

CDIAC

**CALIFORNIA
DEBT AND
INVESTMENT
ADVISORY
COMMISSION**

**CDIAC'S 18TH ANNUAL
BOND BUYER PRE-CONFERENCE**
ADMINISTERING DISCLOSURE OBLIGATIONS UNDER
AMENDED SEC RULE 15C2-12

September 23, 2019

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SESSION 1

THE FACTS: AMENDED SEC RULE 15C2-12

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September 23, 2019

Overview

- The Securities Exchange Commission has recently amended Rule 15c2-12 in ways that (1) will require a much deeper dive into the financial and operating condition of issuers/obligated persons than the Rule previously did and (2) will necessitate new procedures by issuers/obligated persons to ensure that they comply with the amendments.
- The goals of today's sessions are:
 - Provide context and background for the Rule amendments
 - Provide an overview of the new requirements
 - Identify the key questions issuers should be thinking about
 - Get a sense of how other issuers are dealing with these new requirements

Why did the SEC adopt the Amendments?

The SEC remains concerned about the municipal securities market:

- ❑ The SEC published a study on the market in 2012 in which it expressed several concerns about the market, including the lack of transparency of the financial and operating condition of issuers after bonds are issued.
- ❑ The SEC has brought substantial enforcement activity over the last six years designed to bring better care by issuers and other market participants, both in primary offerings and in compliance with continuing disclosure undertakings.
- ❑ The SEC has amended Rule 15c2-12 twice in the last ten years to improve transparency of the financial and operating condition of issuers after bonds are issued.

Why did the SEC adopt the Amendments?

Institutional investors have consistently raised significant concerns about issuers who entered into bank loans and did not disclose those bank loans to the market on a timely basis:

- Some issuers did not disclose that they had incurred bank loans at all and sometimes those bank loans represented a material increase in overall debt of the issuer.
- Some issuers did disclose that they had incurred bank loans but failed to disclose major features of the bank loans that negatively affected holders of bonds such as security terms, covenant and default terms, and other structural aspects of the bank loans that left public bondholders at a disadvantage to the bank lender.
- **In August 2018, the SEC adopted the amendments to Rule 15c2-12 to affirmatively require obligated persons to disclose financial obligations and their material terms.**

What did the Rule require before the Amendments and still does require?

- Underwriters of publicly offered municipal securities are required to ensure that municipal issuers and obligors enter into a continuing disclosure undertaking (CDA) that requires them to provide specified information annually.
- This includes:
 - Filing of audited financial statements
 - Providing notice within 10 business days of the occurrence of 14 specifically identified events (“Material Events”).
- Continuing disclosure notices must be posted on the Electronic Municipal Market Access “EMMA” website of the Municipal Securities Rulemaking Board.

2018 Amendments to Rule 15c2-12

Two new material events must be included in Continuing Disclosure Agreements for bond offerings. These notices must be posted on EMMA within 10 business days of the event.

New Event 15

New or amended “financial obligation” – if material*

*if a reasonable investor would consider it as a significant factor in making the investment decision, based on the total facts and circumstances

New Event 16

Default, acceleration event, termination event, modification of terms or similar events under a “financial obligation,” any of which reflect financial difficulties

What is a “financial obligation”?

Debt

Direct purchase by an investor

Loan from a bank or government agency

Line of credit

Lease entered into to borrow money

Obligation that could affect

- Obligor’s liquidity
- Obligor’s credit
- Obligor bondholders’ rights

Derivative

Derivative instrument entered into in connection with, or pledged as security or a source of payment for, an existing or planned debt obligation

Guarantee

Guarantee of a debt obligation or derivative instrument – includes self-liquidity and other contingent arrangements

A “financial obligation” does not include...

Ordinary financial and operating liabilities

- Most equipment leases
- Non-recourse leases
- Vehicle fleet leases from dealer
- Most rental leases
- Vendor leases

Plus...

- Derivatives used to manage investment risk or commodities risk
- Obligations arising from legal proceedings
- Securities offered using an Official Statement

What makes people go, “huh”?

- What is a *material* financial obligation?
- How does an issuer determine if a lease is a financial obligation?
- What are financial difficulties?
- If a default arising from financial difficulties occurs, does it matter if the financial obligation is material or not?
- What are financial difficulties?
- What are underwriters looking for on the first issuance (the first issuance of municipal securities after the effectiveness of the Amendments)?
- What due diligence are underwriters likely to perform on future offerings?

What should issuers consider in developing or amending policies and procedures?

- Do you know when your entity incurs or amends a financial obligation?
- Do you have a sense of what financial obligations your entity is likely to incur or amend?
- Do you have a sense of what your entity does that could present questions of interpretation?
- Do you have a way to monitor your entity's outstanding financial obligations for defaults and similar events?

What should issuers consider in developing or amending policies and procedures?

- Do you have an approach for determining materiality? Financial difficulties?
- Do the right people know what they are responsible for doing?
- Do you have an approach for filing an event notice when a reportable event occurs?

What process should issuers follow in developing policies and procedures?

- Make sure the “right” people are in the room:
 - **Finance personnel** who are directly involved in incurring, amending and modifying financial obligations;
 - **Knowledgeable counsel** – whether internal issuer counsel or outside bond counsel – to advise on what the Rule requires and assist with interpretative questions; and
 - **Other appropriate personnel** such as personnel who may know of financial obligations the issuer incurs or of what is needed to comply with covenants.

What process should issuers follow in developing policies and procedures?

- Make an inventory of what the issuer has done and is likely to do:
 - What financial obligations does the issuer incur and modify?
 - What covenants has the issuer agreed to?
- Decide what process the issuer will follow (with respect to the questions on the prior slides) and who will be responsible for what.
- Write it down into a policy.

New Amendments, Effective February 27, 2019:

15) Incurrence of a “financial obligation” of the obligated person, if material, or agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation of the obligated person, any of which affect security holders, if material

16) Default, event of acceleration, termination event, modification of terms or other similar events under a financial obligation of the obligated person, any of which reflect financial difficulties

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LUNCH

**NOB HILL ROOM
PROGRAM RESUMES IN 1 HOUR**

September 23, 2019

Session 3

How Public Agencies Are Responding



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**Christine
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Partner,
Orrick Herrington
& Sutcliffe LLP

Question 1

How are issuers getting ready to go to market for the first time under the new Rule?

Question 2

How are issuers perceiving the underwriter's due diligence during the offering?

Question 3

How are issuers managing ongoing post-issuance compliance?

Question 4

What are everyone's final thoughts and key takeaways regarding the new amendments?

Session 4

What Do Underwriters Expect from Issuers

What does the new amended rule mean to underwriters?

Underwriter and issuer collaboration.

Two new events that require posting to EMMA within 10 days of their occurrence.

Reminder about how regulators evaluate these issues.



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UPCOMING CDIAC PROGRAMS

GREEN BONDS IN THE GOLDEN STATE:

A PRACTICAL PATH FOR ISSUERS

WEBINAR 3: MAKING GREEN PENCIL OUT

OCTOBER 2 | WEBINAR

MUNICIPAL MARKET DISCLOSURE

OCTOBER 30, 2019 | IRVINE

PUBLIC FUNDS INVESTING WORKSHOP

NOVEMBER 19, 20, 2019 | WEST SACRAMENTO

CMTA/CDIAC ADVANCED PUBLIC FUNDS INVESTING

JANUARY 15-16, 2020 | CLAREMONT

**PLEASE COMPLETE EVALUATION AND LEAVE AT
YOUR TABLE.**

September 23, 2019