

Debt Used to Be Easy

SEC Disclosure Requirements and Other Post Issuance Compliance

Nabors
Giblin &
Nickerson^{P.A.}

ATTORNEYS AT LAW

Ritesh Patel

Nabors, Giblin & Nickerson P.A.



David Moore, Managing Director
Financial Advisory Group

Overview

- Heightened Regulatory Focus
 - Attention by SEC, MSRB & IRS
- Continuing Disclosure
 - MCDC - just part of the issue



Takeaways

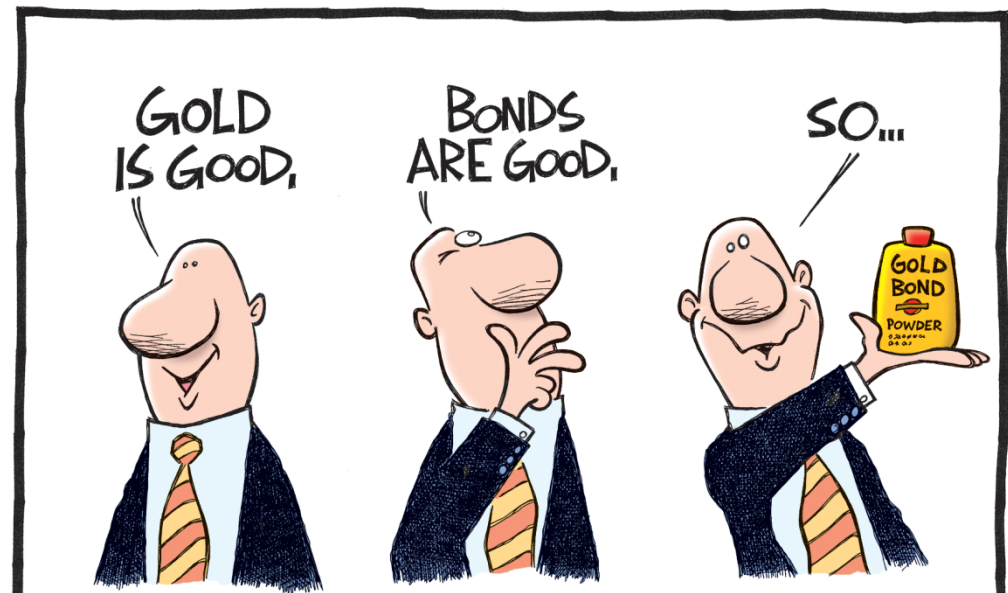
- The Rules are Different Now
- Entire District Finance Team Needs to Understand the Basics
 - You May not be the Debt Administrator, but the Rules Impact You
- IRS and SEC are NOT Going Away
- Detailed Planning BEFORE Issuance and ONGOING Post Issuance Compliance is Critical



Overview of School District Debt in Florida

- Long-Term Debt
 - General Obligation Bonds
 - Certificates of Participation
 - Sales Tax Bonds
 - Pari-Mutual Replacement
 - Equipment Leases

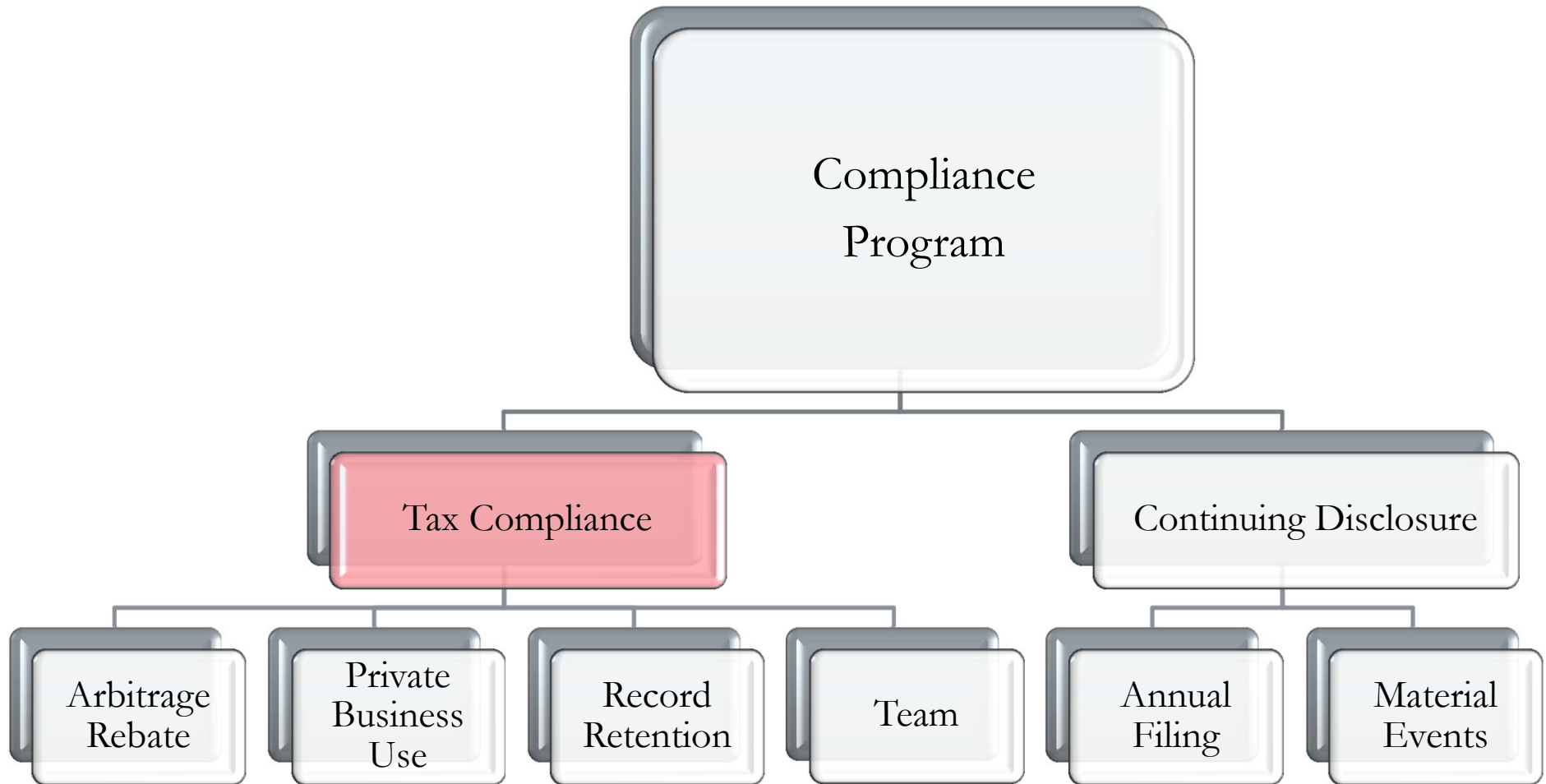
- Short Term Debt
 - TAN
 - RAN



Discussion Topics

- A Greater Focus on Compliance
 - How are facilities used?
 - On which projects were debt proceeds ACTUALLY spent?
 - What is reported to the financial markets?
 - Timely disclosure of information?
- Components of a Compliance Program
 - Tax Compliance
 - Continuing Disclosure

Components of a Compliance Program



A Change In IRS Focus

- Prior focus on pre-issuance type compliance problems
 - Is the project financeable with tax-exempt bond proceeds?
 - Less focus on post-issuance compliance, such as arbitrage rebate
- Beginning in 2007, shift in focus to post-issuance compliance
 - “Soft contact” surveys sent to 501(c)(3) organizations and governmental entities to assess post-issuance compliance
 - Significant increase in IRS audits
 - Emphasis on written policies and procedures to manage post-issuance compliance
 - Change in IRS Forms to include acknowledgement of written procedures
 - Additional changes in 2009 and 2011
- **Arbitrage rebate** is a significant part of post-issuance compliance
 - Also includes private business use compliance and related requirements

The New IRS Form 8038

Form **8038-G**
(Rev. September 2011)
Department of the Treasury
Internal Revenue Service

Information Return for Tax-Exempt Governmental Obligations

► Under Internal Revenue Code section 149(e)

► See separate instructions.

Caution: If the issue price is under \$100,000, use Form 8038-GC.

OMB No. 1545-0720

- 42 If the issuer has superintegrated the hedge, check box ►
- 43 If the issuer has established written procedures to ensure that all nonqualified bonds of this issue are remediated according to the requirements under the Code and Regulations (see instructions), check box ►
- 44 If the issuer has established written procedures to monitor the requirements of section 148, check box ►

- IRS revised Form 8038-G in September 2011 to include lines #43 and #44
- Issuers that are unable to check the boxes on the Form 8038 / 8038-G may receive greater scrutiny



IRS – Best Practices – Written Procedures

- Due diligence review at regular intervals;
- Identifying the official or employee responsible for review;
- Training of the responsible official/employee;
- Retention of adequate records to substantiate compliance;
- Procedures reasonably expected to timely identify noncompliance; and
- Procedures ensuring that the issuer will take steps to timely correct noncompliance.

Golden Rule: add on to IRS best practices is to have processes, procedures and internal controls that prevent failures



Latest IRS Perspectives on Written Procedures

- Recognize that many issuers have “something” in writing solely for the purpose of checking the box
- Issuers need to have “**effective**” written policies and procedures
- Next, in VCAP, issuers may need to demonstrate that they have adopted additional procedures so that the failure would not occur again

Compliance Program Administration

- Assigning responsibilities/designation of individuals
- Post Issuance Compliance Officer: Team includes Business Administrator, Accounting Supervisor, Legal, Purchasing/contracting
- Reporting responsibilities
- Ongoing review, modification, certification procedures
- Annual review by staff
- Review of assigned responsibilities; individuals assigned to monitor and manage post-issuance compliance
- Training and staff education
- This is applicable to both tax and continuing disclosure

Record Retention Requirements

- Requirements are burdensome and may not be consistent with document destruction policies
 - Life of the Bonds + 3 years
 - If the Bonds are refunded, life of refunding bonds + 3 years
- Consider separate document collection, storage and destruction policies for bond related records
- Consider electronic storage systems



Use of Proceeds

- Use of proceeds
- Financed project
- What is an expenditure? (outlay vs. earmarking/encumbering funds)
- Capital expenditures and working capital expenditures
- Allocation methodology options
- Capital expenditure allocation options
- Working capital limitations and exceptions- beyond today's scope
- Timing of allocations
- Reimbursements & reimbursement resolutions
- Project completion; documentation/certification of project completion (occupancy certificate?)
- Costs of issuance

Accounting For Bond Proceeds

- Significant factor in determining arbitrage rebate and yield restriction liabilities
- Permitted to use any reasonable, consistently applied accounting method to account for gross proceeds, investments, and expenditures of an issue
 - Examples: FIFO, direct tracing, ratable allocation, gross proceeds spent first
 - Proceeds are allocated to an issue until they are spent (**actual cash outlay**)
- Expenditure reallocations are permitted, however there are time limits
 - Expenditure allocations must be made no later than 18-months after the later of the expenditure date or the date the project is placed in service
 - Must be made no later than 60 days after five-year anniversary/final maturity date
- Proceeds of working capital financings (e.g., TANS, TRANS) subject to “proceeds-spent-last” requirement

Use of Proceeds & Accounting Procedures

Category		Procedure
Financed Projects	→	Verify use of proceeds for approved projects
Reimburse with bond proceeds	→	Adoption of Reimbursement Resolution
Project Completion	→	Require Occupancy Certificate, Completion Certificate
Spend-down Requirements	→	Monitor 6-mo spending benchmarks
Expenditure Allocations	→	Consistent method to allocate bond proceeds no later than 18-months after expenditure date
Pooled Inv. Approach (Commingled Fund)	→	Ratable allocation of investment earnings on periodic basis (no less than quarterly)

Arbitrage Rebate & Yield Restriction Compliance

- Determine the yield for arbitrage purposes
- Compile and maintain a list of bonds in need of rebate and yield restriction calculations
- Monitor compliance with exceptions
- Identify temporary periods
- Monitor compliance with yield restriction requirements
- Perform calculations no later than 5-year anniversary dates and final maturity dates (may be earlier than 5-years)
- Make payments no later than 60 days after computation date
- Initiate corrective steps if payments are not made timely, or if other violations are identified
- If 501(c)(3) filing IRS Form 990 Schedule K, report date that required rebate calculations were completed



Arbitrage Rebate – Follow the Money!

- There may not be any anticipated liability
- You must complete and keep even if the liability is \$0
- Bond covenants and IRS regulations are not predicated on completion only when you anticipate a liability
- **REALLY IMPORTANT:** the arbitrage rebate computation is the financial roadmap that an IRS uses to trace the expenditure of proceeds and by extension, the facilities financed.
- IRS Consistency Requirement for Sections 141-150 of the Code

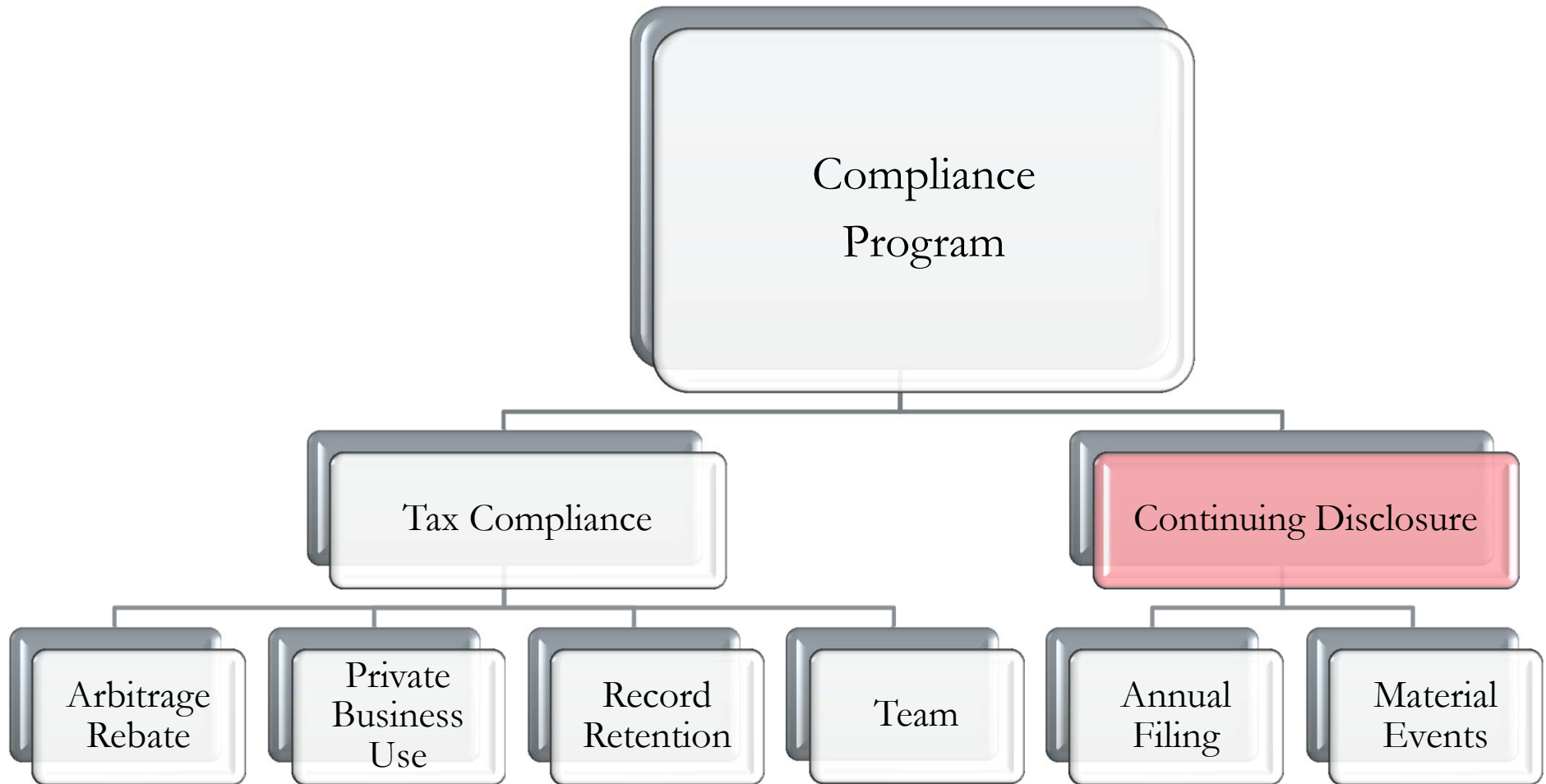


Private Business Use

- Tax law limits private use of TE financed facilities to 5% for unrelated use, 10% for related use
 - Example: Lease space to religious organization
- Maintain records of business activities and measure private business use periodically
- Require legal counsel review of all management & service agreements, leases, sub-leases, naming rights contracts, etc.
- Coordinate use of tax-exempt-bond financed facilities with administrative team to ensure compliance



Components of a Compliance Program



Continuing Disclosure

- Annual filing requirements
- Mandatory filings
- Voluntary filings
- Material Events
- EMMA System
- Recent MCDC Initiative shows failings by many



**"Our financial report stinks so bad, when
I brought it home, my dog rolled on it!"**

Where Do I File Disclosure Documents

- Issuers/Borrowers are required to file disclosure documents on MSRB's EMMA system (msrb.org)

The screenshot shows the MSRB EMMA website homepage. At the top left is the MSRB logo (Municipal Securities Rulemaking Board). To its right is the text "EMMA - Electronic Municipal Market Access" and "The Official Source for Municipal Disclosures and Market Data". In the top right corner, there are links for "Home | Alerts | Feedback | Contact". Below the header is a navigation bar with tabs for "About EMMA", "Muni Search", "Market Activity", "Education Center", and "EMMA Dataport". A "Muni Search" box is located in the top right, containing a search input field labeled "Enter CUSIP or Name" and buttons for "Advanced Search" and "Search Help".

The main content area features a "Muni Search" section on the left with a search input field and a "Welcome to EMMA" section on the right. The "Welcome to EMMA" section includes a paragraph: "EMMA is the comprehensive source for official statements, continuing disclosure documents, advance refunding documents and real-time trade price information on municipal securities." To the right of this is a "New Developments" box titled "MSRB Publishes 2010 Fact Book" dated March 09, 2011, with a "View All News" link.

Below the main content are three columns of information:

- EMMA EDUCATION CENTER:** "In our Education Center you can find a wealth of information to help you learn more about tax-exempt bonds and notes, taxable munis, 529 college savings plans and the full constellation of municipal securities." Includes a link "Getting Started on EMMA".
- MARKET ACTIVITY:** "View market-wide information about municipal securities, including recent trades, daily summaries of market transactions, official statements for new issues and recent advance refundings of outstanding bonds." Includes a link "Trade Activity".
- DOCUMENT SUBMISSION:** "Municipal bond underwriters and issuers submitting official statements, advance refunding documents and continuing disclosures to EMMA may do so through the EMMA Dataport. Submitted documents are made available to the public."

What Needs to be Submitted?

- Refer to official statements, continuing disclosure agreements
 - Annual/periodic filings & Material Event notices
- Examples for a school district:
 - Financial Statements (annual)
 - FTE student enrollment, teachers, schools
 - Tax levies and collections, sales tax collections
 - Millage rates
 - General and Capital projects funds revenues/expenditures
 - Direct and overlapping debt
 - Millage coverage tables

Material Events

- Principal and interest payment delinquencies
- Non-payment related defaults, if material
- Unscheduled draws on debt service reserves
- Unscheduled draws on credit enhancements
- Substitution of credit or liquidity providers or their failure to perform
- Adverse tax opinions, IRS notices or material events affecting the tax status of the security
- Modifications to rights of security holders, if material
- Bond calls, if material, and tender offers
- Defeasances
- Release, substitution or sale of property securing repayment of the securities, if material
- Rating changes
- Bankruptcy, insolvency, receivership, or similar event of the obligated person
- Merger, consolidation, or acquisition of the obligated person
- Appointment of a successor or additional trustee, or the change of name of a trustee, if material

Voluntary Disclosures

- Financial-based disclosures such as.....
 - Monthly financial information
 - Change in fiscal year or accounting standard
 - Budget
 - Investment/debt/financial policy
- Event based disclosures such as.....
 - Amendment to continuing disclosure document
 - Notice to investor pursuant to bond documents
 - Communication from the IRS
 - Litigation/enforcement action
- *Source: msrb.org*

The SEC Acts on Continuing Disclosure

- MCDC Initiative
- Need to develop written policies and procedures similar or part of tax post issuance procedures
- Confirm continuing disclosure requirements before bond closing - standardized
- Tickler
- Assure that postings are on EMMA, timely



Other Disclosure Concerns

- Should you have disclosure counsel?
- Should you use an external dissemination agent?
- What material event disclosures should your external dissemination agent bring to you?
- You hired an external dissemination agent – what more should you do (monitoring for accuracy, timeliness and completeness)?
- Business risk versus personal exposure.

Nabors
Giblin &
Nickerson P.A.
ATTORNEYS AT LAW

THANK YOU!



40 Years of
Independent
Advice
The PFM Group
Financial & Investment Advisors

I'm guessing the Powerpoint presentation
must've been a tad lengthy.

