Due Diligence Considerations in Primary Offerings of Municipal Securities

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The purpose of this paper is to provide members of the National Association of Bond Lawyers with tools and procedures for consideration when undertaking due diligence reviews for their obligated person[1] and underwriter clients in connection with primary offerings of municipal securities. After establishing a working definition of due diligence, this paper considers why due diligence is undertaken, when due diligence is undertaken, where due diligence is undertaken, and how due diligence is undertaken. The appendices include a diligence questionnaire matrix that lists categories of information that might be helpful in the due diligence process and bibliographies of primary and secondary sources that provide more in-depth treatment of the subject, including relevant enforcement actions by the U.S. Securities and Exchange Commission ("SEC").

This paper is not intended to provide an exhaustive treatment of due diligence tools and procedures and should not be read to make any suggestion of, or establish any presumption as to, any best practices in connection with primary offerings of municipal securities.

1. WORKING DEFINITION OF DUE DILIGENCE

The Municipal Securities Rulemaking Board ("MSRB") defines "due diligence" as follows: "The term commonly used to refer to the investigation made by underwriters, usually with the assistance of counsel, in part to determine the accuracy and adequacy of the [offering document][2] and to discover information that may be required in an [offering document] to ensure its completeness."[3] This definition is a good starting point for developing a working definition of due diligence, but it should be broadened to cover other participants in the offering process.

Obligated persons are primarily responsible[4] for the content of disclosures in offering documents, and the SEC also considers underwriters to be critical gatekeepers regarding the information provided in offering documents used in connection with offerings of municipal

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[1] The term "obligated person" means any person, including an issuer of municipal securities, who is either generally or through an enterprise, fund or account of such person committed by contract or other arrangement to support payment of all, or part of the obligations on the municipal securities to be sold in the offering (other than providers of municipal bond insurance, letters of credit, or other liquidity facilities). *See* 17 CFR 240.15c2–12(f)(10). The issuer is generally the primary participant in most primary offerings of municipal securities. In traditional municipal securities offerings, the issuer is a state, city, county, or local authority (e.g., sewer authority or water board). An issuer may also be a special purpose governmental authority, program issuer, or other independent public entity acting on behalf of a governmental unit (e.g., industrial development board, education or health facilities authority, etc.). *See* AMERICAN BAR ASSOCIATION SECTION OF STATE AND LOCAL GOVERNMENT LAW, AMERICAN BAR ASSOCIATION SECTION OF BUSINESS LAW COMMITTEE ON FEDERAL REGULATION OF SECURITIES & NATIONAL ASSOCIATION OF BOND LAWYERS, *Disclosure Roles of Counsel In State and Local Government Securities Offerings*, ch. 2 § A(1), at 54-55 (3d ed. 2009) ("*Disclosure Roles of Counsel*"). In a conduit financing, an issuer issues municipal securities to raise funds for another entity, "thereby bestowing the benefits of tax-exempt financing upon that entity." *Id.* The conduit borrower's credit generally secures the bonds, and thus, the borrower bears primary responsibility for disclosure and financial obligations, not the issuer. The conduit borrower is typically an "obligated person" for purposes of primary and continuing disclosure obligations.

[2] *See infra* note 8 for an explanation of use of the term "offering document" in this paper.

[3] MSRB GLOSSARY OF MUNICIPAL SECURITIES TERMS, http://www.msrb.org/en/glossary (last visited Feb. 22, 2021).

[4] *See infra* note 29.

securities[5]; however, other parties also have responsibilities regarding the accuracy of disclosures in connection with such offerings.[6]

To assist in developing a working definition of due diligence, counsel should consider that the due diligence process in primary offerings[7] of municipal securities takes place in the context of the preparation of offering documents.[8] This preparation process is oftentimes guided by the following two questions:

- What should one include in an offering document for municipal securities?
- How should one undertake a reasonable investigation into the accuracy and completeness of the material information in such offering document?

Consideration of what information should be included in an offering document has been, and continues to be, addressed in a number of publications[9] and is beyond the scope of this paper. Instead, this paper focuses on how one should undertake a reasonable investigation into the

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[5] *See SEC Charges Muni Bond Underwriter with Gatekeeper Failures*, https://www.sec.gov/news/press-release/2017-77.

[6] *See Report on the Municipal Securities Market, U.S. Securities and Exchange Commission* (July 31, 2012), https://www.sec.gov/news/studies/2012/munireport073112.pdf; *Disclosure Roles of Counsel*, *supra* note 1,ch. 2 §§ A-B. Other participants in primary offerings of municipal securities, including conduit borrowers, credit enhancers and liquidity providers, municipal advisors, lawyers, and investment providers, have disclosure responsibilities in connection with their respective roles in a particular offering. *See Id.*, ch. 2 § A, at 55-60.

[7] Under Rule 15c2-12(f)(7), the term primary offering means an offering of municipal securities directly or indirectly by or on behalf of an issuer of such securities, including any remarketing of municipal securities: (i) that is accompanied by a change in the authorized denomination of such securities from $100,000 or more to less than $100,000; or (ii) that is accompanied by a change in the period during which such securities may be tendered to an issuer of such securities or its designated agent for redemption or purchase from a period of nine months or less to a period of more than nine months. While the SEC has not provided guidance on the term primary offering, the SEC staff noted that the examples provided Rule 15c2-12(f)(7) are illustrative only and do not define the universe of remarketings that are subject to Rule 15c2-12. *See* Letter to Pillsbury, Madison & Sutro from the SEC (March 11, 1991), http://www.msrb.org/~/media/Files/MISC/15c2-12RemarketingLetter.ashx?la=en.

[8] An "offering document" is typically prepared by or on behalf of an issuer or conduit borrower in connection with an offering of municipal securities and typically includes information regarding the purpose of the issue, how the securities will be repaid, and the financial and economic characteristics of the obligated person with respect to the offered securities. An offering document may be prepared in preliminary and final form to comply with the federal securities laws, including MSRB rules. Although this paper generally uses the term "offering document", in a number of instances, the term "official statement" is used since that is the term used in SEC Rule 15c2-12. In addition, while this paper's focus is on due diligence in connection with preparing an offering document, due diligence may be conducted in connection with continuing disclosure documents and certain public statements, depending on the facts and circumstances.

[9] *See, e.g.*, *Disclosure Roles of Counsel*, *supra* note 1, ch. 9, at 195; Collection of White Papers Regarding *Best Practices in Disclosure*, NATIONAL FEDERATION OF MUNICIPAL ADVISORS, https://www.nfma.org/best-practices-in-disclosure (last visited Mar. 1, 2021); NATIONAL ASSOCIATION OF BOND LAWYERS, *Crafting Disclosure Policies* (Aug. 20, 2015); NATIONAL ASSOCIATION OF BOND LAWYERS, *Federal Securities Laws of Municipal Bonds Deskbook*, ch. 11 (7th Ed. 2017); ROBERT D. POPE, GOVERNMENT FINANCE OFFICERS ASSOCIATION, *Making Good Disclosure: The Role and Responsibilities of State and Local Officials Under the Federal Securities Laws* (2001). *See also* the materials collected in Appendix B and Appendix C herein.

accuracy of information in an offering document. This process is what this paper calls "due diligence", and the end game for this process is to assist obligated persons, underwriters, and other responsible members of the working group in gaining comfort that an offering document complies with the antifraud provisions of the federal securities laws.[10]

2. CONSIDERATIONS ON WHY DUE DILIGENCE IS UNDERTAKEN

2.1 Legal Framework of Municipal Securities

The municipal securities market is extremely diverse and includes approximately 50,000 state and local issuers of municipal securities,[11] ranging from villages, towns, townships, cities, counties, territories, and states, as well as special districts, constituted authorities, school districts, utility districts, and water and sewer authorities.[12]

The municipal securities market does not have a statutory scheme for registration and reporting[13] both because municipal securities are exempt from registration under the Securities Act and because municipal securities issuers are not subject to reporting under the Exchange Act.[14] Offerings of municipal securities are, however, subject to the antifraud provisions of Section 17(a) of the Securities Act and Section 10(b) and Rule 10b-5 under the Exchange Act. [15] The SEC's investor protection efforts in the municipal securities market have primarily been accomplished through enforcement of the antifraud provisions of the federal securities laws, as well as through regulation of broker-dealers and municipal securities dealers (collectively, "broker-dealers"), SEC interpretations, and SEC oversight of the MSRB.[16]

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[10] The Securities Act of 1933 ("Securities Act") and the Securities Exchange Act of 1934 ("Exchange Act") were both enacted with broad exemptions for municipal securities from all of their provisions except for the antifraud provisions of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated under the Exchange Act. The antifraud provisions of the federal securities laws prohibit any person from making any untrue statement of material fact, or omitting any material facts necessary to make statements made, in the light of the circumstances under which they were made, not misleading, in connection with the offer, purchase, or sale of any security.

[11] *See MSRB, Self-Regulation and the Municipal Securities Market* (Jan. 2018), http://www.msrb.org/MarketTopics/~/media/8059A52FBF15407FA8A8568E3F4A10CD.ashx.

[12] SEC Chairman Cox, *Disclosure and Accounting Practices in the Municipal Securities Market* (July 26, 2007); *see also infra* note 13.

[13] *See* AMERICAN BAR ASSOCIATION SECTION OF STATE AND LOCAL GOVERNMENT LAW, AMERICAN BAR ASSOCIATION SECTION OF BUSINESS LAW COMMITTEE ON FEDERAL REGULATION OF SECURITIES, & NATIONAL ASSOCIATION OF BOND LAWYERS, *Disclosure Roles of Counsel In State and Local Government Securities Offerings* (3d ed. 2009) ("*Disclosure Roles of Counsel*").

[14] *Disclosure Roles of Counsel, Introduction*, § D, pp. 4-6. There are also transactional exemptions under the Securities Act.

[15] *Id.*

[16] *See supra* note 6.

Notably, and in contrast to the municipal market, the SEC's Division of Corporation Finance (the "Division") reviews certain filings of public companies made under the Securities Act and the Exchange Act to monitor and enhance compliance with the applicable disclosure and accounting requirements.[17] In addition, public companies are guided by SEC regulations and forms that dictate specific "line-item" disclosure.[18] Further, the SEC provides public companies with a vast library of SEC guidance, including compliance and disclosure interpretations, accounting and financial reporting guidance, financial reporting manuals, and no-action, interpretive, and exemption letters.[19] All of these documents, taken together, provide structure and guidance to companies when they draft and prepare offering documents.

Obligated persons and their counsel in the municipal securities market do not benefit from similar structure or guidance when drafting and preparing offering documents for investors. Instead, disclosure for municipal securities is primarily guided by accepted market practices and the application of the antifraud provisions of the federal securities laws in enforcement proceedings, including settlements of enforcement proceedings against obligated persons and other municipal finance participants. [20]

2.2 Due Diligence Requirements in Municipal Securities Offerings

The Securities Act does not include an affirmative obligation to investigate or verify statements made by an obligated person.[21] Rather, Section 11 of the Securities Act establishes the affirmative due diligence defense available for everyone except the issuer of registered securities in response to a liability claim. While Section 11 is not specifically applicable to municipal securities, undertaking due diligence in the same manner as might be undertaken in a registered offering is widely thought to protect underwriters from liability under the antifraud provisions of the federal securities laws (as they would be for registered securities offerings), including Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and the rules promulgated thereunder.[22]

Despite the absence of any explicit statutory requirement for underwriters of municipal securities or others to perform a due diligence investigation, the SEC has found implied duties under the various antifraud rules of the federal securities laws. To avoid fraud, the underwriter is

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[17] *See* SEC DIVISION OF CORPORATION FINANCE website, available at https://www.sec.gov/page/corpfin-section-landing.

[18] *Id*.

[19] *Id*. Although the SEC's guidance to public companies is not directly applicable to issuers of municipal securities, the guidance may be consulted to aid development of disclosure or due diligence materials in municipal securities offerings.

[20] *See Disclosure Roles of Counsel, Introduction*, § D, pp. 4-6; s*ee also* the various "White Papers" prepared by the NATIONAL FEDERATION OF MUNICIPAL ANALYSTS at https://www.nfma.org/best-practices-in-disclosure.

[21] ROBERT A. FIPPINGER, *The Securities Laws of Public Finance*, § 7:3.1[B] (PLI 3rd. ed.) ("FIPPINGER"), citing *SEC, Obligations of Underwriters, Brokers and Dealers in Distributing and Trading Securities, Exchange Act Release No. 9671* (July 26, 1972).

[22] John McNally, *"Due Diligence In the Context of Municipal Securities Underwriting"*, NABL QUARTERLY NEWSLETTER, March 1, 1997.

said to have a duty to make a reasonable investigation into the accuracy of the information presented in an offering document.[23] In the Proposing and Adopting Release for Rule 15c2-12 in 1988, the SEC states that an underwriting constitutes an implied recommendation about the underwritten securities and that such a recommendation cannot be made without a reasonable basis for the belief that the key information in the offering document complies with the antifraud provisions. Specifically, the SEC states:

> By participating in an offering, an underwriter makes an implied recommendation about the securities. Because the underwriter holds itself out as a securities professional, and especially in light of its position vis-a-vis the issuer, this recommendation itself implies that the underwriter has a reasonable basis for belief in the truthfulness and completeness of the key representations made in any disclosure documents used in the offerings.[24]

The 2010 Adopting Release[25] reaffirms the SEC's prior interpretations of the reasonable investigation requirement set forth in the Proposing Release and the Adopting Release. Further, in March 2012, the SEC's Office of Compliance Inspections and Examinations ("OCIE") issued a national examination risk alert entitled "Strengthening Practices for the Underwriting of Municipal Securities."[26] The risk alert summarizes the SEC's prior guidance that, by participating in an offering, an underwriter makes an implied recommendation about the securities it is offering. This risk alert emphasizes that underwriters have a duty under the antifraud provisions of the federal securities laws, in both negotiated and competitively bid offerings, to review the obligated person's disclosures in a professional manner with respect to accuracy and completeness of statements made in connection with an offering.[27] In addition to highlighting the SEC's prior interpretations, OCIE also states that, if an underwriter fails to undertake such efforts to form a reasonable belief, it may violate the antifraud provisions of the securities laws.[28]

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[23] *See* Proposed Amendments to Municipal Securities Disclosure – Rule 15c2-12, Exchange Act Release No. 34-26100 (Sept. 22, 1988), 53 Fed. Reg. 37778, 37787 (Sep. 28, 1988) (the "1988 Proposing Release"); FIPPINGER, *supra* note 21, § 7:3.1[B] (citing *In re* Dolphin & Bradbury Inc. v. SEC, 512 F3d 634 (D.C. Cir. 2008); Piper Jaffray & Co., Securities Act Release No. 9472 (November 5, 2013) (cease and desist order)).

[24] 1988 Proposing Release, *supra* note 23, at 37787 (emphasis added). The 1988 Proposing Release, in addition to proposing Rule 15c2-12, describes certain disclosure obligations of issuers, underwriters, and other participants in municipal securities offerings. Part III of the 1988 Proposing Release, which is entitled "Municipal Underwriter Responsibilities", describes the SEC's view of the disclosure and due diligence obligations of municipal securities underwriters in the context of various securities laws. *Id.*

[25] *See* Interpretive Guidance with Respect to Obligations of Participating Underwriters, Exchange Act Release No. 62184A (May 26, 2010), 75 Fed. Reg. 331003 (June 10, 2010) (the "2010 Adopting Release"). In Part IV of the 2010 Adopting Release accompanying amendments to Rule 15C2-12, the SEC describes its interpretations of the due diligence obligations of municipal security underwriters. *Id.*

[26] SEC OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS, *Strengthening Practices for the Underwriting of Municipal Securities*, National Examination Risk Alert, Mar. 19, 2012, https://www.sec.gov/about/offices/ocie/riskalert-muniduediligence.pdf.

[27] FIPPINGER, *supra* note 21, §7:3.4[C]

[28] *See supra* note 26.

Because obligated persons, like underwriters, are also subject to the antifraud provisions of the federal securities laws, obligated persons might be well-advised to consider how to document or evidence the absence of intent to defraud, recklessness, or negligence when preparing offering documents.[29] For example, an obligated person could document such absence by showing it used reasonable care in following reasonably designed disclosure policies and procedures, including the conduct of a reasonable diligence investigation, when preparing offering documents. By following reasonably designed policies and procedures, an obligated person would make it difficult for the SEC to demonstrate that the obligated person acted with intent to defraud or was reckless or negligent, which is a necessary element to establish a violation of the antifraud provisions. Following such policies and procedures is evidence that shows the obligated person used reasonable care when preparing the offering document.

2.3 Due Diligence Standards and Practices

As mentioned, obligated persons and underwriters are subject to the antifraud provisions of the federal securities laws. Accordingly, while their perspectives may differ on certain aspects of disclosure, both parties in an offering of municipal securities have a similar goal – avoiding violations of the federal securities laws. So obligated persons and underwriters typically must conduct a due diligence review of both the obligated person and the securities in connection with the preparation of the offering document and sale of the securities. Further, although counsel may be engaged to assist the parties with compliance with disclosure obligations, the obligated person, as the entity primarily responsible for the disclosure, and the underwriter, as the gatekeeper for underwritten primary offerings of municipal securities, are the primary responsible parties for the disclosure contained in the offering document. While it may be appropriate for the obligated person and the underwriter to rely on counsel for review of legal matters (including whether information is material to the offering), financial matters (e.g., revenue projections and debt service coverage ratios) should be reviewed by the obligated person and the underwriter. Such review should not be delegated to others, although an underwriter may satisfy a portion of its due diligence obligations by, for example, requesting accountants to review and report on financial statements.[30]

The standard of care for due diligence is dictated by the antifraud provisions of the federal securities laws. A violation of Section 17(a)(1) of the Securities Act and Section 10 (and Rule 10b-5) under the Exchange Act requires scienter; however, a showing of negligence is sufficient to prove a violation of Sections 17(a)(2) and (3) of the Securities Act. In *SEC v. Dain Rauscher, Inc.*,[31] the Ninth Circuit rejected the conclusion that compliance with industry standards alone may be adequate due diligence procedures. The court held that the standard of care for an underwriter of municipal offerings is one of reasonable prudence, for which the industry standard is only one

[29] *See In re* Richmond Corp., 41 S.E.C. 398, 406 (1963); Ernst & Ernst v. Hochfelder, 425 U.S. 185, 208 (1976).

[30] *Disclosure Roles of Counsel*, *supra* note 1, Introduction, ch. 6 § J, at 144.; s*ee Piper Jaffray & Co.*, Securities Act Release No. 9472 (November 5, 2013) (cease and desist order); *In the Matter of Donaldson, Lufkin & Jenrette Securities Corporation*, Securities Act Release No. 6959, 1992 WL 280784 (Sep. 22, 1992) (administrative proceeding); *see also* S.C. Nat'l Bank v. Stone, 139 F.R.D. 335, 341 (D.S.C. 1991).

[31] SEC v. Dain Rauscher, Inc., 254 F.3d 852 (9th Cir. 2001).

factor to be considered.[32] If the departure from that standard is extreme, the scienter element could be satisfied.[33]

Similar to an obligated person following reasonably designed disclosure policies and procedures, an underwriter following accepted standards of practice in the industry will continue to help evidence reasonable prudence in most circumstances. At the most general level of determining reasonable prudence, counsel should consider whether (1) there are red flags suggesting that the information in the offering document is misleading or omits material facts, (2) those participating in due diligence are critically evaluating the information they are given or are simply accepting the statements of the obligated person, and (3) if reasonable, those participating in due diligence are seeking outside sources of information in order to challenge or verify information.[34]

In conducting a due diligence investigation, one source of information for certain underwriters is the "reservoir of knowledge" within the underwriting firm, and an investment banker should consider reviewing such information, particularly for resolving any matters which may have arisen in the course of the due diligence review.[35] For example, in a proceeding against Credit Suisse First Boston[36] concerning the underwriting of Orange County's pension obligation bonds, the SEC stated that, despite the importance of certain investment pools in the offering and the media articles voicing concerns about the investment strategy of the pools, the investment bankers did not make any inquiry within their firm for information related to the pools.[37] The SEC further stated that, given that the information about the pools was known and readily available to them, the firm and the bankers made insufficient inquiry.[38] Such insufficient inquiry was a factor, among others, in the SEC's finding that the firm and bankers had violated the antifraud provisions of the federal securities laws.[39]

3. CONSIDERATIONS ON WHEN DUE DILIGENCE IS UNDERTAKEN

3.1 Considerations for Timing of Due Diligence

Due diligence is a continuous process throughout a transaction, from the first working group call through the closing. The more formal aspects of the due diligence process, such as the delivery of a questionnaire or a document request list, may commence at a later point in the transaction, particularly if the details of the transaction are not determined at the outset, such as

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[32] *Id*.

[33] *Id*. at 856 (citing Aaron v. SEC, 446 U.S. 680 (1980)).

[34] *See* FIPPINGER, *supra* note 21, §7:5.2[E].

[35] *See* MSRB Rule G-17, including related interpretations; *see also* FIPPINGER, page 7-128 [7:5.2 E].

[36] Credit Suisse First Boston Corporation, Securities Act Release 33-7498, 1998 WL 30378 (Jan. 29, 1998); *see* FIPPINGER, *supra* note 21, § 7:5.2[E].

[37] *Id*.

[38] *Id*.

[39] *Id*.

the source of payment and security, project description, and identification of transaction participants. The guiding principle as to when due diligence is undertaken is to strike the right balance among (1) having enough information about the transaction to tailor the formal requests to include relevant information, (2) providing sufficient time for the obligated person to produce the relevant information for thoughtful review, and (3) ensuring that the most current information available is provided so as to avoid multiple "updates". Depending on the experience of the obligated person, one might also build in time in advance of the formal due diligence requests for a discussion of the process and the relative responsibilities of the transaction parties.

3.2 Key Timing Considerations for the Due Diligence Process

There are certain timing "checkpoints" in a municipal securities transaction to take into consideration in planning the due diligence process for any publicly offered transactions (including limited placements using an offering document). These checkpoints include (1) the posting of the preliminary offering document or any supplement, (2) the execution of a bond purchase agreement, (3) the posting of the final offering document or any supplement, and (4) the closing and delivery of the municipal securities. Each of these checkpoints is significant; however, the time immediately prior to the posting of the preliminary offering document is the point at which all formal diligence review should be completed. From that point on, there should only be "bring-down" inquiries to provide assurance that no material developments have occurred that might necessitate additional diligence review.

As described later in this paper, it is typical in many publicly offered transactions (including limited offerings) that a due diligence meeting with the senior management team of the obligated person may be conducted fairly close in time to the posting of a preliminary offering document (e.g., a day or two prior to posting). The timing consideration is to have the responsible members of the working group agree that the preliminary offering document is ready to be posted to the market (something akin to a "speak now or forever hold your peace"). This acknowledgement occurring as close in time to the posting date as reasonable affords the underwriter and the obligated person a level of comfort that will support the giving of, and the reliance upon, certifications to be made in the bond purchase agreement and at closing as to the accuracy and completeness of the preliminary offering document as of its date and as of the date of the bond purchase agreement.

Bond purchase agreements typically include a representation by the obligated person that the preliminary offering document was accurate and complete (in typical Rule 10b-5 vernacular) as of its date and the date of the bond purchase agreement (except for permitted exceptions under Rule 15c2-12). This representation is important to the underwriter because it provides comfort that the offering document it has used to market the bonds it is about to purchase was accurate and complete under the securities laws. This representation serves as a "bring-down" of the diligence previously undertaken, but it will not absolve a transaction participant from liability if, in fact, the transaction participant knows or should have known the representation was false. Additionally, the bond purchase agreement typically includes an affirmative covenant on the part of the obligated person to notify the underwriter if, at any time from the date of the bond purchase agreement, any event occurs that would make the offering document contain an inaccurate or incomplete material statement.

The final offering document is typically prepared and circulated for review and comment by the working group soon after the bond purchase agreement is signed. The review and comment period is the opportunity for transaction participants to confirm the absence of material changes in the matters disclosed in the preliminary offering document.[40] Transaction participants typically rely on the affirmative covenant of the obligated person to disclose to the underwriter any circumstance that would result in the offering document not being accurate and complete. If an auditor is involved in the offering, a supplemental agreed-upon-procedures and consent letter may be obtained. The diligence process is an ongoing and continuous one and might include checking local headlines for any newsworthy developments (this is fairly simple today with internet searches). More complex transactions may include more formal bring-down diligence at this checkpoint.

At the closing of the transaction, the obligated person will again provide certification as to the accuracy and completeness of the final offering document as of its date and the date of delivery of the municipal securities. Additional bring-down of the due diligence may or may not be conducted through the closing, including with respect to any auditor's comfort that may be provided in the offering. In offerings of municipal securities that are subject to Rule 15c2-12, the underwriter is under a continuous duty to deliver a final official statement to any potential customer until the earlier of ninety days after the end of the underwriting period or the time when the official statement is available to any person on the MSRB's Electronic Municipal Market Access System ("EMMA") website, but in no case may this duty be abandoned less than twenty-five days after the end of the underwriting period.[41] A new diligence checkpoint is created anytime an offering document is supplemented, whether prior to or after closing.[42]

4. CONSIDERATIONS ON WHERE DUE DILIGENCE IS UNDERTAKEN

4.1 Overview

In determining where to conduct due diligence, it is best, to paraphrase a saying falsely attributed to bank robber Willie Sutton, to "go where the information is."[43] Information may be embodied within a document or collection of documents, within a unique set of records, on a web site, or within an individual's mind. In some cases, the information may even be embodied at the

[40] One must keep in mind that, at this point in time, securities typically have already been sold to investors so material changes to the preliminary offering document may give rise to investors refusing to honor their purchase commitments. *See generally* FIPPINGER, *supra* note 21, § 5.

[41] Rule 15c2-12(b)(4). This provision was originally included in Rule 15c2-12 to encourage the use of the document repositories ("NRMSIRs") and some commenters questioned whether such provision would be necessary after a single repository was created.

[42] Although beyond the scope of this paper, transactions involving the forward delivery of municipal securities potentially present additional checkpoints members of a working group should consider. *See* FIPPINGER, *supra* note 21, §§ 4 and 7.

[43] The story goes that Sutton was asked by a reporter why he robbed banks and retorted, "Because that's where the money is."

location of the project being financed. The nature of the source of information will dictate where diligence can or should be conducted.

As the last sentence implies, much of the information counsel will want to review as part of due diligence is retrievable by telecommunications or electronic means. Thus, the question of "where" due diligence is conducted is less about physical location[44] than it is about the medium through which information is communicated and the event within the transaction during which communication occurs. The medium through which due diligence is conducted can be an in-person meeting, a conference call, a delivery of documents (either physically or electronically), a response to an email inquiry, or an online video call. As for the event, most due diligence takes place through a dedicated, scheduled due diligence meeting or call. Nonetheless, counsel should consider due diligence to be a continuing process throughout the course of a transaction. Any meetings, consultations, or conference calls during which proposed or existing disclosure included in the preliminary or final offering document are discussed affords an opportunity to conduct due diligence.[45]

4.2 Meetings

The dedicated due diligence meeting—whether in-person, by telephone, or by video—has multiple advantages for conducting due diligence. For example, senior personnel gather at the dedicated due diligence meeting and this gathering provides the underwriter and its counsel with an opportunity to ask questions of the senior personnel. Their technical or operational expertise may be needed for specific parts of the preliminary and final offering documents, including confirming such disclosures. Further, senior personnel and experts may not participate in regular working group meetings where the contents of the offering document are discussed. This is also the opportunity to confirm the key representatives have reviewed the offering document. [46]

4.3 Site Visits and Tours

Site visits and tours of projects for securities secured by a revenue stream from a particular project or operation of the obligated person are more important than site visits and tours for securities secured by an obligated person's full faith and credit, collections of a generally applicable tax, or the general credit of an obligated person. In some instances (such as during the COVID-19 pandemic) it may be necessary to conduct a virtual site visit or tour (e.g., using a video camera, personnel may conduct a walk-through of the project site). In such situations, counsel should reserve the right to carry out follow-on virtual inspections to account for different perspectives or limited attendee in-person inspections, if permitted.

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[44] The authors observe that, as of this writing, the impact of the COVID-19 pandemic and its related restrictions on travel and gatherings of groups has caused counsel to adapt to telecommunication and electronic means as the primary way to conduct due diligence. This or other local, national, or international events in the future could affect the locations at which the due diligence process is conducted.

[45] *See* FIPPINGER, *supra* note 21, § 7:5.6, at 7-135.

[46] *Id*.

4.4 Document Reviews

Diligence document reviews can now be done largely anywhere, but the growing trend is to conduct them virtually, through a virtual data room.[47] The operative and closing documents of the transaction (for example, a bond resolution or trust indenture) can also be handled in this manner, although the differing nature of diligence documents may result in different handling procedures.[48] Many documents also may be publicly available on the obligated person's website or on the MSRB's EMMA website.

Due diligence documents are static; they must be to fulfill their intended purpose of undertaking a reasonable investigation into the accuracy of the statements in the preliminary and final offering documents. A virtual data room is ideal for handling such documents. Obligated persons that frequently access the municipal securities market may find it efficient to permanently establish a data room, as it will allow them to gather materials pertinent to multiple transactions once and update them for future use. The virtual data room also can be subdivided, so that access to more sensitive documents (or documents that may not be directly applicable) that are not required to be reviewed by all working group members (e.g., litigation documents or documents that may need to be shielded from government open records requests) can be limited.

There are certain practical considerations for counsel if they have input into the creation and organization of a virtual data room. Ideally, a virtual data room's architecture would allow documents to be categorized and grouped by type and sub-type to minimize the amount of unnecessary site exploration users have to undertake to find a document. In more complex transactions with multiple diligence purposes (e.g., a housing finance transaction with a heavy real estate focus) categorizing the documents by who requested the diligence may also be of benefit. The virtual data room also could have an email notification system alerting users when documents have been posted, changed, or removed, so users do not have to periodically search the room to see what changes have been made. Ideally, users would be able to configure their own notice profile to eliminate unwanted notices about documents for which they have no interest.

Virtual data room security is also important, and access should be limited to specified users because, among other things, certain diligence documents may contain confidential information. Users should further be required to establish a password and, if necessary, a second means of authentication as well. Passwords or authentications can be set to automatically terminate within a certain time after closing to preserve security. Alternatively, if the obligated person maintains a permanent data room, it can establish a temporary, transactional data room, migrate pertinent files over from the permanent room, and have the temporary room disappear when the transaction closes. In certain financing transactions, it may be necessary to have non-disclosure and

[47] Some transactions may instead use a file-hosting service, such as Dropbox, Google Drive, or Citrix ShareFile. Certain diligence documents may contain confidential information, including account numbers, telephone numbers, and email addresses. As such, care should be taken that the service used has sufficient security protocols.

[48] Operative documents are dynamic; they will continue to change as the transaction proceeds to consummation. If a data room or other file-hosting service is being used to distribute operative documents to the working group, authors will usually post all clean iterations of the documents for which they are responsible, as well as marked versions showing the changes between iterations. To help authors maintain control of the drafting process for their respective documents, common practice is for comments to documents to be sent directly to the authors (usually copying other relevant members of the working group), rather than posting them to the data room.

confidentiality agreements executed. For example, in certain health care financing transactions, it may be necessary to protect private health records.

5. CONSIDERATIONS ON HOW DUE DILIGENCE IS UNDERTAKEN

5.1 Variables Affecting Due Diligence Approaches

As counsel engaged by an underwriter or obligated person to assist in conducting a reasonable investigation as to the accuracy and adequacy of the information in an offering document, it is important to understand that the scope of a due diligence investigation by counsel will necessarily depend on the specific circumstances of the transaction, as well as the scope of the counsel's engagement and apportionment of duties. Counsel should be mindful of this variability in drafting its engagement letter with the underwriter, if any, or obligated person and should consider addressing the anticipated scope of the due diligence inquiry either in counsel's engagement letter with the underwriter or obligated person or in a separate writing.

In recent years, in-house legal departments for underwriters have developed general instructions or memoranda for counsel's representation, including, in some cases, the specific expectation of the apportionment of duties in the due diligence investigation, which may include deliverables from counsel. These instructions by in-house legal departments should be reviewed and discussed at the time of the engagement so that the terms for any particular transaction are clearly understood by both the underwriter and counsel.[49]

Factors that may impact the scope of counsel's due diligence review include, for example:

- *Type of financing*. The scope of due diligence review will depend on the type of financing at issue, which has long been cited by the SEC[50] as an important factor to consider in developing the appropriate scope of the due diligence inquiry. For example, the "due diligence responsibility is likely to increase when the type of bond being issued changes from a routine general obligation bond to a revenue bond or a private activity bond."[51]

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[49] SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION, *Model Memorandum to Underwriter's Counsel for New Issues of Municipal Securities* (September 26, 2018), https://www.sifma.org/wp-content/uploads/2018/09/SIFMA-Model-Memo-to-UW-Counsel.docx; *see also* NATIONAL ASSOCIATION OF BOND LAWYERS, *NABL Analysis of SIFMA Model Memorandum to Underwriter's Counsel* (Mar. 2019). Some underwriters may prefer to perform certain due diligence activities themselves, such as a review of the obligated person's compliance with SEC Rule 15c2-12. Counsel should be mindful of this variability in drafting its engagement letter with the underwriter, to the extent the underwriter will accept an engagement letter, and should consider addressing the anticipated apportionment of duties either in counsel's engagement letter with the underwriter, pursuant to an agreed-upon due diligence plan with the underwriter, or in a separate writing.

[50] *See* 1988 Proposing Release, *supra* note 23, at 37789 (listing, among other factors, the type of bonds being offered as a relevant factor is determining the reasonableness of an underwriter's basis for assessing truthfulness of disclosures made in offering documents).

[51] FIPPINGER, *supra* note 21, § 7.3.4(D).

- *Familiarity with the obligated person*. An underwriter's familiarity with an obligated person has also been referenced by the SEC as an appropriate factor to consider in calibrating the scope of the underwriter's due diligence inquiry.[52] For example, for certain long-established clients of an underwriter, an underwriter or its counsel may already have detailed information regarding the obligated person, so the due diligence inquiry may be appropriately limited to confirming the information already on hand and updating certain information since the last offering.

- *Lapse of time since last issuance*. In addition to an underwriter's familiarity with an obligated person, the lapse of time since the last issuance of the obligated person may be a factor to be considered in assessing the scope of the due diligence investigation. For example, for an obligated person who recently prepared and circulated on offering document, the underwriter may direct counsel to limit the inquiry about the period of time since the last offering and to inquire as to whether there have been any material changes in the key representations since the last offering. This, of course, assumes the underwriter was satisfied with the level of due diligence inquiry conducted in connection with the previous offering.

- *Presence of red flags*. Throughout the due diligence inquiry, regardless of the scope of engagement or type of offering, counsel should be alert to "red flags" that suggest further inquiry is warranted. For example, a response to an inquiry as to any ongoing litigation that "we currently have three active litigation matters" would typically lead to a follow-up inquiry into the nature of the claims at issue, the status of the litigation, the amount at dispute, and whether an unfavorable decision would have a material impact on the obligated person. Other possible red flags and follow-up inquiries include, for example:

    - Outdated financial information: Is there more recent financial information available?

    - Dramatic revenue trends or missed financial covenants: What is the source of the trend or circumstances leading to the covenant breach, and are the circumstances recurring?

    - Management or employee turnover: Was the turnover planned (for example, retirement) or unplanned?

    - Environmental reports noting significant recognized environmental conditions: Are these subject to federal or state investigation, and what is the magnitude of potential expense or liability?

[52] *See* 1988 Proposing Release, *supra* note 23, at 37789.

- Significant public opposition at public hearings or in local media: Depending on the status of the approvals, will the public opposition interfere with or affect final approval of the securities or the project?

- Feasibility studies that rely upon dramatic increase in revenues: What is the sensitivity analysis of the revenue projection?

5.2 Utilization of Checklists and Questionnaires in the Conduct of Due Diligence Review

There is a broad array of projects and industries financed in the public finance market, including education, utilities, convention centers, public infrastructure, and affordable housing. Some of the key representations made in offering documents are unique to the project and industry and are influenced by the issues relating to legal authority, regulatory matters, security, and political landscape surrounding that project, industry, particular jurisdiction, and particular obligated person.

The methodology to undertake a reasonable investigation into the key representations in an offering document is driven by the design of the offering document and the overall deal structure. Understanding the deal structure, including the project and the industry, will inform what questions to ask and where to focus. A general basic checklist, questionnaire, or matrix may be helpful as a starting point; however, such tools are only part of the diligence process.[53]

If utilizing a checklist or questionnaire, consider the broad categories of information that might be elicited, such as:

- Organizational or authorizing documents: This might include a request and review of the organizational documents, statutory provisions, or similar information about the valid existence of the obligated person.
- Authority for the issuance of the securities: This will vary by jurisdiction but would address federal, state, and local authority for the particular securities issuance and the particular project being financed.
- Required approvals for the issuance of the securities and the project: This will also vary by jurisdiction and type of transaction but may include state or local legislation (e.g., ordinances, resolutions, etc.).
- Nature of the security for the obligations: This section will be wholly dependent upon the particular transaction and may include information about eligibility to receive pledged revenues, historical receipts, trends, economic risks, and underlying contracts.
- Financial condition of the obligated person: This broad category may include a request and review of historical financial information, including pension and OPEB liability, material litigation and investigations, and budgetary information.

[53] *See generally* FIPPINGER, *supra* note 21, § 7.

Consider placing an emphasis on current information, even if unaudited, rather than relying solely on historical data.

- Future expected financial and operating condition of the obligated person: The SEC[54] has suggested that the current financial and operational impacts and the potential future impacts of COVID-19 and other events on the obligated person be fully disclosed in an offering document.
- Management information about the obligated person and project: This may include inquiry as to the experience and credentials of management, as well as any expected changes in management and succession plans and any plans for addressing any financial deficits or declines.
- Information about the status and the development of the project: This is particularly relevant for project-finance and real estate transactions and start-up projects (e.g., charter schools, healthcare facilities, affordable housing, industrial and manufacturing facilities). This can include economic factors that could affect receipt of revenues to pay bondholders such as general demographic and economic trends affecting ratepayers, taxpayers, student enrollment, tenant leases, TIF developers, casino attendees, hospital admittance, demand for products and services, and availability of feedstock.
- Federal, state law and regulatory factors influencing the offering: This may include specific state, local, or federal approvals that must be obtained in advance of issuing the debt, or before the obligated person may operate the project.
- Obligated person's internal policies regarding debt, investments, and disclosure: This inquiry may include whether there are written policies, whether the policies are reasonable, and whether the policies are followed.
- Compliance with prior continuing disclosure undertakings: This is a key area of focus by the SEC, as evidenced by the SEC Division of Enforcement's 2014 Municipalities Continuing Disclosure Cooperation Initiative.[55]
- Other specific information necessary to be discussed in the offering document: This is a catch-all category, but serves as a reminder that the representations made in the offering document should drive the due diligence inquiry.

Understanding the unique characteristics of a particular industry will also guide counsel in refining the broad categories above for the particular offering being undertaken. For example, the information requested for a school district's general obligation financing secured by voter-approved property taxes in a developed community may focus on, among other things, information as to assessment or valuation appeals, general budget issues, school board politics, district operations, or pension obligations. In contrast, a financing secured solely by voter-approved taxes on a raw land development may focus on, among other things, the financial stability of the developer, development product mix, or economic health of the area.

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[54] *See generally* SEC Public Statement, The Importance of Disclosure for our Municipal Markets, May 4, 2020, https://www.sec.gov/news/public-statement/statement-clayton-olsen-2020-05-04 (last visited June 26, 2021)

[55] *See generally infra* text at notes 64 through 67 for a discussion of due diligence considerations related to compliance with prior continuing disclosure undertakings.

External information sources may supplement the standard diligence inquiry of an obligated person. Counsel should address the use of such third-party information at the outset of the diligence process to determine if the nature of the transaction warrants the additional costs associated with such reports. Depending on the nature of the transaction, another working group member (e.g., lender or credit enhancer) may be requiring this information so counsel can "piggy-back" off those requests and review the information provided.

Documents counsel may consider reviewing or requesting from the obligated person include, for example:

- Obligated person and other party meeting minutes
- Formal debt, investment, and disclosure policies
- Audited and/or unaudited financial statements
- Management letters and responses
- Attorney litigation letters
- Budgets
- Publicly available information on the obligated person's website or in news sources
- Public statements by officials of the obligated person
- Economic data (demographics, Bureau of Labor data, Census data)
- Litigation documents
- Retirement plans
- Industry background material
- Appraisals
- Market studies or feasibility reports
- Consultant reports[56]
- Governmental investigations
- Recent legislation and, in some cases, proposed legislation
- Rating agency reports
- Forecasts[57]
- Environmental reports, lien searches, and litigation searches[58]

New technologies also can assist in the due diligence process by automating certain time-consuming processes. For example, artificial intelligence software can assist in the due diligence process by reviewing, identifying, and analyzing documents to target issues relevant to

[56] Consultant reports used in connection with an offering (e.g., engineering and feasibility reports) may alleviate the need for first-hand diligence into the matters covered by the report, and a thoughtful review of such reports may reveal areas meriting further inquiry. For example, an engineering report for a utility system financing may include information about the condition of the system and compliance with regulatory requirements. If the report indicates the system has not complied with regulatory requirements, this information and the obligated person's response and remedial plan may need to be addressed in the offering document.

[57] Forecasts relating to ongoing operations can be checked against past performance and current year's budget. For example, one of the keys to the usefulness and reasonableness of any forecast is whether the first year in the forecast is consistent with current operations.

[58] In conduit offerings or project finance and real estate backed transactions, third-party lien searches, title reports, environmental reports, and litigation searches, may provide verification of certifications and disclosure provided by the obligated person and alert counsel and the underwriter to other potential risks.

underwriter's and disclosure counsel in drafting disclosure documents. AI software also can continuously scan third-party resources throughout the drafting process to ensure that current developments are addressed in disclosure documents. While AI processes are not a replacement for traditional due diligence questionnaires and calls, such processes may assist underwriters in meeting their due diligence obligations under the federal securities laws, as well as aid underwriters' counsel and disclosure counsel in fulfilling their respective obligations to their clients.

Developing a diligence request list that addresses the key representations in an offering document is a dynamic exercise combining many factors and requiring careful thought and frequent adjustment. To provide a framework for potential diligence requests, a matrix highlighting some of the considerations involved in different types of transactions is included herewith as Appendix A. The issues identified in the matrix are by no means exhaustive, and review of other materials will further assist with developing a comprehensive set of diligence requests.[59]

5.3 Persons to Whom the Due Diligence Questionnaire Should be Sent

After the diligence request list is developed and reviewed by the underwriter, the list then would be sent to the primary contact within the obligated person's organization with a copy to their legal counsel. A preliminary call may be held to walk through the request list and discuss the process for the return of the information. This call will also be an opportunity to discuss who will be responsible for coordinating the delivery of the information and who within the obligated person's organization will be preparing the responses, which may include the key subject-matter experts in the organization, senior officials who would have access to relevant information and overall strategy, and outside consultants (e.g., accountants, attorneys, and municipal advisors). The obligated person should confirm that all of the employees and officials who possess relevant material information are sufficiently involved in the process and that the officials involved have appropriate knowledge and authority.

5.4 Use of Formal Due Diligence Calls or Meetings

There are practical benefits to scheduling formal due diligence meetings for working group members to supplement due diligence. Such formal meetings emphasize the importance attached to the process and place key issues, problems, and concerns in sharper focus for the obligated person, allowing such concerns and problems to be discussed and providing a forum for reaching agreement on whether and how to dispose properly of any such matters.[60]

Additionally, confirming that key representatives of the obligated person have reviewed and affirmed the accuracy of the offering document by either holding a final call or receiving email sign-offs from these individuals just prior to printing and posting is a common practice in the municipal securities market. Scheduling such a call or receiving such sign-off emails as close as

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[59] *See, e.g.*, NATIONAL FEDERATION OF MUNICIPAL ANALYSTS, *White Papers and Best Practices,* https://www.nfma.org/disclosure-guidelines.

[60] *Disclosure Roles of Counsel*, *supra* note 1, at 154.

possible to the printing and posting date of the offering document is preferable in order to "bring-down" the diligence previously conducted to the offering document's publication date.

Due diligence calls and meetings, and the process generally, should include all members of the deal team and, in particular, any co-managers. Meaningful participation by co-managers assists senior managers in discharging their own responsibilities and can provide additional insight and information.[61]

5.5 Considerations for Review of Financial Information of Obligated Person

An important part of the due diligence process is the review of the obligated person's financial statements, regardless of the type of financing. Although evaluating the financial feasibility of an offering is outside the scope of counsel's review, a review of the financial statements provides both an opportunity to confirm that the financial information presented in the offering document is consistent with the obligated person's financial statements and an opportunity to identify possible issues that may require additional investigation and disclosure. Below are some examples for considerations when reviewing financial information:

- If the underwriter is requiring an agreed-upon-procedures letter, under which an accountant is engaged to "perform specific procedures on subject matter and report the findings without providing an opinion or conclusion,"[62] review this document to understand what information in the offering document is included in the procedures.

- Determine whether an auditor consent/inclusion letter will be obtained, by which the auditor agrees to the inclusion of the audited financial statements as an attachment to the offering document.[63]

- While reviewing past audited financial statements, associated management letters, and responses be alert for any red flags that suggest further investigation is necessary, including:

    - Trends in revenues or expenses;

    - Shifts in total net assets or any particular category of assets;

    - Shifts in total liabilities or incurrence of any new liabilities;

[61] *Id*. Keep in mind, too, that co-managers have independent due diligence obligations; hence, their participation in the due diligence process is not merely useful for the senior managers but also is important for them to aid their compliance with these obligations.

[62] Auditing Standards Board, "Statement on Standards for Attestation Engagements, No. 19" (Dec. 2019).

[63] *See* GOVERNMENT FINANCE OFFICERS ASSOCIATION OF THE UNITED STATES AND CANADA, *Offering Statements and the Independent Auditor's Role*, https://www.gfoa.org/materials/offering-statements-and-the-independent-auditors-role.

- Findings from the auditor that identify material weaknesses in the obligated person's accounting practices or policies;

- Notes to audited financial statements, particularly those relating to outstanding liabilities or implementation of new accounting and auditing standards; and

- An inquiry as to whether there are outstanding disputes with the auditor and the obligated person's practice for engaging new auditing firms, if appropriate.

5.6 Rating Agency Presentations and Calls

Counsel should seek to be invited to participate in the rating agency process because reviewing rating agency presentations and participating in rating agency calls may assist the underwriter and its counsel and disclosure counsel in the due diligence process. While the offering document need not contain all information provided to a rating agency in order to be complete, issues raised by rating agency requests or questions may elicit substantive responses from an obligated person that may warrant further discussion among the members of the working group and, perhaps, inclusion in the offering document. Rating agency presentations also frequently provide information about recent developments or new issues not previously included in the offering document. Accordingly, reviewing rating agency materials (including old and new rating agency reports) and listening in on rating agency calls may assist counsel in providing negative assurance that the offering document complies with the antifraud provisions of the federal securities laws.

5.7 Specific Considerations Regarding 15c2-12 Compliance Review

It is important to establish at the outset of an engagement who will be responsible for the five-year review of the obligated person's compliance with prior continuing disclosure undertakings. Underwriters typically either engage a third party to provide a report of prior compliance or conduct the compliance review internally. If a third party is engaged to provide a compliance report, counsel may be expected only to review the report and analyze errors or omissions for the purpose of determining whether such information should be disclosed in the final official statement as required by Rule 15c2-12. Further, the third-party report on historical compliance is only a starting point and counsel should consider testing the report itself by "spot-checking" filing information on the MSRB's EMMA website. Many underwriters have specific requirements with respect to the five-year compliance review and specific diligence questions to be asked of the obligated person. Counsel should confirm that all internal policies of the underwriter regarding such requirements and questions are followed.

If counsel is engaged to perform the five-year compliance review, the following provides a basic framework for such review:

- Utilize the MSRB's EMMA website to compile a list of the obligated person's securities that are subject to Rule 15c2-12 and have been outstanding at any point within the five years prior to the offering.
- Compile a list of CUSIP numbers for each outstanding security.

- Compile a list of the continuing disclosure requirements (e.g., annual/quarterly reports, audit, and event notices) for each continuing disclosure undertaking and the deadlines for filings.[64]
- Determine, to the extent possible, whether any events have taken place in the past five years (e.g., ratings changes and redemptions).
- Review all annual/quarterly filings made for the past five years and determine if they are timely, contain correct information, and are filed under the correct CUSIP identifiers on the MSRB's EMMA website.

In addition to examining whether audits, tables, or other types of financial information and operating data have been filed, it is necessary to determine whether the obligated person has made a timely filing of the required notice of certain events in accordance with Rule 15c2-12 occurring within the last five years. Neither the underwriter nor its counsel may be able to independently verify the occurrence of such events. As such, common practice is to explicitly ask the obligated person whether such events have taken place in a due diligence questionnaire or on a due diligence call. Such questions will need to be asked by counsel regardless of whether a third party is engaged to perform a compliance review. If a reportable event has occurred, counsel should confirm whether the obligated person filed notice of the event: (1) in a "timely manner" for continuing disclosure undertakings entered into before the 2010 amendments to Rule 15c2-12; or (2) in a "timely manner not in excess of 10 business days" after the event for continuing disclosure undertakings entered into after the 2010 amendments to Rule 15c2-12.[65]

For obligated persons who have entered into continuing disclosure undertakings since February 27, 2019,[66] additional inquiry and discussions with the obligated person may be warranted to determine whether it has incurred any material "financial obligations" or made any changes or amendments to material financial obligations. The notes to the financial statements could be reviewed to determine if any financial obligation (material or otherwise) has been incurred. Additionally, specific inquiry should be made about the compliance with these reporting requirements. For example, the diligence questionnaire could include the following inquiries:

- Who within the obligated person's organization is responsible for monitoring and reporting the occurrence of the new events?

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[64] Rule 15c2-12 specifically requires disclosure of only certain annual financial information. *See* 17 C.F.R. § 240.15c2-12(b)(5); *see also* Statement of the Commission Regarding Disclosure Obligations of Municipal Securities Issuers and Others, Exchange Act Release No. 42, 1994 WL 73628 at *5-6 (Mar. 9, 1994). However, it is common in certain types of revenue bond transactions (for example, health care revenue and land-secured infrastructure financings) to have quarterly disclosures related to operations or other material matters.

[65] *See* 2010 Adopting Release, *supra* note 25, at 33109; Proposed Amendment to Municipal Securities Disclosure, Exchange Act Release No. 60332, 2009 WL 2138447 (Jul. 17, 2009). The compliance date for the Rule 15c2-12 amendments in the 2010 Adopting Release was December 1, 2010. Prior to the 2010 amendments, Rule 15c2-12 specified that such notices were to be filed merely "in a timely manner." *Id.* at 33100. The 2010 amendments specified that such notices must be filed in a timely manner not in excess of ten business days after the event's occurrence. *Id.* at 33109.

[66] *See* Amendments to Municipal Securities Disclosure - Rule 15c2-12, Exchange Act Release No. 83885 (Aug. 20, 2018), 83 Fed. Reg. 44700, 44700 (Aug. 31, 2018).

- How will the obligated person determine materiality of an event (15)[67] or whether an event (16) "reflects financial difficulties"?

If failures in compliance are identified, counsel and the underwriter, as well as disclosure counsel, if applicable, should then work with the obligated person to determine the corrective action needed to address such failures and any necessary disclosure (e.g., posting failure-to-file notices and catch-up filings on EMMA).

5.8 Documenting the Conduct of Diligence

In 2012, the staff of the SEC published the OCIE Risk Alert concerning the level of due diligence and supervision carried out by underwriters in connection with offerings of municipal securities.[68] SEC examiners observed that some broker-dealers have not maintained, nor did they require the maintenance of, adequate written evidence that they complied with their obligations under Rule 15c2-12 and applicable SEC guidance regarding due diligence and supervision.[69] Some firms asserted that it is their specific policy not to maintain any due diligence records and stated that "it is not industry practice" or that they are following advice from outside counsel.[70] The staff of the SEC disagreed and provided a number of examples of effective practices that evidence due diligence and supervisory review, including the use of commitment committees, due diligence memoranda, outlines for due diligence calls, and recordkeeping checklists.[71] Additionally, the FINRA Notice, states "… a broker-dealer should retain records documenting both the process and results of its investigation.[72] Such records may include descriptions of the meetings that were conducted in the course of the investigation…the tasks performed, the documents and other information reviewed, the results of such reviews, the date such events occurred, and the individuals who attended the meetings or conducted the reviews."[73]

Depending on an underwriter's written policies and procedures, underwriter's counsel may be asked to assist with the retention of written documentation of the conduct of due diligence, or may be asked to provide such documentation in the case of a regulatory exam. The extent of counsel's participation in documenting the due diligence process should be addressed in counsel's engagement letter or otherwise as early in the transaction as possible.

There is a wide divergence among counsel about creating and/or retaining documentary evidence of the conduct of due diligence on behalf of an underwriter (such as a formal due diligence memorandum), some of which is dictated by internal law firm policy, as well as the

[67] The materiality requirement is satisfied when there is "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." Matrixx Initiatives, Inc. v. Siracusano, 131 S. Ct. 1309, 1318 (2011) (quoting Basic Inc. v. Levinson, 485 U.S. 224, 2331-32 (1988)).

[68] *See* SEC Office of Compliance Inspections and Examinations, *supra* note 26.

[69] *Id*.

[70] *Id*.

[71] *Id*.

[72] *See* FINRA Rule 2111.

[73] *Id*.

relationship with the particular underwriter making such request. For some law firms, a formal due diligence memorandum may not be cost effective to prepare and bears the risk of being incomplete or omitting a material fact. However, drafting such memorandum may have advantages, including demonstrating that care was taken in providing the services requested and providing a written record if an attorney on the deal departs. Other law firms may forego the cost of preparation of a formal due diligence memorandum in favor of the due diligence questionnaire, document request list, notes, and relevant emails. If any notes or emails have a claim to be attorney-client privileged, they could be segregated and retained separately, and, if forwarded, counsel should be mindful in preserving the attorney-client privilege.

Another approach is to discard all notes and papers, but keep careful records of the time spent on due diligence inquiries, the date and circumstances under which due diligence was conducted, who was present, and the general subject of the investigation.[74] The retention of contemporaneous notes should be fairly scrutinized if retained, as notes are ambiguous and incomplete shorthand expressions can easily be taken out of context or misinterpreted. Both underwriters and their counsel may want to take a few minutes at closing to verify that their respective due diligence files can be neither misconstrued nor considered incomplete. As a general rule, files would be stored for the statute of limitations period for an antifraud action, that is, five (5) years. Underwriters are subject to their own special document retention requirements under SEC and MSRB rules.

[74] FIPPINGER, *supra* note 21, § 7.5.7.

Appendix A

Diligence Questionnaire Matrix[75]

Type of Deal	Common Security Source	Potential Items of Concern/Risk	Potential Sources of Information
General Obligation	• Limited/unlimited tax based on obligated person authority	• Growth of tax base • Reassessments of major landowners • Environmental issues (hurricanes, flood, fire, earthquake, etc.) • Pension issues	• Historical property assessment values • Population and demographic trends (population growth, unemployment, median income, school enrollment, etc.) • Bankruptcy filings for key industries • Tax collections and delinquency rates • EMMA • Audits, budgets, budget vs actual • Interim financials • Actuarial reports • Reports provided to other governmental entities • Audits or inquiries conducted by other governmental entities • Internet search/local news search
Utility Revenue	• Revenues generated by obligated person utilities	• Use of/demand for utilities • Rates charged • Environmental issues affecting demand (for example, drought) • Water supply contracts and arrangements	• Audits, budgets, budget vs actual • Interim financials • EMMA • Actuarial reports • Reports provided to other governmental entities • Audits or inquiries conducted by other governmental entities • Internet search/local news search
Toll Revenue	• Revenues generated by tolls collected	• Potential use of toll facilities	• Feasibility studies • EMMA • Audits, budgets, budget vs actual

[75] Note: This Appendix A highlights some of the considerations involved in different types of transactions to assist with a framework for potential diligence requests. The issues identified in this matrix are by no means exhaustive, and review of other materials will further assist with developing a comprehensive set of diligence requests; for example, review of other materials may be necessary in transactions involving non-essential governmental projects, transactions involving annual-appropriation risks, and transactions involving revenue bonds issued on behalf of nonprofit organizations. Further, due diligence issues evolve over time; for example, cybersecurity, climate change, and pandemics have arisen in recent years as issues meriting due diligence consideration.

Type of Deal	Common Security Source	Potential Items of Concern/Risk	Potential Sources of Information
		• Cost of toll • Necessity of facility to potential users	• Interim financials • Actuarial reports • Reports provided to other governmental entities • Internet search/local news search
Airport Revenue	• Gate contract revenues, taxes, etc.	• Airlines involved • Daily flights • Airport traffic generally • Impact of federal regulations	• Audits, budgets, budget vs actual • Interim financials • EMMA • Actuarial reports • Reports provided to other governmental entities • Airline financial statements • Reports of regulatory agencies (for example, FAA) • Internet search/local news search

Charter School	• School revenues	• Number of students
		• Cost of attendance
		• Student retention
		• Impact of changes to state aid/state reimbursement amounts and formulas
		• Charter authorizations and renewals
			• Audits, budgets, budget vs actual
			• Interim financials
			• EMMA
			• Reports provided to other governmental entities
			• School diligence requests such as:
			  • Charter school agreement
			  • Approval letters of state
			  • Charter school application
			  • Copies of annual reports submitted to authorizer
			  • Material correspondence with authorizer
			  • Enrollment
			  • Waiting list
			  • Demographics in area
			  • Competition materials
			  • Credentials of management/teaching staff
			  • Test results or reports, ranking data
			• Internet search/local news search

Stadium	• Special taxes or other revenues generated by or around a sports facility	• Teams involved • Uses of stadium • Fees charged • Annual attendance	• Audits, budgets, budget vs actual • Interim financials • EMMA • Reports provided to other governmental entities • Audits or inquiries conducted by other governmental entities

Type of Deal	Common Security Source	Potential Items of Concern/Risk	Potential Sources of Information
			• Contracting entities (sports team, etc.) • Internet search/local news search
Health Care/Hospital	• Hospital revenues • Taxes • Mortgage or additional security	• Patient mix • Procedure mix • Insured vs. uninsured population • Location of facility • Levels of care served • Federal reimbursement formula changes	• Audits, budgets, budget vs actual • Interim financials • EMMA • Actuarial reports • Reports provided to other governmental entities • Audits or inquiries conducted by other governmental entities • Reports of regulatory agencies (for example, CMS, etc.) • System diligence requests • Internet search/local news search

Retirement Community	• Facility revenues
	• Mortgage/real property security
	• Initial entrance fees
		• Resident mix
		• Revenues charged (rates by unit/service type)
		• Retention
		• Occupancy
		• Project plans, feasibility
			• Audits, budgets, budget vs actual
			• Interim financials
			• EMMA
			• Actuarial reports
			• Reports provided to other governmental entities
			• Audits or inquiries conducted by other governmental entities
			• Reports of regulatory agencies (for example, CMS, etc.)
			• System diligence requests
			  • Approval letters of state/authorization to operate
			  • Copies of annual reports submitted to authorizer
			  • Waiting list
			  • Demographics in area
			  • Competition materials
			  • Credentials of management/teaching staff
			• Internet search/local news search

Sales Tax	• Taxes generated by various sales in obligated person jurisdiction	• Type of sales tax (rate, sales covered) • Exemptions from charge • Jurisdiction charging	• Historical collections • Population and demographic trends (population growth, unemployment, median income, etc.) • EMMA • Audits, budgets, budget vs actual • Interim financials

Type of Deal	Common Security Source	Potential Items of Concern/Risk	Potential Sources of Information
		• Change in economic activity	• Actuarial reports • Reports provided to other governmental entities • Audits or inquiries conducted by other governmental entities • Internet search/local news search
Hotel/Convention Center Tax	• Special tax based on obligated person authority generated by and for a specific purpose (tourism, etc.)	• Hotel occupancy rates • Tax collections • Attractiveness of destination/facility	• Feasibility studies • Chamber of commerce/tourism bureau/trade organizations • EMMA (if prior securities issued) • Audits, budgets, budget vs actual • Interim financials • Actuarial reports • Reports provided to other governmental entities • Audits or inquiries conducted by other governmental entities • Internet search/local news search

Special Assessment/Development	• Special assessments (not tax) on undeveloped land	• Experience of developer
		• Location of development
		• Capital stack
		• Demand for product developed
			• Chamber of Commerce/tourism bureau/trade organizations
			• EMMA (if prior securities issued)
			• Audits (if available)
			• Appraisals
			• Feasibility Studies
			• Engineering Reports
			• Market Studies
			• Reports provided to other governmental entities
			• Audits or inquiries conducted by other governmental entities
			• Internet search/local news search
			• Site tours
			• Developer diligence requests
			  ◦ Prior experience
			  ◦ Financial capability to complete project
			  ◦ Competition information

Higher Education	• Tuition and student fees • Tax revenues or appropriated revenues, if applicable	• Enrollment • Tuition/fee rates • Housing/residence life occupancy	• Audits, budgets, budget vs actual • Interim financials • EMMA • Reports provided to other governmental entities

Type of Deal	Common Security Source	Potential Items of Concern/Risk	Potential Sources of Information

		• State appropriations (if governmental)
		• Endowment/investment returns
		• Accreditation status
			• School diligence requests such as:
			  • Copies of annual reports
			  • Enrollment
			  • Waiting list
			  • Test results or reports, ranking data

Appendix B

Bibliography—Primary Sources

1. Basic Inc. v. Levinson, 485 U.S. 224 (1988).

Basic, Inc. (Basic) made three public statements denying that merger conversations were taking place. Former Basic shareholders who sold their stock after Basic's first denial sued Basic and a director for making false and misleading statements in violation of Rule 10b-5. The Sixth Circuit reversed the trial court's grant of summary judgment for Basic, which was based on the fact that the statements were immaterial. The Supreme Court found that there was no reason to exclude the statements from the definition of materiality. The Court explained that the materiality of a fact depends on its significance to the reasonable investor, and it is impractical to require individuals to show a specific reliance on misleading information. The Court held that it is reasonable for courts to use a presumption of reliance, but the presumption may be rebutted.

2. Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976).

Customers of the brokerage firm who invested in a fraudulent securities scheme perpetrated by the president of the firm sued for violation of Section 10(b) of the Exchange Act and Rule 10b-5. The complaint was based on a theory of negligent nonfeasance. The Supreme Court held that pleading mere negligence was insufficient and inferred intent to be a necessary component of pleading fraud. However, the Court proposed, but did not rule, that recklessness might fulfill the scienter requirement of Section 10(b) of the Exchange Act and Rule 10b-5.

3. Escott v. Barchris Construction Corporation, 283 F. Supp. 643 (S.D.N.Y. 1968).

Class action by buyers of debentures against bowling alley construction company which issued the debentures, underwriters, and certain other parties for damages sustained as a result of misstatements and omissions in a prospectus contained in a registration statement. The court held, among other things, that the prospectus contained misstatements and omissions and that the defendants failed to sustain their burden of proving the due diligence defenses asserted.

4. Financial Industry Regulatory Authority, *Regulation D Offerings: Obligation of Broker-Dealers to Conduct Reasonable Investigations in Regulation D Offerings*, Regulatory Notice 10-22 (April 2010), https://www.finra.org/rules-guidance/notices/10-22.

FINRA released guidance in 2010 regarding broker-dealers' obligations to conduct a reasonable investigation of the issuer and the securities they recommend in private placements. FINRA discusses in this release the minimum required investigation procedures required in such offerings and specific factors that may heighten the due diligence obligations of broker-dealers (including affiliation with the issuer, preparation of a private placement memorandum, and red flags in available information).

5. *In re* Dolphin & Bradbury Inc. v. SEC, 512 E3d 634 (D.C. Cir. 2008).

The underwriter for a municipal bond offering and its principal petitioned for judicial review of an order in which the SEC held them liable for violation of Section 10(b) of the Exchange Act and Rule 10b-5. The court of appeals found that substantial evidence supported the SEC's conclusions that (1) cautionary statements made by the underwriter and principal were so deficient that the underwriter and principal must have known that investors would be misled by the offering documents and (2) the underwriter and principal could not negate scienter by their reliance upon counsel, bond counsel, and municipal advisor.

6. Matrixx Initiatives, Inc. v. Siracusano, 131 S. Ct. 1309 (2011).

Investors in Matrixx Initiatives, Inc. (Matrixx) alleged that Matrixx violated Section 10(b) of the Exchange Act and Rule 10b-5 by failing to disclose reports of a possible link between its leading product and anosmia. Matrixx moved to dismiss because the investors had not pleaded materiality or scienter because they did not allege that the reports reflected statistically significant evidence that the product caused anosmia. The Supreme Court determined that an allegation of statistical significance is not required to establish materiality or scienter.

7. S.C. Nat'l Bank v. Stone, 139 F.R.D. 335 (D.S.C. 1991).

The purchasers of municipal bonds issued to finance construction and operation of a retirement center brought a securities fraud action against various defendants. The court explained that, more than any other party to a bond issue, the underwriter has the responsibility to conduct due diligence to investigate and disclose the material facts about the bond issue. The court further explained that the underwriter cannot delegate that responsibility to another party, including its counsel.

8. SEC, Credit Suisse First Boston Corporation, Securities Act Release 33-7498, 1998 WL 30378 (Jan. 29, 1998).

In interpreting the obligations of Credit Suisse First Boston Corporation (First Boston) as underwriter in connection with a bond offering by Orange County, California, the SEC determined that it failed to meet its obligations under the Securities Act and MSRB Rule G-17. The official statement included false and misleading information about the County's investment pools, which was received directly from the County. The SEC determined that First Boston failed to adequately investigate the information, which it should have known was materially misleading.

9. SEC, Piper Jaffray & Co., Securities Act Release No. 9472 (November 5, 2013) (cease and desist order).

The SEC concluded that Piper Jaffray & Co., the underwriter, and Jane Towery, Piper's managing director and the lead investment banker, had violated the Securities Act because they had "conducted inadequate due diligence and, as a result, failed to form a reasonable basis for believing the truthfulness and completeness of material statements" made in an official statement. Piper was a successor underwriter to the underwriter who had completed the preliminary official statement. The SEC determined that Piper and Towery failed to inquire about certain projections provided by an interested third-party and ignored certain reports by independent consultants in drafting the final official statement.

10. SEC, *In re* Richmond Corp., 41 S.E.C. 398 (1963).

The SEC issued a stop order, which suspended the effectiveness of a registration statement that was materially false and misleading. Although the underwriter for the proposed offering was not a party to the proceeding, the SEC emphasized that the underwriter's investigation was inadequate. This order transformed the statutory standard of "reasonable investigation" into an affirmative duty of an underwriter to exercise due diligence in ensuring a registration statement is accurate and adequate.

11. SEC, Donaldson, Lufkin & Jenrette Securities Corporation, Securities Act Release No. 6959, 1992 WL 280784 (Sep. 22, 1992) (administrative proceeding).

The SEC determined that DLJ, an underwriter of stock of Matthews & Wright (M&W), a municipal bond broker-dealer, failed to investigate information that M&W may have engaged in questionable municipal bond "closings" to evade pending changes in the tax law. The SEC noted that "simple inquiry … would have revealed the unusual and questionable nature of the transactions." According to the SEC, just a review of the closing documents would have led DLJ to discovery of the fraudulent nature of the closings.

12. SEC, Interpretive Guidance with Respect to Obligations of Participating Underwriters, Exchange Act Release No. 62184A (May 26, 2010), 75 Fed. Reg. 331003 (June 10, 2010).

This release finalized the SEC's amendment to Rule 15c2-12 to apply continuing disclosure requirements to demand securities. The interpretative guidance contained in the release reaffirmed the SEC's prior interpretations of due diligence standards and described the relationship of those standards to demand securities.

13. SEC, Obligations of Underwriters, Brokers and Dealers in Distributing and Trading Securities, Exchange Act Release No. 9671 (July 26, 1972).

In response to an investigation into trends in securities markets, the SEC issued this release to address the obligations of underwriters, brokers, and dealers in primary offerings. In addition to describing a proposed program for increased disclosure, the Release scrutinized the due diligence undertakings of underwriters in relation to their unique position as the intermediary between the public and issuer. The SEC acknowledged the potential difference in standards of managing and other participating underwriters. Additionally, the SEC described the importance of due diligence meetings between underwriters and issuers prior to circulating offering documents.

14. SEC, Proposed Amendment to Municipal Securities Disclosure, Exchange Act Release No. 60332, 2009 WL 2138447 (Jul. 17, 2009).

The SEC announced in this release proposed rules to require broker-dealers involved in an offering of municipal securities to reasonably determine that the issuer or obligated person has agreed to provide notice of the events listed in Rule 15c2-12 within ten business days after occurrence and amend the list of notice events, including modification of events that are subject to a materiality determination.

15. SEC, Proposed Amendments to Municipal Securities Disclosure – Rule 15c2-12, Exchange Act Release No. 26100 (Sept. 22, 1988), 53 Fed. Reg. 37778 (Sep. 28, 1988).

In 1988, the SEC released its proposed Rule 15c2-12. In the proposing release, the SEC described the interplay of Rule 15c2-12 and the antifraud provisions of the federal securities laws and the effect on the disclosure obligations of the various parties involved in a municipal securities offering. In particular, the 1988 Proposing Release contains interpretive guidance for primary offering participants in meeting their disclosure and due diligence obligations under these rules.

16. SEC, *Disclosure and Accounting Practices in the Municipal Securities Market White Paper to Congress* (July 26, 2007), https://www.sec.gov/news/press/2007/2007-148wp.pdf.

In 2007, the SEC released this white paper to highlight disclosure and accounting problems it observed in the municipal securities market and provided an overview of the municipal securities market, an overview of the availability of information in the municipal securities market, an overview of accounting standards in the municipal securities market, an overview of disclosure policies and procedures in the municipal securities market, and an overview of transaction professionals in the municipal securities market.

17. SEC, *Report on the Municipal Securities Market* (July 31, 2012), https://www.sec.gov/news/studies/2012/munireport073112.pdf.

In 2012, the SEC's Office of Municipal Securities released this report, which provided an overview of the municipal securities market, an overview of disclosure practices in the municipal securities market, an overview of the municipal securities market structure, recommendations for improvements to disclosure practices in the municipal securities market, and recommendations for improvements to municipal securities market structure.

18. SEC, Office of Compliance Inspections and Examinations, *Strengthening Practices for the Underwriting of Municipal Securities*, National Examination Risk Alert, Mar. 19, 2012, https://www.sec.gov/about/offices/ocie/riskalert-muniduediligence.pdf.

This report was released by the SEC to clarify underwriters' and broker-dealers' obligations to assess the likelihood of an issuer or obligor complying with the Rule 15c2-12's continuing disclosure requirements prior to underwriting an offering. The SEC notes that such obligations require inquiry into relevant facts and prior undertakings.

19. SEC, *Report under Section 21(a) of the Exchange Act; Attorney's Conduct in Issuing an Opinion Letter Without Conducting An Inquiry Of Underlying Facts Failed to Comport With Applicable Standards of Conduct*, Exchange Act Release No. 17831 (June 1, 1981), https://www.sec.gov/info/municipal/mbonds/bc.htm.

This report was prompted by the SEC's investigation into a Tennessee attorney's failure to object to the omission from the offering document of any financial information about the adverse past operations of the obligor hospital when he was acting as underwriter's counsel in a municipal bond offering. Instead of bringing an enforcement action, the SEC issued this report, detailing an

attorney's ethical obligation to reasonably investigate relevant facts in connection with issuing a legal opinion in connection with a bond offering.

20. SEC v. Dain Rauscher, Inc., 254 F.3d 852 (9th Cir. 2001).

The SEC alleged that, by failing to conduct a proper investigation and by omitting material information from offering statements, the underwriter violated, among other things, Section 10(b) of the Exchange Act and Rule 10b-5. The district court held that because the underwriter's conduct satisfied the industry standard, he was entitled to summary judgment. The SEC appealed. The Ninth Circuit held that the "reasonable prudence" standard is the appropriate standard for evaluating an underwriter's conduct, and the industry standard is only one factor to consider in applying the reasonable prudence standard.

21. SEC, Statement of the Commission Regarding Disclosure Obligations of Municipal Securities Issuers and Others, Exchange Act Release No. 42, 1994 WL 73628 (Mar. 9, 1994).

In this Release, the SEC addressed the need for improved disclosure of certain financial relationships, risks involved with the securities, financial position of the issuer or obligor(s), and plans for secondary market disclosures.

Appendix C

Bibliography—Secondary Sources

1. AMERICAN BAR ASSOCIATION COMMITTEE ON ETHICS AND PROFESSIONAL RESPONSIBILITY, Formal Opinion 335 (1974).

The ABA's Formal Opinion 335 established the ethical guidelines a lawyer should follow when furnishing an assumed-facts opinion in connection with the sale of unregistered securities. The ABA emphasizes the duties of counsel to scrutinize and investigate facts not within the lawyer's personal knowledge. Though the opinion is aimed at guiding due diligence in connection with giving formal opinions, the principles of reasonable investigation can be applied in other circumstances.

2. AMERICAN BAR ASSOCIATION, SUBCOMMITTEE ON SECURITIES LAW OPINIONS, COMMITTEE ON FEDERAL REGULATION OF SECURITIES, SECTION OF BUSINESS LAW, *Negative Assurance in Securities Offerings (2008 Revision)*, 64 Bus. Lawyer 395 (2008).

The ABA published this model letter to assist ABA members in rendering negative assurance letters in connection with registered and unregistered securities offerings.

3. AMERICAN BAR ASSOCIATION and NATIONAL ASSOCIATION OF BOND LAWYERS, *Disclosure Roles of Counsel In State and Local Government Securities Offerings* (3d ed. 2009).

Disclosure Roles of Counsel is a comprehensive guide to the disclosure obligations of parties to municipal securities offerings. The book examines the disclosure obligations and antifraud provisions of the Securities Act and the Exchange Act. In addition, the book details the roles of bond counsel, underwriters' counsel, and other representatives of financing participants in crafting offering documents.

4. AUDITING STANDARDS BOARD, *Statement on Standards for Attestation Engagements No. 19* (Dec. 2019).

The ASB's SSAR No. 19 was issued to provide performance and reporting requirements and relevant guidance for auditors engaged to provide agreed-upon procedures in connection with securities offerings. The SSAE provides detailed requirements and considerations to assist auditors in performing agreed-upon procedures engagements, including specific documents and supporting materials that should be obtained to substantiate an issuer's unaudited financial statements.

5. *Barchris: Due Diligence Refined*, 68 Colum. L. Rev. 1411 (1969).

This student comment explicates the "due diligence" defense in the context of Escott v. Barchris Construction Corporation, 283 F. Supp. 643 (S.D.N.Y. 1968).

6. Collection of White Papers Regarding Best Practices in Disclosure, NATIONAL FEDERATION OF MUNICIPAL ADVISORS, https://www.nfma.org/best-practices-in-disclosure (last visited Mar. 1, 2021).

The National Federation of Municipal Analysts has published many white papers describing disclosure factors in different financing situations. Each white paper covers specific transaction types, including state and local government debt, housing revenue debt, land-secured debt, hospital debt, water and sewer debt, and more. The NFMA's white paper resource page also contains a number of "best practices" publications that can assist municipal securities financing participants in preparing offering documents.

7. ROBERT W. DOTY, *Application of the Antifraud Provisions of the Federal Securities Laws to Exempt Offerings: Duties of Underwriters and Counsel*, 16 *B.C. L. Rev.* 393 (1975).

This article covers a number of disclosure-related topics, and, in particular, contains a detailed description of the due diligence standards required under the Securities Act and Exchange Act. The article also describes how those investigatory procedures assist financing participants with drafting informative offering documents in both exempt and non-exempt financings. The article contains a description of several enforcement actions related to adequate disclosure.

8. GOVERNMENT FINANCE OFFICERS ASSOCIATION OF THE UNITED STATES AND CANADA, *Offering Statements and the Independent Auditor's Role*, https://www.gfoa.org/materials/offering-statements-and-the-independent-auditors-role.

This GFOA advisory advises governments to use their audited financial statements as appropriate, not to permit auditors to create artificial "involvement" with offerings of municipal securities, to take steps to avoid unwarranted delays and costs, and to clarify publishing permission within their audit contracts.

9. John McNally, *Due Diligence In the Context of Municipal Securities Underwriting*, QUARTERLY NEWSLETTER (NABL), March 1, 1997.

This article contains a discussion of various issues in due diligence. The article describes the various due diligence aspects of the antifraud provisions, Rule 15c2-12, and MSRB rules. The article contains a discussion of analogous corporate securities due diligence obligations and the burden of proof for the due diligence defense in municipal securities enforcement actions.

10. MUNICIPAL SECURITIES RULEMAKING BOARD, Glossary of Municipal Securities Terms, http://www.msrb.org/Glossary/Definition/DUE-DILIGENCE.aspx (last visited Feb. 22, 2021).

The MSRB maintains a glossary of terms related to the municipal securities industry, with definitions that reflect the common meanings of such terms in the municipal market.

11. NATIONAL ASSOCIATION OF BOND LAWYERS, *Federal Securities Laws of Municipal Bonds Deskbook* (7th Ed. 2017).

The NABL Federal Securities Laws of Municipal Bonds Deskbook is an essential guide for bond lawyers and other professionals engaged in the municipal securities market. The book contains key sections of the Securities Act, Exchange Act, and the Investment Company Act of 1940, as well as select SEC cease-and-desist orders, interpretive and no-action letters, and summaries of important SEC enforcement actions and reports. Chapter 11 of the book, titled "Disclosure Resources for Primary Offerings and Continuing Disclosure", contains relevant resources to assist municipal securities participants in meeting their various disclosure obligations.

12. NATIONAL ASSOCIATION OF BOND LAWYERS, *Model Letter of Disclosure Counsel* (2018).

NABL published this Model Letter of Disclosure Counsel to assist NABL members in their role as disclosure counsel in municipal securities offerings.

13. NATIONAL ASSOCIATION OF BOND LAWYERS, *Model Letter of Underwriters' Counsel* (2d Ed. 2017).

NABL published this Model Letter of Underwriters' Counsel to assist NABL members in their representation of underwriters of municipal securities.

14. NATIONAL ASSOCIATION OF BOND LAWYERS, *NABL Analysis of SIFMA Model Memorandum to Underwriter's Counsel* (Mar. 2019).

In response to the SIFMA Model Memorandum to Underwriter's Counsel, NABL drafted a companion article that annotates SIFMA's model with additional guidance for NABL members to consider in certain transactions.

15. ROBERT A. FIPPINGER, PRACTICING LAW INSTITUTE, *The Securities Laws of Public Finance* (3d ed. 2011).

This treatise covers nearly all aspects of municipal securities offerings. In particular, Chapter 7 discusses a range of disclosure issues that arise with drafting the various offering documents, with a focus on practical explanation of various parties' disclosure obligations in relation to the Securities Act and Exchange Act.

16. ROBERT D. POPE, GOVERNMENT FINANCE OFFICERS ASSOCIATION, *Making Good Disclosure: The Role and Responsivities of State and Local Officials Under the Federal Securities Laws* (2001).

This book contains discussion of disclosure obligations throughout the life of a municipal securities transaction. From offering documents to continuing disclosure, this book describes, among other topics, the standards for determining what should be disclosed by an issuer at each disclosure stage, disclosure issues in private placements, and various enforcement actions.

17. SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION, *SIFMA Model Memorandum to Underwriter's Counsel for New Issues of Municipal Securities* (Sept. 2018).

In 2018, SIFMA released its Model Memorandum to Underwriter's Counsel for New Issues of Municipal Securities to assist underwriter's counsel in connection with municipal securities financings. SIFMA has additional resources for municipal securities financing participants on their Municipal Securities Resources website (https://www.sifma.org/resources/general/municipal-securities-markets/).

Appendix D

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