



FLORIDA SCHOOL FINANCE OFFICERS ASSOCIATION

Post MCDC and the SEC's Proposed Expansion of Issuer Continuing Disclosure Duties Issuer Continuing Disclosure Duties

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Learning Objectives

- Understanding Issuers' Continuing Disclosure Obligations Post-MCDC
- Outlining SEC's Proposed Amendments to Rule 15c2-12 on Financial Obligations
- Focusing on the Substance of New Financial Obligations Disclosures
- Identifying New Steps Issuers Would Need to Take to Comply with Expanded Disclosure Duties

Introduction – Continuing Disclosure

- Securities & Exchange Commission (SEC) Rule 15c2-12
Continuing Disclosure Requirement
 - Most new issues require issuer or obligor to agree in continuing disclosure agreement (CDA) to provide:
 - Annual financial/operating data & audited financial statements
 - Notices of occurrence of 14 specified events
 - Official statement (OS) must include description of:
 - Continuing disclosure obligations under CDA
 - Instances in previous 5 years of failures by issuer/obligor to comply, in all material respects, with any previous CDA

Continuing Disclosure Post-MCDC

- SEC's Municipalities Continuing Disclosure Cooperation (MCDC) Initiative
 - SEC market-wide settlement offer to:
 - Issuers/obligors for materially inaccurate statements in OSs about past compliance with CDAs
 - Underwriters for failure to conduct adequate due diligence regarding issuer/obligor disclosures in OS of past compliance with CDAs
 - SEC completed its settlements under the MCDC
 - 72 underwriters settled, effectively comprising the entire municipal market underwriting community
 - Underwriters paid reduced fines & agreed to have consultants review & recommend changes to their due diligence policies & procedures

Continuing Disclosure Post-MCDC

- SEC actions toward issuers/obligors
 - 71 issuers/obligors settled, representing only a small fraction of those who offered to settle
 - Settling issuers/obligors agreed to:
 - establish policies & procedures for continuing disclosures, including periodic training & designation of responsible individual
 - remediate past disclosure failures
 - disclose settlement terms in OSs for next five years

Continuing Disclosure Post-MCDC

- SEC actions toward issuers/obligors
 - Remaining issuers/obligors participating in MCDC but not settling with SEC should have received following e-mail:

We have concluded our review of the submission pursuant to the Municipalities Continuing Disclosure Cooperation Initiative from [Issuer/Obligor Name]. Based on the information we have as of this date, we do not intend to recommend an enforcement action by the Commission against [Issuer/Obligor Name]. ... [T]his notice ... “must in no way be construed as indicating that the party has been exonerated or that no action may ultimately result from the staff’s investigation.”

- Bottom line for participating non-settling issuers/obligors:
 - Policies & procedures not required but still advisable
 - Disclosure failures during past 5 years still must be disclosed
 - No OS disclosure of MCDC settlement
 - SEC won’t sue on past disclosure problems for MCDC-reported issues, other failures found during review still could be pursued

Continuing Disclosure Post-MCDC

- Likely SEC expectations post-MCDC:
 - Tolerance for disclosure non-compliance sharply reduced
 - While “material” still undefined, SEC has low threshold
 - Assessing event notices; MCDC focused on annual filings
 - Settling issuer/obligor with MCDC-required policies & procedures who fall out of compliance will be slammed
 - SEC will likely seek fines against issuers/obligors misstating CDA compliance in future OSs
 - SEC also may seek enforcement against individuals causing violations; new SEC chair emphasizes individual culpability

The “Personal Risk” CAN NOT BE FORGOTTEN!



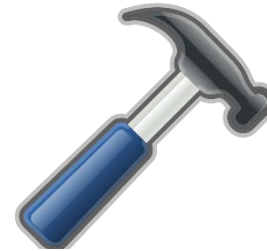
Miami Herald Headline November 14, 2016 read:

The SEC wants \$450,000 penalty against former Miami budget director...

<http://www.miamiherald.com/news/local/community/Miami-dade/article114769368.html>

Important to Remember

SEC's Toolbox contains only a hammer



And every problem is a



Why Amend Rule 15c2-12?

- After financial crisis, use of bank loans to displace traditional bond financing surged
- Regulators became concerned about:
 - Bank loans not disclosed like typical municipal bonds
 - only disclosed in notes to financial statements
 - no contemporaneous notice of incurrence and terms
 - investors in borrower's outstanding bonds potentially impacted
 - Broker-dealer/municipal advisor regulatory issues:
 - loan vs. security
 - municipal advisor vs. placement agent
- Proposed rule amendment seeks to address first concern

How Would Rule 15c2-12 Be Amended?

- SEC would add one definition & two new event notices:
 - New definition: “*financial obligation*”
 - means a (i) debt obligation, (ii) lease, (iii) guarantee, (iv) derivative instrument, or (v) monetary obligation resulting from a judicial, administrative, or arbitration proceeding
 - Excludes bond issues with OSs already appearing on EMMA website
 - Extends well beyond just bank loans
 - New event notices related to a financial obligation:
 - *Incurrence*, if material, & covenants, events of default, remedies, priority rights, or similar terms affecting securities holders, if material
 - default, event of acceleration, termination event, modification of terms, or other similar event reflecting *financial difficulties*

How Would Rule 15c2-12 Be Amended?

- On its face, proposed amendment would not change current structure for making disclosures
 - simply expands list of event notices from 14 to 16 event types
 - New disclosures would be submitted to EMMA website through same process as other event notices
- However, depending on the financial activities of an issuer/obligor, additional efforts to identify new events and produce notices could be considerable

What Is a Financial Obligation?

Financial obligations that would be subject to new event notice requirements include:

- Debt obligations
- Leases
- Guarantees
- Derivative instruments
- Monetary obligations resulting from judicial, administrative, or arbitration proceedings

What Is a Financial Obligation?

- Debt obligations – include:
 - Bank loans
 - Bond/note issues exempt from OS requirement, such as:
 - Direct sale to investor without underwriter
 - Issues under \$1 million
 - Limited offerings
 - Notes maturing in less than 9 months
 - VRDO issues

What Is a Financial Obligation?

- Leases – include:
 - Capital leases
 - e.g., lease-purchase agreement for equipment or buildings
 - Operating leases
 - e.g., lease of office space for a defined lease term

What Is a Financial Obligation?

- Guarantees – include:
 - Contingent guarantee of obligations of:
 - the guarantor itself
 - an affiliate of the guarantor
 - an entity unrelated to the guarantor
 - Can take form of:
 - formal payment guarantee
 - other arrangement creating contingent financial obligation

What Is a Financial Obligation?

- Derivatives – include:
 - Financial derivatives, such as:
 - Interest rate swaps
 - Call options
 - Commodities derivatives, such as:
 - Natural gas forward supply contract

What Is a Financial Obligation?

- Monetary obligations resulting from judicial, administrative, or arbitration proceedings – include:
 - Proceedings unrelated to entity's debt obligations
 - Settlements or consent decrees arising from such proceedings

What Information Would Be Filed?

New event notices would consist of:

- Incurrence notice
- Financial difficulty notice

What Information Would Be Filed?

- Incurrence notice – includes:
 - description of material terms, including but not limited to:
 - date of incurrence
 - principal amount
 - maturity and amortization
 - interest rate, if fixed, or method of computation, if variable
 - agreed-to covenants, events of default, remedies, priority rights or other similar terms that may impact security holders

What Information Would Be Filed?

- Financial difficulty notice – includes:
 - Description of the default, event of acceleration, termination event, modification of terms, or other similar event reflecting financial difficulties
 - Description of the consequences of the event, if any

Thresholds and Timing of Filings?

- Notice of incurrence required only if financial obligation is “material”
- Description of agreed-to covenants required only if:
 - they “affect” “security holders” and
 - they are “material”
- Notice of an event required only if:
 - relates to a financial obligation and
 - event reflects “financial difficulties”
- Notice provided within 10 business days of occurrence

What Amendments Could Mean for You

New notices could significantly affect existing processes:

- To identify covered financial obligations:
 - wherever they arise within your organization and
 - that meet threshold of materiality
- To assess which terms must be disclosed as:
 - affecting security holders
 - meeting threshold of materiality
- To identify when an event:
 - occurs during performance of financial obligation
 - that could reflect financial difficulties

What Amendments Could Mean for You

- Identifying event, internally routing info about event, assessing event, & drafting/submitting notice:
 - Must occur within 10 business days of occurrence, notwithstanding fact that event can occur:
 - anywhere in organization – not just finance department but in any operating unit where financial obligations exist or can be impacted
 - at any juncture during course of day-to-day activities
- Disclosure policies & procedures would become increasingly important to achieve compliance
 - Need to assign duties & describe how each step in process is to be undertaken & overseen

SEC Request for Comments

The SEC sought comments on the proposed amendments through May 15, 2017

- Government Finance Officers Association (GFOA), individual state GFOAs, & other industry associations sought input from issuers & obligors on proposal – submitted a response
- DAC submitted a response
- Only 1 Florida Issuer (not a School District) submitted a response

When the Rule will be amended? – end of 2017

Annual Filings – Remember

Be clear in CDAs about deadlines for submitting annual financial information

- MCDC created a premium on precise undertaking of deadlines
i.e. 180 days does not equal 6 months
- What is a “provisional” filing?
- Assign responsibility for monitoring “events”
- Review any new CDA carefully – don’t allow “boiler plate”
- Know your CUSIP numbers (pre and un-refunded CUSIPS)
- Create your School District’s continuing disclosure legacy
- Remember tax compliance is equally important

Questions & Answers

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