited to, the costs associated with fixing an issuer's Year 2000 problems, any loss associated with fixing an issuer's Year 2000 problems, any loss an issuer may incur because of Year 2000 problems, and any liabilities associated with an issuer's Year 2000 problems.

While not binding on issuers of municipal securities, issuers and persons assisting in preparing municipal issuer disclosures seeking further guidance may wish to review Sections III. A, [and] B [excerpted in the next section] of this release applicable to public companies. The anti-fraud provisions of the federal securities law prohibit materially false and misleading statements or omissions, including those relating to the Year 2000 issues we have discussed in this release.

III A. Specific Guidance for Year 2000 Disclosure under MD&A

The following specific guidance sets forth the type of Year 2000 disclosure that companies should provide...

1. Basic MD&A Analysis

MD&A [Management's Discussion and Analysis] is intended to give investors the opportunity to look at a company through the eyes of management by providing both a short and long-term analysis of the company's business -- with particular emphasis on the company's prospects for the future. MD&A requires a discussion of liquidity, capital resources, results of operations, and other information necessary to an understanding of a company's financial condition, changes in financial condition, and results of operations. The language of the MD&A requirement is intentionally general. This reflects our view that a flexible approach best elicits meaningful disclosure and avoids boilerplate discussions.

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One of the challenges that a company faces when drafting its MD&A is discussing forward-looking information. One of the few regulations that require forward-looking disclosure, MD&A contains a variety of formulations calling for this information, including a requirement to disclose known material events, trends or uncertainties.

In the 1989 Release, we [SEC] gave guidance to companies on various aspects of MD&A disclosure. Under the 1989 Release, companies should apply the following analysis to determine if they should disclose forward-looking information.

Where a trend, demand, commitment, event, or uncertainty is known, management must make two assessments:

(1) Is the known trend, demand, commitment, event or uncertainty likely to come to fruition? If management determines that it is not reasonably likely to occur, no disclosure is required.

(2) If management cannot make that determination, it must evaluate objectively the consequences of the known trend, demand, commitment, event or uncertainty on the assumption that it will come to fruition. Disclosure is then required unless management determines that a material effect on the company's financial condition or results of operations is not reasonably likely to occur.

The determination made by management must be objectively reasonable, viewed as of the time the determination is made.

This test essentially requires companies to disclose forward-looking information based on currently known events, trends or uncertainties that are reasonably likely to have material effects on the company's financial condition or results of operations. Because of the prevalence of computers and embedded technology in virtually all businesses and the potential consequences of not adequately addressing the Year 2000 problem, we believe that almost every company will need to address this issue.

2. How We [SEC] Interpret MD&A in the Year 2000 Context

a. Whether to Disclose Year 2000 Issues

The first decision that a company must make is whether it has an obligation to provide any disclosure regarding its Year 2000 issues. [GASB's Technical Bulletin provides required disclosures for governments. Therefore, this section of the SEC Release should be read in conjunction with the GASB TB]. By applying the 1989 Release's guidance regarding forward-looking information, we believe that a company must provide Year 2000 disclosure if:

(1) its assessment of its Year 2000 issues is not complete, or

(2) management determines that the consequences of its Year 2000 issues would have a material effect on the

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company's business, results of operations, or financial condition, without taking into account the company's efforts to avoid those consequences.

Our two-part test is substantially similar to the revised Staff Legal Bulletin's guidance for whether companies have a Year 2000 disclosure obligation. We believe that a large majority of companies will meet one or both of these tests and therefore will be required to provide Year 2000 disclosure. We expect that significantly more companies will be providing Year 2000 disclosure in future disclosure documents than the 70% found by the task force.

Under the first test, a company's assessment should take into account whether third parties with whom a company has material relationships are Year 2000 compliant. The determination of whether a relationship is material depends on the nature of the relationship.

For vendors and suppliers, the relationship is material if there would be a material effect on the company's business, results of operations, or financial condition if they do not timely become Year 2000 compliant. The same 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 also should consider its potential liability to third parties if its systems are not Year 2000 compliant, resulting in possible legal actions for breach of contract or other harm.

In our [SEC's] view, a company's Year 2000 assessment is not complete until it considers these 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. We understand that this is often done by analyzing the responses to questionnaires sent to these third parties. In the absence of receiving responses to questionnaires, there may be other means to assess third party readiness.

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. In other words, 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 of this unpreparedness. As part of this analysis, the company must assume that material third parties will not be ready either, unless these third parties have delivered written assurances to the company 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 this issue.

b. What to Disclose about Year 2000 Issues

[GASB's Technical Bulletin provides required disclosures for governments Therefore, this section of the SEC Release should be read in conjunction with the GASB TB].

Once a company determines that it has a Year 2000 disclosure obligation, it has to decide what to disclose about its Year 2000 issues. MD&A does not require categories of specific information because each company has to consider its own circumstances in drafting its MD&A. For Year 2000 disclosure to be meaningful, we

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believe that companies will have to address the following four categories of information in their MD&A, as discussed in more detail below:

- (1) the company's state of readiness;
- (2) the costs to address the company's Year 2000 issues;
- (3) the risks of the company's Year 2000 issues; and
- (4) the company's contingency plans.

The disclosure should be specific to each company and quantified to the extent practicable. Some companies may have to provide this information by business segment or subdivision. Companies should avoid generalities and boilerplate disclosure. In addition, each company must consider if its own Year 2000 circumstances require that additional matters be disclosed.

(1) The Company's State of Readiness

When a company has to provide disclosure regarding a known material event, trend, or uncertainty, it first has to describe that event, trend, or uncertainty. A company should describe its Year 2000 issues in sufficient detail to allow investors to fully understand the challenges that it faces. We suggest that the description be similar to that provided to a company's board of directors -- which typically is non-technical plain English and answers the important questions -- such as "will we be ready?" and "how far along are we?" So far, most companies have provided only a cursory description of their Year 2000 issues.

A full description of a company's Year 2000 readiness will generally include, at the very least, the following three elements. First, the discussion should address both information technology ("IT") and non-IT systems. Non-IT systems typically include embedded technology such as micro controllers. These types of systems are more difficult to assess and repair than IT systems. In fact, companies often have to replace non-IT systems since they cannot be repaired. To date, only a few companies have addressed non-IT issues in their disclosure. We are concerned that companies are overlooking non-IT systems when they provide Year 2000 disclosure.

Second, for both their IT and non-IT systems, companies should disclose where they are in the process of becoming ready for the Year 2000. 41 The status of the company's progress, identified by phase, including the estimated timetable for completion of each remaining phase, is vital information to investors and should be disclosed. There are no universal definitions for the phases in a Year 2000 remediation program. However, for the most part, the phases are self-explanatory, and we recommend that companies briefly describe how they define each phase. Another challenge is describing the status of multiple computer systems. Companies should tailor the disclosure and the format for their own particular circumstances.

The third essential component is a description of a company's Year 2000 issues relating to third parties with

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which they have a material relationship. Due to the interdependence of computer systems today, the Year 2000 problem presents a unique policy issue. For example, if a major telecommunications company discloses that it may have a business interruption, this may require many other companies to disclose that they too may have a business interruption, if material. Thus, each company's Year 2000 issues may affect other companies' disclosure obligations. Companies should disclose the nature and level of importance of these material relationships, as well as the status of assessing these third party risks.

(2) The Costs to Address the Company's Year 2000 Issues

Companies must disclose material historical and estimated costs of remediation. This includes costs directly related to fixing Year 2000 issues, such as modifying software and hiring Year 2000 solution providers. In most cases, the replacement cost of a non-compliant IT system should be disclosed as an estimated Year 2000 cost. This is so even if the company had planned to replace the system and merely accelerated the replacement date. A company does not need to include the replacement cost as a Year 2000 estimated cost if it did not accelerate the replacement due to Year 2000 issues.

(3) The Risks of the Company's Year 2000 Issues

Companies must include a reasonable description of their most reasonably likely worst case Year 2000 scenarios. The essence of MD&A is whether the consequences of a known event, trend, or uncertainty are likely to have a material effect on the company's results of operations, liquidity, and financial condition. If a company does not know the answer, this uncertainty must be disclosed, as well as the efforts made to analyze the uncertainty and how the company intends to handle this uncertainty. For example, companies must disclose estimated material lost revenue due to Year 2000 issues, if known.

(4) The Company's Contingency Plans

Companies must describe how they are preparing to handle the most reasonably likely worst case scenarios. This information will help investors evaluate the company's Year 2000 exposure by answering the important question -- "what will the company do if it is not ready?" Under this category of information, the company must describe its contingency plans. We recognize that describing contingency plans may be particularly challenging. Many companies have not yet established a contingency plan. In this case, the company should disclose that it does not have a contingency plan, whether it intends to create one, and the timetable for doing so.

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III B. Year 2000 Financial Statement Considerations

Existing accounting and auditing standards provide guidance concerning the accounting and disclosure issues

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arising from the Year 2000 problem. Matters that companies and their auditors should consider include the following.

1. Accounting and Disclosure in Financial Statements

Costs of Modifying Software. A company's need or plan to modify its own software for Year 2000 compliance does not result in a liability that is recognized in financial statements. Instead, the costs of modifying the software are charged to expense as they are incurred.

Costs of Failure to Be Year 2000 Compliant. Operating losses expected to result if a company, its suppliers, or customers fail to correct Year 2000 deficiencies are recognized only as they are incurred.

Disclosure of Year 2000 Related Commitments. Companies should consider the need to disclose payments to be made pursuant to unfulfilled or executory contracts or commitments with vendors to remediate Year 2000 noncompliance problems. Companies also should consider the need to disclose the potential for acceleration of debt payments due to covenant defaults tied to Year 2000 readiness.

...

Allowances for Loan Losses. The credit quality of a loan may be affected by the failure of a borrower's operating or other systems as a consequence of a Year 2000 issue or a borrower's failure to comply with debt covenant terms regarding Year 2000 issues. Creditors' allowances for loan losses, however, should be provided only for losses incurred as of the balance sheet date, and should not be based on the effects of future events.

...

Disclosure of Risks and Uncertainties. A company must explain any risk or uncertainty of a reasonably possible change in its estimates in the near term that would be material to the financial statements. Examples of estimates that may be affected by Year 2000 issues include estimates of warranty liability, reserves for product returns and allowances, capitalized software costs, inventory, litigation, and deferred revenue.