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# SEC MUNICIPALITIES CONTINUING DISCLOSURE COOPERATION INITIATIVE: A CALL TO ALL MUNICIPAL ISSUERS

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April 28, 2014

10:00 AM – 11:00 AM

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# **SEC MUNICIPALITIES CONTINUING DISCLOSURE COOPERATION INITIATIVE: A CALL TO ALL MUNICIPAL ISSUERS**

## **SPEAKERS**

**DANIEL DEATON**  
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**PETER H.M. CHAN**  
ASSISTANT REGIONAL DIRECTOR  
DIVISION OF ENFORCEMENT  
SECURITIES AND EXCHANGE COMMISSION  
CHICAGO, IL

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# SEC MUNICIPALITIES CONTINUING DISCLOSURE COOPERATION INITIATIVE: A CALL TO ALL MUNICIPAL ISSUERS

DANIEL DEATON  
NIXON PEABODY LLP



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# WHAT IS THE MCDC INITIATIVE?

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The MCDC Initiative is a Municipal Continuing Disclosure Compliance initiative of the Division of Enforcement of the SEC that:

- ▣ Addresses instances in which issuers have issued bonds and underwriters have underwritten bonds with offering documents that misrepresented the past continuing disclosure compliance by the issuer; and
- ▣ Offers issuers and underwriters favorable settlement terms for voluntarily self-reporting potential violations of the federal securities laws in connection with those misrepresentations.

# WHAT IS THE MCDC INITIATIVE?

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Misrepresentations in offering documents may constitute violations of the federal securities laws:

- Information concerning past continuing disclosure compliance can constitute material information to investors;
- Investors need and are entitled to ongoing financial and operating information concerning the issuer in order to make informed investment decisions of whether to buy, hold or sell bonds;
- When offering documents state that an issuer is in material compliance with their past continuing disclosure undertakings, investors purchase the bonds with the belief that the issuer will be likely to provide it timely financial and operating information; and
- Thus, if the offering document is inaccurate concerning that past continuing disclosure compliance of the issuer or obligated person, it can constitute a violation of the federal securities laws.

# WHAT IS THE MCDC INITIATIVE?

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The SEC Enforcement Division is offering favorable settlement terms to resolve these potential violations of the federal securities laws:

▣ Issuers:

- Enforcement Division will recommend no penalties;
- Issuers agree to implement procedures, correct deficiencies and take other actions;
- Entry into a consent decree promising no future violation of federal securities law; and
- No admission of wrongdoing.

# WHAT IS THE MCDC INITIATIVE?

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The SEC Enforcement Division is offering favorable settlement terms to resolve these potential violations of the federal securities laws:

▣ Underwriters:

- Enforcement Division recommends penalties ranging from \$20,000 to \$60,000 with a cap of \$500,000;
- Underwriters agree to implement procedures and take other actions, including hiring an independent consultant and cooperating with the SEC in any investigation of the potential violations;
- Entry into a consent decree promising no future violation of federal securities law; and
- No admission of wrongdoing.



# WHAT IS THE MCDC INITIATIVE?

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## What are the undertakings for issuers?

- Establish appropriate policies and procedures and training regarding continuing disclosure obligations within 180 days of the institution of the proceedings;
- Comply with existing continuing disclosure undertakings, including updating past delinquent filings within 180 days of the institution of the proceedings;
- Cooperate with any subsequent investigation by the Enforcement Division regarding the false statement(s), including the roles of individuals and/or other parties involved;
- Disclose in a clear and conspicuous fashion the settlement terms in any final official statement for an offering by the issuer within five years of the date of institution of the proceedings;
- Provide the SEC staff with a compliance certification regarding the applicable undertakings by the issuer on the one year anniversary of the date of institution of the proceedings; and
- Cease and desist from any future federal securities law violations.

# WHAT IS THE MCDC INITIATIVE?

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## How do you self-report?

- ▣ File before midnight (Eastern Time) on September 10, 2014 (which is really September 9, 2014!)
- ▣ Complete a questionnaire that identifies the municipal securities offerings in which the inaccurate statements were made and other information.

# AN EXAMPLE

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West Clark Community Schools is an example of the type of violations of the Federal antifraud laws that the MCDC Initiative is targeting.

What happened?

- The official statement prepared in 2007 for a bond offering on behalf of West Clark Community Schools stated that it was in compliance with its disclosure obligations related to prior bond offerings.
- West Clark had not submitted any of the required annual reports or notices pursuant to a continuing disclosure undertaking entered into for 2005 bond offering.
- The SEC found that West Clark had violated the federal antifraud laws by misstating its continuing disclosure history in its 2007 offering.
- The SEC found that the underwriter violated the federal antifraud laws too because it did not perform adequate due diligence in the offering.

**\*\*\*NOTE:** *The federal antifraud violation was not the failure to file the continuing disclosure filings, but the misstatement of that failure in the 2007 offering.*

# WHAT ARE SOME THINGS TO KNOW

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## What are some things you should know about the MCDC Initiative?

- The initiative does not cover individuals and they remain exposed to uncertain action by the SEC;
- If an issuer does not take advantage of the MCDC Initiative:
  - The Enforcement Division offers no assurances as to any settlement terms if the Enforcement Division pursues such violations not reported by the issuer; and
  - The Enforcement Division will likely seek financial sanctions against issuers; and
- The Enforcement Division has assured the municipal markets that there will be substantial enforcement activity following the close of the MCDC Initiative.

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# WHAT SHOULD ISSUERS DO?

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## Did you do an offering in the last five years?

- ▣ Were you subject to a continuing disclosure undertaking?
- ▣ Were you in compliance?
  - Did you timely file your annual reports in the proper place and under the proper CUSIP numbers?
  - Did the annual reports contain everything required by your continuing disclosure undertaking?
  - Did you fail to timely file any material event notices?
- ▣ If you had any material non-compliance problems, were those non-compliance events properly disclosed to investors in each subsequent offering document?

# WHAT SHOULD ISSUERS DO?

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- ❑ If you are concerned that you may have misstated your compliance, this is an opportunity to resolve the problem.
- ❑ The SEC will recommend favorable settlement terms so that issuers do not need to pay anything so long as they agree to the undertakings and the other terms of the MCDC Initiative.

# WHAT DO WE RECOMMEND?

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- ❑ Be aware of whether you have misstatements concerning continuing disclosure compliance that can be resolved through the MCDC Initiative:
  - ❑ It ends quickly; and
  - ❑ SEC enforcement activity will likely increase after it ends.
- ❑ Contact your bond counsel and/or disclosure counsel and your city attorney, county counsel or general counsel. ***Do not proceed without legal advice—filing the MCDC Initiative is a very important decision that has legal consequences.***



# WHAT DO WE RECOMMEND?

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- ❑ Communicate with any underwriters for bonds you issued in the last five years:
  - ❑ If you are going to file with respect to any such bond issue under the MCDC Initiative, they will want to know; and
  - ❑ If they are going to file with respect to any such bond issue under the MCDC Initiative, you will want to know.
- ❑ The MCDC Initiative may require some underwriters to process many offerings and communications between issuers and underwriters will be important.