The Asset Management Industry
SERVING INDIVIDUAL INVESTORS
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SEC Adopts Enhancements to Municipal Securities Continuing Disclosure Regime

[24337]

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TO: MUNICIPAL SECURITIES ADVISORY COMMITTEE No. 22-10
MONEY MARKET FUNDS ADVISORY COMMITTEE No. 23-10 RE: SEC ADOPTS ENHANCEMENTS TO MUNICIPAL SECURITIES CONTINUING DISCLOSURE REGIME

The Securities and Exchange Commission has adopted amendments to Rule 15c2-12 under the Securities Exchange Act of 1934 relating to municipal securities disclosure. [1] The amendments eliminate an exemption from the rule for variable rate demand obligations ("VRDOs") and modify certain requirements regarding continuing disclosure obligations including the list of specific disclosure events ("event notices") and the timing of such disclosure. In addition, the SEC has provided interpretive guidance to assist issuers, brokers, dealers and municipal securities dealers in meeting their obligations under the antifraud provisions of the securities laws.

Elimination of Exemption for VRDOs

The amendments 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 Municipal Securities Rulemaking Board ("MSRB"). The amendments apply to any initial offering of VRDOs, or remarketing of VRDOs that are primary offerings, occurring on or after the compliance date of December 1, 2010. However, the SEC has adopted a limited grandfather provision for remarketings of currently outstanding demand securities so long as such securities are outstanding in the form of demand securities on the day preceding the compliance date of the amendments and have remained outstanding continuously in the form of demand securities.

Timeframe for Submitting Event Notices

The amendments establish a time certain – ten business days after the occurrence of the event – for reporting event notices under a continuing disclosure agreement. An

underwriter, therefore, must 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. The amended timeframe would not apply to continuing disclosure agreements entered into with respect to primary offerings that occurred prior to the compliance date of the amendments.

Materiality Determination for Certain Event Notices

The amendments eliminate the condition in Rule 15c2-12 that provides that event notices need be made only "if material." Instead, some event notices must be provided whenever such an event occurs because of their importance to investors and other market participants. These events include: (1) principal and interest payment delinquencies with respect to the securities being offered; (2) unscheduled draws on debt service reflecting financial difficulties; [2] (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. [3] A materiality determination has been retained for the other events currently listed in Rule 15c2-12. [4]

In addition, the amendments provide specifically for the disclosure to the MSRB of adverse tax opinions, the issuance, by the Internal Revenue Service, 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. As adopted, the Release includes two clarifications to the original proposal. First, the Release states that notices of events not specified in Rule 15c2-12 that affect the tax status of a security are required only if the events are material to investors. Second, the Release explains that underwriters must comply with the provisions of Rule 15c2-12 for Build American Bonds and other taxable municipal bonds with associated tax credits or direct federal payments to the issuer because such bonds are municipal securities.

Additional Event Notices

The amendments incorporate four additional events into the list of event notices in Rule 15c2-12 because of the SEC's concern that information regarding these events should be made more widely available to investors on a more consistent basis. Required notices now include an event notice for tender offers and an event notice for bankruptcy, insolvency, receivership or similar proceeding of the obligated person. The amendments also include 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. Lastly, the amendments 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 Institute and other commenters had recommended a number of additional disclosures as well as more granular disclosure with respect to the existing and proposed event notices. The SEC responded to commenters by stating that the suggested modifications would require more detailed disclosures than it intended for purposes of this rulemaking. It also stated, however, that it "is committed to considering proposals to further enhance the scope of municipal market disclosures and their dissemination to investors … as it

continues its efforts to bring greater transparency and other improvements to the municipal securities markets."

Compliance Date

The compliance date for the amendments is December 1, 2010.

Interpretive Guidance for Underwriters

The Release includes SEC guidance with respect to the obligations of underwriters relating to continuing disclosure agreements. It generally reaffirms the SEC's 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.

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endnotes

[1] See SEC Release No. 62184A (May 26, 2010) ("Release"), available at http://www.sec.gov/rules/final/2010/34-62184a.pdf.

[2] The Release clarifies that a notice would not be provided in the event of a draw that does not reflect financial difficulties with respect to the demand securities. Further, it states that a determination regarding the existence of financial difficulties must be made on a case-by-case basis, depending on the facts and circumstances surrounding such draws and failed remarketings.

[3] According to the Release, for each event that no longer is subject to a materiality condition, an underwriter must reasonably determine that the issuer or obligated person has agreed to submit a notice to the MSRB within ten business days of the event's occurrence, without regard to materiality.

[4] These events include: non-payment related defaults, modifications to the rights of security holders, bond calls, and the release, substitution, or sale of property securing repayment of the securities.