

**MEMO# 23655**

July 27, 2009

## **SEC Proposes Enhancements to Municipal Securities Disclosure Regime; Conference Call Scheduled for July 30**

[23655]

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TO: MUNICIPAL SECURITIES ADVISORY COMMITTEE No. 36-09  
MONEY MARKET FUNDS ADVISORY COMMITTEE No. 32-09 RE: SEC PROPOSES  
ENHANCEMENTS TO MUNICIPAL SECURITIES DISCLOSURE REGIME; CONFERENCE CALL  
SCHEDULED FOR JULY 30

The Securities and Exchange Commission ("SEC") has proposed several amendments to Rule 15c2-12 under the Securities Exchange Act of 1934 relating to municipal securities disclosure. [1] Specifically, the proposal would amend certain requirements regarding continuing disclosure obligations including the list of specific disclosure events ("event notices") and the timing of such disclosure. [2] In addition, the proposal would eliminate an exemption from Rule 15c2-12 for variable rate demand obligations ("VRDOs"). Finally, the SEC would provide interpretive guidance to assist issuers, brokers, dealers and municipal securities dealers in meeting their obligations under the antifraud provisions. Comments on the proposal, which is summarized below, are due to the SEC on or before September 8, 2009.

We have scheduled a conference call for Thursday, July 30 at 3:00 p.m. Eastern time to discuss the Institute's comment letter on the proposal. The dial-in information for the conference call is 1-866-541-3298 and the passcode for the call is 6501781. If you plan to participate on the call, please contact Ruth Tadesse by email at [rtadesse@ici.org](mailto:rtadesse@ici.org) or 202-326-5836.

## **Basis for the Proposal**

In the proposal, the SEC stated that changes in the municipal market since 1994 – the last time the SEC amended the municipal securities disclosure requirements – merit clarifications and enhancements to the current disclosure regime. In the context of recent market events, the SEC noted, in particular, the increase in the amount of outstanding municipal debt, the diversity of the municipal securities market, and the fact that municipal bonds can and do default. The SEC expressed its belief, therefore, that the proposed amendments would help deter fraud and manipulation in the municipal securities market by prohibiting the underwriting and recommendation of transactions in municipal securities for which inadequate information is available on an ongoing basis.

## **Elimination of Exemption for VRDOs**

The proposal would eliminate the exemption from the requirement in Rule 15c2-12 that an underwriter for VRDOs determine that an issuer has undertaken, in a continuing disclosure agreement, to provide continuing disclosure documents to the MSRB. The amendment would apply to any initial offering of VRDOs, or remarketing of VRDOs that are primary offerings, occurring on or after the effective date of any final amendments that the SEC may adopt.

The SEC explained in the proposal that investors need more information to understand the risks associated with these securities and to oversee their investments in these securities, especially because of the increased amount of VRDO issuances since implementing the exemption, high VRDO trading volume, the increased number of investors in VRDOs, and some investors' tendency to hold these securities for long periods of time. In addition, the SEC noted that the exemption was originally created to address operational concerns related to the nascent VRDO market. The SEC stated its beliefs that these concerns are no longer justified due to developments in this market, and the benefits of improved disclosure in this market outweigh the minimal burdens to issuers and underwriters.

The SEC seeks comment on the need for continuing disclosure information in the VRDO market and the extent to which this proposal would provide benefits to investors and other municipal market participants.

## **Timeframe for Submitting Event Notices**

The proposal would establish a time certain for reporting event notices under a continuing disclosure agreement. It would provide that an underwriter reasonably determine that an

issuer has agreed in its continuing disclosure agreement to submit event notices to the MSRB in a timely manner not in excess of ten business days after the occurrence of the event. Moreover, the SEC stated in the proposal that it is likely, in many instances, that an event notice could be submitted in fewer than ten business days, depending on the facts and circumstances of the particular event. The proposed timeframe would not apply to continuing disclosure agreements entered into with respect to primary offerings that occurred prior to the effective date of any final amendments that the SEC may adopt.

In selecting this time period, the SEC stated that longer delays would undermine the effectiveness of Rule 15c2-12 because the importance of the event notices to investors has already been established by their inclusion in the Rule. It also said that prompt disclosure of information about municipal securities should promote greater transparency and investor confidence in the municipal securities market as a whole.

The SEC seeks comment on the need to establish a timeframe and whether the trigger for the timeframe should begin when an issuer knows or should have known of the occurrence of the event, rather than the actual occurrence of the event.

### **Materiality Determination for Certain Event Notices**

The proposal would eliminate the condition in Rule 15c2-12 that provides that event notices need be made only “if material.” Instead, some event notices would be required whenever such an event occurs because of their importance to investors and other market participants. These events would include: (1) principal and interest payment delinquencies with respect to the securities being offered; (2) unscheduled draws on debt service reflecting financial difficulties; (3) unscheduled draws on credit enhancements reflecting financial difficulties; (4) substitution of credit or liquidity providers, or their failure to perform; (5) defeasances; and (6) rating changes. In addition, the proposal would provide specifically for the disclosure to the MSRB of adverse tax opinions, the issuance, by the Internal Revenue Service (“IRS”), of proposed or final determinations of taxability, Notices of Proposed Issue or other material notices or determinations with respect to the tax-exempt status of securities, or other events affecting the tax-exempt status of the security. A materiality determination would be retained for the other events currently listed in Rule 15c2-12. [\[3\]](#)

The SEC seeks comment on the proposed application of the materiality determination to some, but not all, event notices. It also questions whether a copy of the determination or other IRS materials regarding taxability issues should be provided to the MSRB, or whether notice of such a determination would provide sufficient information to investors.

## **Proposed Additional Event Notices**

The proposal would incorporate four additional events into the list of event notices in Rule 15c2-12 (two of these additional events would include materiality determinations) because of the SEC's concern that information regarding these events should be made more widely available to investors on a more consistent basis.

First, the proposal would add tender offers to the list of required event notices to ensure that bondholders are informed of tender offers. The SEC seeks comment on whether an underwriter should be required to determine whether an issuer had agreed to provide particular information regarding a tender offer, such as the offer price, change in offer price, or withdrawal rights, in addition to notice of the tender offer. It also seeks comment on whether exchange offers should be included with this disclosure item.

Second, the proposal would add an event notice for bankruptcy, insolvency, receivership or similar proceeding of the obligated person because of the SEC's belief that the occurrence of such events, even if rare, can significantly impact the value of a municipal security. The proposal sets out that this type of event would be considered to occur when any of the following occur: the appointment of a receiver, fiscal agent or similar officer for an obligated person in a proceeding under the U.S. bankruptcy Code or in any other proceeding under state or federal law in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the issuer or obligated person, or if such jurisdiction has been assumed by leaving the existing governing body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan or reorganization, arrangement or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets or business of the obligated person.

Third, the proposal would add an event notice requiring disclosure of the consummation of a merger, consolidation, or acquisition involving an obligated person or the sale of all or substantially all of the assets of the obligated person, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material. The proposal would impose a materiality determination on this proposed event notice because of the SEC's belief that it is possible for such an event to be so sufficiently insignificant that an event notice would not be required. The SEC seeks comment on the frequency of such events and whether this information would be meaningful to investors.

Fourth, the proposal would implement a requirement to provide notice of the appointment of a successor or additional trustee, or the change or name of a trustee, if material. The SEC acknowledges in the proposal that this information may have little or no influence on a

decision whether to buy or sell a municipal security under normal circumstances. However, it notes that a bondholder would have need to know the identity of a trustee to be able to contact the trustee for various reasons, particularly when an issuer or other obligated person may be experiencing financial difficulty. Accordingly, the SEC seeks comment on whether the continuing disclosure agreement should set forth additional information regarding the trustee and whether a materiality determination is appropriate.

## **Effective Date and Transition**

The proposal would become effective three months after final adoption of the proposed amendments. The SEC seeks comment on the potential effects of existing continuing disclosure agreements having different terms and also raises the issue of amending all prior continuing disclosure agreements.

## **Interpretive Guidance for Underwriters**

The proposal includes SEC guidance with respect to the obligations of underwriters relating to continuing disclosure agreements. It generally reaffirms its previous interpretations regarding an underwriter's obligation to make a reasonable determination that an issuer has agreed to satisfy the continuing disclosure requirements, emphasizing that sole reliance on the representations of an issuer will not suffice. The SEC also restates that disclaimers by underwriters of responsibility for the information provided by the issuer or other parties without further clarification regarding the underwriter's belief as to accuracy are misleading and should not be included in official statements.

Heather L. Traeger  
Associate Counsel

### **endnotes**

[1] SEC Release No. 60332 (July 18, 2009), 74 FR 36831 (July 24, 2009), available on the SEC's website at: <http://www.sec.gov/rules/proposed.shtml>.

[2] Rule 15c2-12 requires that a broker, dealer or municipal securities dealer acting as an underwriter in a primary offering of municipal securities must reasonably determine that an issuer of municipal securities or an obligated person has undertaken, in a written agreement or contract for the benefit of holders of such securities ("continuing disclosure agreement"), to provide certain information to the Municipal Securities Rulemaking Board ("MSRB"). The requisite information includes: (1) certain annual financial and operating

information and audited financial statements; (2) event notices of the occurrence of any of eleven specified events; and (3) notices of the failure of an issuer or other obligated person to make a submission required by the continuing disclosure agreement. (An obligated person means persons, including the issuer of municipal securities, committed by contract or other arrangement to support payment of all or part of the obligations on the municipal securities to be sold in an offering.)

[\[3\]](#) These include event notices regarding non-payment related defaults, modifications to rights of security holders, bond calls, and the release, substitution, or sale of property securing repayment of securities.

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