National Association
of Bond Lawyers

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September 2, 2011

Commissioner Elisse B. Walter
U.S. Securities and Exchange Commission
100 F St NE Room 10200
Washington, DC 20549

Re: Additional NABL Comments for Interpretive Guidance Update

Dear Commissioner Walter:

NABL commends you for your ongoing interest in reviewing and updating the 1994 Interpretive Guidance. On May 14, 2010, in response to your request, NABL submitted suggestions for areas that we believed could benefit from clarification and guidance regarding the application of the federal securities laws to municipal finance. The additional comments below reflect further deliberations regarding issues that have come to light since NABL's May 14 submission that we believe warrant consideration for inclusion in the updated 1994 Interpretive Release and that would benefit the municipal market.

The submission was prepared by the individuals listed on Appendix B and was approved by the NABL Board of Directors.

NABL is an organization of approximately 2,800 public finance attorneys that exists to promote the integrity of the municipal market by advancing the understanding of and compliance with the law affecting public finance.

We thank you for this opportunity. If NABL can provide further assistance, please do not hesitate to contact me or Penny Rostow in our Washington Office.

Sincerely,

John M. McNally
President, National Association of Bond Lawyers

ADDITIONAL STATEMENT
OF THE
NATIONAL ASSOCIATION OF BOND LAWYERS
TO
UNITED STATES SECURITIES AND EXCHANGE COMMISSION
REGARDING
MUNICIPAL SECURITIES DISCLOSURE

In response to an invitation by Commissioner Elisse B. Walter, on May 14, 2010, the National Association of Bond Lawyers ("NABL") submitted a statement (the "2010 NABL Statement") to the United States Securities and Exchange Commission (the "SEC" or the "Commission") relating to the SEC's anticipated update to SEC Release No. 33-7049 (the "1994 Interpretive Release"), which addressed municipal securities disclosure. The 2010 NABL Statement identified issues NABL believed could benefit from SEC clarification and suggested guidance regarding these issues.

Subsequent to submission of the 2010 NABL Statement, NABL has identified additional issues that NABL believes could benefit from SEC clarification. Those issues (along with suggested guidance regarding those issues that NABL believes would be helpful and appropriate) are set forth in this additional statement (the "2011 NABL Statement") in a question-and-answer format. For the SEC's convenience, a copy of the 2010 NABL Statement is included as Appendix A.

As mentioned in the 2010 NABL Statement, NABL also will continue to work with municipal securities market participants to improve disclosure practices. We note, for example, that NABL currently is leading an initiative to improve pension disclosure practices. We will look for other opportunities like the pension project.

This 2011 NABL Statement was prepared by an *ad hoc* subcommittee of the NABL Securities Law and Disclosure Committee comprised of those individuals listed on Appendix B and was approved by the NABL Board of Directors.

Q1. How can the SEC facilitate improved secondary market disclosure by providing guidance to issuers and other obligated persons as to how, with appropriate disclaimers, they can be assured that they would not be subject to an SEC enforcement action for releasing monthly budgetary data and other unaudited data that later proves to be inaccurate (absent recklessness or intentional deceit)?

In order to promote the dissemination of interim financial and other information by issuers and obligated persons without the fear of SEC enforcement should such information subsequently be shown to be inaccurate, NABL suggests that the recommendations it made in the 2010 NABL Statement with respect to the responsibilities of issuers, members of issuers' governing bodies, and issuers' staff for primary offering disclosure should be extended to secondary market disclosure of interim financial and other information.[1] Additionally, NABL suggests that the Commission recognize that there is a distinction between information that is made publicly available in the normal course of government operations and information that is made publicly available pursuant to contractual obligations contained in continuing disclosure undertakings. Finally, NABL requests that the Commission provide guidance as to how issuers and obligated persons, through the use of appropriate disclaimers, can reasonably limit liability under the antifraud provisions for secondary market disclosure of interim financial and other information.

Clarification of Standard of Care for Primary Disclosure/Extension to Secondary Disclosure. In the 2010 NABL Statement, NABL suggested that the Commission clarify that, for purposes of assessing the responsibilities of members of an issuer's governing body under the federal securities laws, a member who responsibly and reasonably authorizes staff to prepare and approve an offering document (and has no actual knowledge of "red flags") would not be liable for a violation of Section 10(b) of the Exchange Act, although the issuer itself (through the actions of its staff) might be liable for such a violation.[2]

In part, this suggestion reflected NABL members' experience that there sometimes can be significant differences between the knowledge levels of an elected member and a staff member or official with respect to the finances of an issuer. Elected members often have no choice but to rely on financial information provided by staff, provided that, as the Commission established in the Orange County Report with respect to offering materials,

- A public official may not *approve* disclosure that the official knows to be false.

[1] In the 2010 NABL Statement, NABL addressed, in three separate questions, (1) the responsibilities of an issuer and its governing body in approving or authorizing primary offering and secondary market disclosure, (2) what measures issuers should employ to prevent disclosed financial data in official statements from being materially misleading due to volatility or seasonality of data, and (3) the appropriate uses and limitations of disclaimers in official statements.

[2] *See* 2010 NABL Statement, at FN 4.

- A public official may not *authorize* disclosure while recklessly disregarding facts that indicate that there is a risk that the disclosure may be misleading.[3]

NABL suggested in the 2010 NABL Statement that the Commission clarify that "adopting and then adhering to a reasonable disclosure process[4] would satisfy a governing body member's responsibility, absent knowledge of a material misstatement or omission, when taking action to adopt or approve an offering document," and that the standard of care for individual members of a governing body with respect to primary disclosure be expanded to cover secondary disclosure, such that they would only be liable for "secondary market disclosures that they approve with knowledge of, or reckless disregard for, a material misstatement or omission."[5] NABL now suggests that the Commission provide guidance and clarify that an issuer or obligated person that adopts and adheres to a reasonable secondary market disclosure process (which, similar to a reasonable primary disclosure process, would need to be reasonably designed to produce accurate and reliable information) and that authorizes staff to release, for example, monthly budgetary data and other unaudited data would be considered "reasonable," even *without* further review or approval by the elected officials.

Publicly Available Information. At the time that SEC Rule 15c2-12 was amended in 1994, most issuers did not have access to the Internet. Procedures that are now considered routine, such as the posting of agendas for meetings of governing bodies on their websites, may have been contemplated, but were not commonplace in 1994. In some instances, and in order to reduce the costs of copying voluminous documents, the background materials for "action" items to be considered by the governing body of an issuer are included in these postings and can be downloaded by any interested member of the public.

In the Executive Summary to the 1994 Interpretive Release, the Commission points out that,

> (3) Particularly because of their public nature, issuers in the municipal market routinely make public statements and issue reports that can affect the market for their securities; without a mechanism for providing ongoing disclosures to investors, these disclosures may cause the issuer to violate the antifraud provisions.

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[3] Securities and Exchange Commission, Report on Investigation in the Matter of County of Orange, Cal., SEC Rel. No. 34-36761 (Jan. 24, 1996) (the "Orange County Report").

[4] As stated in the 2010 NABL Statement, *Disclosure Roles of Counsel*, 3rd ed., at 80-81, suggests that public officials and their counsel consider the following questions in establishing a basis for reasonable reliance: (1) Have we adopted disclosure processes for preparing Official Statements, and if we have, am I satisfied that such processes have been reasonably designed to produce accurate and reliable information? (2) Do I have a reasonable basis to have confidence in the integrity and competence of the financing team (e.g., financial staff, in-house counsel, outside counsel) that has prepared the Official Statement? (3) Do I know anything that would cause me to question the accuracy of the disclosures or that would indicate that they are misleading? (4) Do I know of any potentially material issues that should be brought to the attention of the financing team or for which I would like further explanation?

[5] *See* 2010 NABL Statement, at FN 9.

> Basic mechanisms to address potential antifraud liability include:
>
> - publication of financial information, including audited financial statements and other financial and operating information, on at least an annual basis;
>
> - timely reporting of material events reflecting upon the creditworthiness of the issuer of the obligor and the terms of its securities, including material defaults, draws on reserves, adverse rating changes and receipt of an adverse tax opinion; and
>
> - submission of such information to an information repository.[6]

But in the 1994 Interpretive Release, the Commission also underscored the difficulty facing issuers by not limiting antifraud liability to that information submitted to an "information repository" by stating that, "A municipal issuer may not be subject to the mandated continuous reporting requirements of the Exchange Act, but when it releases information to the public that is reasonably expected to reach investors and the trading markets, those disclosures are subject to the antifraud provisions."[7] In the Commission's view, "The fact that [these disclosures] are not published for purposes of informing the securities markets does not alter the mandate that they not violate antifraud proscriptions."[8]

NABL believes that the exponential growth of publicly available information now makes it imperative for the Commission to distinguish between the types of information that are made publicly available by an issuer or obligated person and to provide guidance with respect to the associated antifraud liability. For example, (a) information that is subjected to review through an issuer's secondary disclosure process before posting on EMMA (for example, quarterly information provided in satisfaction of a continuing disclosure undertaking) would be expected to be more reliable than (b) information posted on an issuer's website in advance of a board meeting (for example, background material for an agenda item), which in turn would be expected to be more reliable than (c) information that is not posted on an issuer's website (for example, statements made to local media characterizing the status of labor negotiations).[9]

Disclaimers. NABL recognizes that some issuers or obligated persons may voluntarily wish to provide financial or other information that is not required under a continuing disclosure undertaking or Rule 15c2-12 information (i.e., information that falls between that described in (a) and (b) in the preceding paragraph). Although NABL believes that the best practice would be

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[6] The 1994 Interpretive Release, at FN1.

[7] *Id.* at FN 87.

[8] *Id.* at FN 88.

[9] In some circumstances (for example, the instructions to SEC Form 8-K), the Commission has provided that information "furnished" to it (rather than "filed" with it) will be relieved from some (but not all) liability provisions under the federal securities laws. The Commission should consider a distinction similar to the furnished/filed distinction in providing guidance with respect to antifraud liability associated with publicly available information in the municipal securities market.

for issuers and obligated persons to subject this information to a robust secondary market disclosure review process before posting it on EMMA, it may be determined that such information should be disseminated as quickly as possible and should only be posted on the issuer's or obligated person's website, perhaps under an "investor relations" icon with an appropriate disclaimer that the information is preliminary, unaudited, partial, not presented in accordance with GAAP, etc.[10]

As discussed in the 2010 NABL Statement, disclaimers are widely used in official statements prepared in connection with primary offerings of municipal securities, but the Commission has not directly addressed or provided advice with respect to their use by issuers, conduit borrowers, trustees, or credit enhancement providers. NABL suggested that the Commission clarify that official statement disclaimers, in certain instances, could be used to appropriately limit the disclaiming party's liability, provided that (1) the disclaimer is specific and appropriately tailored as to the information disclaimed, (2) the disclaiming party does not know, and is not reckless in not knowing, that the statements disclaimed are materially false or misleading, and (3) the disclaimer does not materially mislead investors as to the disclaiming party's responsibilities under the federal securities laws. NABL now suggests that the Commission recognize that disclaimers that accurately describe the limitations of the information provided, may also be used in connection with secondary market disclosure.

***Summary*.** NABL suggests that (a) the recommendations it made in the 2010 NABL Statement with respect to the responsibilities of issuers, the members of issuers' governing bodies and issuers' staff for primary offering disclosure should be extended to secondary market disclosure of interim financial and other information and (b) the Commission provide guidance as to how issuers and obligated persons, through the use of appropriate disclaimers, can reasonably limit liability under the antifraud provisions for secondary market disclosure of interim financial and other information. Such guidance would facilitate the Commission's goal to have more timely information provided to the municipal securities market.

[10] As pointed out in footnote 20 to the 2010 NABL Statement, "the kind of analysis often appropriate in an official statement will delay and inhibit the timely release of such information. Institutional investors and other market participants have made clear that getting such information promptly is more important than requiring any analysis of what it means or what trend it reflects."

Q2. When, if ever, do remarketings of demand securities[11] constitute "primary offerings" for purposes of SEC Rule 15c2-12?

Importance of Ascertaining Meaning of "Primary Offering". By repealing the exemption in Rule 15c2-12 from the continuing disclosure requirements afforded to large denomination demand securities issued on or after December 1, 2010, the Commission made the meaning of "primary offering" relevant to remarketings of demand securities for the first time.

The term "primary offering," as defined by Rule 15c2-12, describes when a broker-dealer must comply with the requirements of the Rule in purchasing, offering, and selling municipal securities. Since purchases, offers, and sales of large denomination demand securities were previously exempt from all provisions of the Rule, broker-dealers did not need to determine which remarketings, if any, are primary offerings. In remarketing demand securities issued on or after December 1, 2010, however, broker-dealers must comply with the continuing disclosure requirements of the Rule whenever the remarketing is a primary offering. They therefore must either be able to determine when a remarketing is a primary offering, or they must assume that all remarketings are primary offerings and incur the added time and expense (and risks to liquidity) associated with compliance.

As described in more detail below, NABL accordingly suggests that the Commission clarify that, in order to comply with Rule 15c2-12, remarketing agents do not need to reasonably determine that a currently complying continuing disclosure undertaking (CDU) has been entered into upon each remarketing of demand securities at the option of the owners or at the end of commercial paper mode rate periods.

Whenever purchasing, offering, or selling municipal securities in a non-exempt primary offering, broker-dealers must reasonably determine that the issuer or an obligated person has undertaken to provide to the Municipal Securities Rulemaking Board (a) audited financial statements (and updates of quantitative financial and operating data of the type included in the offering document prepared for the offering, which must be specified in the undertaking) for each obligated person annually and (b) timely notice of certain events. Broker-dealers must take steps to reasonably determine (1) that a continuing disclosure undertaking is in place, (2) that it complies with the requirements of the Rule, and (3) that it is reasonable to conclude, after reviewing compliance by the issuer with prior continuing disclosure undertakings, that the issuer will comply with the new continuing disclosure undertaking.

Even though a continuing disclosure undertaking may meet the requirements of the Rule when demand securities are initially issued, it may cease to meet the requirements of the Rule for a subsequent remarketing of the demand securities in a "primary offering" if, for example, (a) one or more additional obligated persons (e.g., new members of a nonprofit healthcare obligated group) become obligated to pay the demand securities and have not been added to the continuing disclosure undertaking, or (b) the offering document incorporates by reference an obligated person's post-issuance continuing disclosure filings and these contain quantitative financial or operating data of a type not specified in the continuing disclosure undertaking. If a remarketing

[11] See Appendix C for a summary discussion of "demand securities."

agent must make an inquiry as to the existence of a new obligated person or the incorporation of new financial or operating data into the offering document, or other possible events that could require an amendment to the continuing disclosure undertaking, before every remarketing of tendered demand securities, it is likely that both the cost and timeliness of remarketing efforts would be adversely affected. In fact, it is likely that remarketing agents would be unable to remarket demand securities with daily demand privileges without making daily inquiries to assure compliance with the Rule when and if demand securities are tendered and remarketed.

The Commission recognized this unwarranted burden before it adopted the Rule amendments that repealed the exemption for demand securities, since it grandfathered demand securities outstanding before the effective date of the amendment to avoid the market disruption that could result. However, the grandfather provision does not at all mitigate the burden for demand securities issued on or after December 1.

Current Lack of Clarity in Meaning of "Primary Offering" in Remarketings of Demand Securities. The Rule defines "primary offering" as "an offering of municipal securities directly or indirectly by or on behalf of an issuer of such securities." As stated and interpreted to date, the definition does not make clear if and when a remarketing of demand securities after their initial issuance is a primary offering of securities. Until clarified, the Rule will effectively require conscientious broker-dealers to perform unwarranted procedures before remarketing tendered demand securities, with the consequences described above.

The definition of "primary offering" in Rule 15c2-12 does clarify that it includes remarketings that are associated with a decrease in the minimum authorized denomination below $100,000 or an increase in the frequency of demands to more than once every nine months. The Commission staff has made clear that primary offerings are not limited to such remarketings, though. In *Pillsbury, Madison & Sutro,*[12] the Commission staff stated that the definition includes every remarketing that is directly or indirectly on behalf of an issuer and that the remarketings in question there were primary offerings because an obligated person was obligated to purchase the tendered securities if they were not successfully remarketed.

In response to comments on the proposed Rule change that pointed out the definitional uncertainty posed by the Rule and the *Pillsbury* letter, the Commission stated in adopting the most recent Rule amendments that "remarketings of VRDOs *may* not be primary offerings" (emphasis added) and added the following attempt at clarification in a footnote:

> "Making a determination concerning whether a particular remarketing of demand securities is a primary offering by the issuer of the securities requires an evaluation of relevant provisions of the governing documents, the relationship of the issuer to the other parties involved in the remarketing transaction, and other facts and circumstances pertaining to such remarketing, particularly with respect to the extent of issuer involvement."[13]

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[12] *Pillsbury, Madison & Sutro* (March 11, 1991).

[13] SEC Release No. 34-62184A (June 10, 2010).

While helpfully pointing out that the extent of issuer involvement in a remarketing should govern when a new determination must be made by the remarketing agent as to the existence of a then-complying continuing disclosure undertaking, the footnote unfortunately failed to clearly distinguish remarketings that are not primary offerings.

The "facts and circumstances" interpretation of the "primary offering" clarification effectively makes it impossible for a remarketing agent to readily determine that any remarketing is clearly not a primary offering for purposes of the Rule. The clarification states that document provisions and issuer relationships are important, but it does not say which ones lead to a primary offering conclusion and which ones lead away from it. While the extent of issuer involvement in a remarketing is stated to be particularly important, that is clearly the case only in identifying other facts and circumstances that could affect the conclusion, not overriding the importance given to document provisions and issuer relationships.

In routine remarketings, the issuer or another obligated person may be required to purchase demand securities if they are not remarketed, or may have contracted for a bank to purchase them in that case and to pay the bank a higher rate of interest on the securities than the rate payable to public investors, and it will have contracted with a remarketing agent to use best efforts to remarket. These typical facts would suggest document provisions and issuer relationships that make the remarketing look like a primary offering (made on behalf of the issuer because it avoids an issuer purchase option or higher interest rate). On the other hand, routine remarketings (those made of demand securities tendered at the instance of an investor or at the end of a commercial paper mode rate period and not in connection with a mode change or credit substitution) are typically completed with no issuer or obligated person involvement at all. That fact or circumstance would suggest that the remarketing is not a primary offering. Faced with these conflicting signals, unless the Commission brings further clarity to the subject, a remarketing agent cannot safely remarket demand securities in routine remarketings without assuming that each remarketing is a primary offering.

Clarification that Routine Remarketings are Not "Primary Offerings". Rule 15c2-12 is not an anti-fraud rule. Rather, it is a procedural rule intended to reduce the opportunities for fraud. As a procedural rule, it should make clear when it applies (and when it does not) and what is required for compliance. To make clear when the continuing disclosure requirements of the Rule apply to remarketings, we recommend that the Commission clarify, by Rule amendment or interpretive statement, that the requirements do not apply when demand securities are merely tendered at the option of an investor or upon expiration of a rate period in a commercial paper mode, provided that all securities of the issue are not then required to be tendered for remarketing (e.g., in connection with the expiration or replacement of a letter of credit or liquidity facility or a change in interest rate mode) and there is no accompanying change in a material obligor on the securities. While mandatory tenders of an entire issue may sufficiently involve the issuer or other obligated person[14] and (at least when followed by a remarketing)

[14] As noted in the September 23, 2009 comment letter that NABL submitted in connection with the amendments to Rule 15c2-12 that became effective on December 1, 2010 (www.nabl.org/library/documents/1113), some types of remarketings following mandatory tenders of demand securities (e.g., conversions among short-term interest rate modes) involve issuers or other obligated persons to a very limited extent and, arguably, should not be treated as primary offerings.

occur with sufficient notice to allow a remarketing agent to comply with the Rule without adversely affecting liquidity or the cost of demand securities, optional tenders by the holder and remarketings of securities in a commercial paper mode can occur at any time on short notice and, as noted above, generally do not involve the issuer or other obligated person.[15]

By adopting such an interpretation, the Commission would not undermine the adequacy of continuing disclosure available to investors in demand securities. If an existing continuing disclosure undertaking failed to satisfy the requirements of the Rule for a remarketing due to the incorporation of new types of data filed with the MSRB, that data would nevertheless be accessible to investors. In addition, the existing undertaking to provide notice of specified events would remain fully effective, except possibly for notice of insolvencies of any new immaterial obligated person. Finally, since demand securities may be tendered for repurchase at any time, investors would have the means to protect themselves against non-compliant continuing disclosure undertakings after they purchase demand securities in remarketings that follow tenders for purchase at the option of holders or at the end of commercial paper mode rate periods.

[15] Should the Commission be willing to clarify that the continuing disclosure requirements of Rule 15c2-12 do not apply to remarketings of demand securities tendered at the option of the holders or at the end of a commercial paper rate period, the Commission also should clarify that such remarketings do not constitute "secondary distributions" under the federal securities laws. For a fuller discussion of when remarketings may become secondary distributions, see Robert A. Fippinger, *The Securities Law of Public Finance* §§ 6:6.2 and 7:2.4 (2d ed. 2006).

Q3. Does the exemption in SEC Rule 15c2-12 for sales to 35 or fewer sophisticated purchasers apply to primary offerings of demand securities?

NABL suggests that the Commission confirm that the exemption from Rule 15c2-12 afforded to large denomination securities sold to 35 or fewer investors, if they are believed to be knowledgeable and purchasing for their own account without a view to distributing, remains effective for offerings of demand securities.

When the Commission repealed the exemption from Rule 15c2-12 that had been applicable to demand securities, it failed to make clear whether the exemption afforded by paragraph (d)(1)(i) of the Rule to securities with authorized denominations of $100,000 or more that are sold to 35 or fewer persons whom the broker or dealer reasonably believes have knowledge and experience that enable them to evaluate the merits and risks of the investment and are not purchasing for more than one account or with a view to distributing the securities (the "limited sale exemption") could continue to apply to VRDO offerings. The Commission should confirm that the limited sale exemption remains effective for offerings of demand securities. The Rule ambiguity should be resolved so that brokers and dealers are fairly apprised of their legal duties in offering and remarketing demand securities. It should be resolved by preserving the applicability of the exemption, since owners are better able to protect themselves from the consequences of stale or otherwise inadequate disclosure better than owners of long-term securities without demand privileges, to which the exemption clearly continues to apply.

Recent Ambiguity Relating to Rule. Prior to the amendments to Rule 15c2-12 that became effective on December 1, 2010, the Rule contained two exemptions that could apply to offerings of demand securities: (1) the limited sale exemption afforded by paragraph (d)(1)(i) and (2) the demand securities exemption afforded by paragraph (d)(1)(iii).[16] The December 1 amendments repealed the demand securities exemption, but not the limited sale exemption. The amendments also added paragraph (d)(5), which states that, except for the provisions of paragraphs (b)(1) through (b)(4) and except for grandfathered demand securities outstanding on November 30, 2010 "this section [i.e., Rule 15c2-12] shall apply to a primary offering" of demand securities that formerly qualified for the demand securities exemption.

Reading paragraph (d)(5) together with paragraph (d)(1), brokers and dealers may reasonably conclude that the Rule, as amended, continues to exempt primary offerings of demand securities that qualify for the limited sale exemption. Nonetheless, Commission staff members have made public comments warning broker-dealers not to rely on the limited sale exemption. As we understand the argument, if an initial primary offering of demand securities was exempt under Rule 15c2-12 because of satisfying the exemption provided by paragraph (d)(1)(iii), and there is a remarketing of such securities that is a new primary offering, such remarketing would continue to be exempt under Rule 15c2-12 only if it satisfies the grandfather provision of new paragraph (d)(5). If it does not satisfy such grandfather provision, the new

[16] The prior Rule and the current rule also include the commercial paper exemption contained in paragraph (d)(1)(ii). This exemption, conceivably, could apply to demand securities; thus, the logic of our arguments about the applicability of the limited sale exemption to demand securities also could be applied to the applicability of the commercial paper exemption to demand securities.

primary offering cannot otherwise look to the other exemptions provided by paragraphs (d)(1)(i) and (d)(1)(ii). Similarly, a new issue of demand securities could not avail itself of either exemption. We do not understand this rationale. If a primary offering satisfies either of the two exemptions that were not amended, such primary offering should be exempt. To conclude otherwise leads to anomalous results, as explained below.

Need for Commission Resolution of Ambiguity. As noted above, Rule 15c2-12 is not an anti-fraud rule. Rather, it is a procedural rule intended to reduce the opportunities for fraud. As a procedural rule, it should make clear when it applies and when it does not. Some obligated persons are not willing (for competitive reasons) to make their financial statements available to the public. Other obligated persons are loathe to incur the expense of preparing and vetting annual disclosure requirements unless necessary to issue municipal securities. Broker-dealers should have fair notice as to whether they may offer demand securities in these circumstances without a continuing disclosure undertaking.

Logic of Commission Resolution of Ambiguity in Favor of Limited Sale Exemption. The Commission should clarify that the limited sale exemption continues to apply to eligible offerings of demand securities, because (1) doing so is consistent with the purposes of the exemption and (2) not doing so would be anomalous.

When the Commission first proposed the Rule in 1988, it stated that the "primary intent of the rule is to focus on those offerings that involve the general public, and which are likely to be traded in the secondary market," and it therefore asked for comment as to whether offerings to a limited number of sophisticated investors should be exempted.[17] Commentators on the proposed Rule endorsed such an exemption "almost unanimously."[18] In its adopting release, the Commission particularly referred to NABL's recommendation that the Rule exempt "privately placed issues where purchasers conduct their own credit investigation."[19] Consequently, in adopting the final Rule, the Commission included a limited sale exemption in addition to independent exemptions for demand securities and short-term securities, notwithstanding a concern that securities sold in exempt limited sales might find their way into the secondary market.

In most cases, purchasers of demand securities make their investment decision exclusively or principally on the strength of a letter of credit or bond insurance and a purchase agreement with a bank, and the purchasers rely on their own investigation into and other publicly available materials about the credit of the credit enhancer (rather than the typically one-page description of the credit enhancers included in offering documents). In addition, they almost always dispose of their holdings through a remarketing agent, rather than by direct sales to other investors. The remarketing agents, through their remarketing agreements with the issuer or other obligated person, have ongoing access to information about changes in the credit of the obligated persons, which they are able to use if and when required to remarket the securities.

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[17] SEC Release No. 34-26100 (September 22, 1988) at notes 41-42.

[18] SEC Release No. 34-26985 (June 28, 1989) at note 72.

[19] *Id.* note 46.

Consequently, just as in a private placement, demand securities are sold to purchasers who can fend for themselves under circumstances under which they have access to the information that they need to make an informed investment decision. Accordingly, including demand securities among those that qualify for a limited sale exemption is consistent with the purposes of the exemption.

In addition, it would be inappropriate to afford the limited sale exemption to long-term securities without a demand privilege while denying the exemption to demand securities. The value of long-term fixed rate securities can vary substantially with changes in the creditworthiness of the issuer of or other obligor on the securities. Without access to current credit information, it would therefore be difficult to value such securities or make informed decisions as to whether to purchase, hold, or sell the securities. In the case of demand securities, on the other hand, the rate of interest borne by the securities is adjusted to maintain a constant value, and when supported by a letter of credit issued by a creditworthy bank, their value is not affected by changes in the creditworthiness of the issuer or other obligor on the securities. In addition, if investors who are not voluntarily supplied with the updated credit information that they deem necessary to maintain a position in the demand securities, they may exercise their demand privilege and be taken out of the investment at their cost basis. In these circumstances, we are aware of no principled reason for extending the limited sale exemption to offerings of long-term fixed-rate securities and not extending the exemption to demand securities.

APPENDIX A

COPY OF 2010 NABL STATEMENT

National Association
of Bond Lawyers

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May 14, 2010

Commissioner Elisse B. Walter
U.S. Securities and Exchange Commission
100 F St NE Room 10200
Washington, DC 20549

Re: Transmittal of NABL's Suggestions for Interpretive Guidance Update

Dear Commissioner Walter:

On behalf of the National Association of Bond Lawyers (NABL), I thank you for taking the time to meet with Ken Artin, Terri Guarnaccia, John McNally, Penny Rostow, and Jodie Smith on April 12, 2010 to discuss the SEC's initiative to update the 1994 Interpretive Guidance and related matters. NABL commends you for your interest in reviewing certain matters where additional guidance will enhance the municipal securities market.

As you have requested, we are pleased to enclose our statement describing those areas that we believe could benefit from clarification and guidance regarding the application of the federal securities laws to municipal finance. In preparing these comments, we have read with care your presentation of October 28, 2009, and the recent speech by Chairman Schapiro that was presented to the ICI regarding the municipal securities market. We appreciate the opportunity to offer our suggestions as you update the 1994 Interpretive Guidance and we would similarly like to be helpful as you and others at the Commission begin to work through other aspects of your ambitious agenda for the municipal sector.

NABL is an organization of approximately 2,800 public finance attorneys, and our mission statement is "to promote the integrity of the municipal market by advancing the understanding of and compliance with the law affecting public finance." We respectfully provide this submission in furtherance of such mission statement. The statement was prepared under the auspices of the NABL Securities Committee by the individuals listed on Exhibit I of the statement, and was approved by the NABL Board of Directors.

We thank you for this opportunity. If NABL can provide further assistance, please do not hesitate to contact me or Penny Rostow in our Washington Office.

Sincerely,

Kathleen C. McKinney

Kathleen C. McKinney
President
National Association of Bond Lawyers

National Association *of* Bond Lawyers

STATEMENT
OF THE
NATIONAL ASSOCIATION OF BOND LAWYERS
TO
UNITED STATES SECURITIES AND EXCHANGE COMMISSION
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MUNICIPAL SECURITIES DISCLOSURE

In response to an invitation by Commissioner Elisse B. Walter, this statement is submitted to the United States Securities and Exchange Commission (the "SEC" or the "Commission") on behalf of the National Association of Bond Lawyers ("NABL") relating to the SEC's anticipated update to SEC Release No. 33-7049 (the "1994 Interpretive Release"), which addressed municipal securities disclosure. This statement identifies issues NABL believes can benefit from SEC clarification and suggests guidance regarding these issues that NABL believes would be helpful and appropriate. This statement also anticipates forthcoming NABL guidance and technical assistance for improving municipal securities disclosure practices, including NABL white papers on disclosure regarding use of interest rate swaps and other derivative products by issuers and on disclosure regarding variable rate securities.

This statement is organized as a series of questions and answers under the following headings: (1) Current Issues Common to Both Primary Offering Disclosure and Secondary Market Disclosure; (2) Current Issues Relating to Primary Offering Disclosure; and (3) Other Issues of Interest. Certain capitalized terms used frequently in this statement are defined in the glossary located on page 21 of this statement.

This statement was prepared by an *ad hoc* subcommittee of the NABL Securities Law and Disclosure Committee comprised of those individuals listed on Exhibit I and was approved by the NABL Board of Directors.

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CURRENT ISSUES COMMON TO BOTH PRIMARY OFFERING DISCLOSURE AND SECONDARY MARKET DISCLOSURE

Q1. What are the appropriate responsibilities of an issuer and its governing body in approving or authorizing primary offering disclosure and secondary market disclosure?

Disclosure Responsibilities of Members of Issuer's Governing Body. Although municipal securities are exempt from most sections of the Securities Act and the Exchange Act, issuers remain subject to the antifraud provisions of those acts. Briefly summarized, Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act (and Rule 10b-5 thereunder) prohibit an issuer of municipal securities from making a material misstatement or omission in connection with the offer or sale of a security. Such provisions also extend to members of the issuer's governing body when they themselves make (or are deemed to make) statements in connection with the offer or sale of the issuer's securities (for example, by approving a disclosure document for that purpose). However, unlike in corporate offerings (where directors are liable for material misstatements and omissions in a registration statement unless they exercise reasonable care to prevent them), members of a municipal issuer's governing body have liability only to the extent that they have taken action that is actionable under Section 17(a) of the Securities Act or Section 10(b) of the Exchange Act.

Lessons from Orange County. The Commission has established the following principles regarding the potential liability of a member of a governing body in reviewing and approving offering materials:

- A public official may not *approve* disclosure that the official knows to be false.
- A public official may not *authorize* disclosure while recklessly disregarding facts that indicate that there is a risk that the disclosure may be misleading.[1]

If a member of the issuer's governing body has "knowledge of facts bringing into question the issuer's ability to repay the securities, it is reckless for that official to approve disclosure to investors without taking steps appropriate under the circumstances to prevent the dissemination of materially false or misleading information regarding those facts."[2]

Legal Distinction between Approving Offering Materials and Authorizing Preparation of Offering Materials. There should be a distinction between action by members of a governing body approving an offering document, on the one hand, and action authorizing the preparation of an offering document by issuer staff and delegating responsibility for deeming it complete, on

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[1] Securities and Exchange Commission, Report on Investigation in the Matter of County of Orange, Cal., SEC Rel. No. 34-36761 (Jan. 24, 1996) (the "Orange County Report").

[2] *Id.*

the other hand. SEC enforcement actions largely use the concepts interchangeably,[3] as reflected in the two principles from the Orange County Report highlighted above. In the Orange County Report, the SEC took issue with resolutions adopted by the County Board of Supervisors that approved misleading offering materials and authorized the retention of certain public finance professionals to assist in preparation of the materials.

We suggest that the Commission clarify that, for purposes of assessing the responsibilities of members of an issuer's governing body under the federal securities laws, a member has a legal duty to exercise care in approving the text of an offering document that will be distributed or otherwise made accessible to investors in the issuer's securities (that is, a member who knowingly or recklessly approves a document with a material misstatement or omission will be liable for a violation of the federal securities laws), but a member who authorizes staff and public finance professionals (whom the member reasonably believes to be capable) to prepare and approve the document (and has no actual knowledge of "red flags") would not be liable for a violation of the federal securities laws if the offering document contains a material misstatement or omission (although the issuer, through the actions of its staff, might be liable for such a violation)[4].

Delegation to and Reliance Upon Staff or Professionals. As discussed above, issuers have "an affirmative obligation to know the contents of their securities disclosure documents, including their financial statements" and this duty is not discharged by the employment of public finance or accounting professionals.[5] Facts may be known to an issuer because of information included in its files. In addition, in enforcement actions, the SEC has shown a willingness to impute knowledge of material facts to the issuer itself based on knowledge of the issuer's officials.[6] Accordingly, a governing body member could help an issuer satisfy its securities law duties by reviewing the document and comparing it to facts known to the member. However, it should be recognized that there are often significant differences between the knowledge levels of a member of an issuer's governing body and a member of the issuer's staff with respect to the finances of a governmental entity, and, in most cases, governing body members would almost certainly need to rely on the issuer's staff and retained professionals in compiling and preparing the document. We suggest that the SEC confirm that, in approving offering documents, governing body members may rely on public finance professionals to the extent that such reliance is reasonable.[7] The next question is how governing body members can establish the reasonableness of such reliance.

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[3] *Id.*

[4] *Cf.* In re Worldcom, Inc. Securities Litigation, 2005 WL 638268 (S.D.N.Y.)

[5] City of Miami, Fla., SEC Rel. Nos. 33-8213 (March 21, 2003).

[6] In the Matter of City of San Diego, Cal., SEC Release No. 54745 (Nov. 14, 2006); City of Miami, Fla., SEC Rel. Nos. 33-8213 (March 21, 2003).

[7] William R. McLucas, Dir., Div. of Enforcement, SEC, Remarks at the Government Finance Officers Association (Jan. 30, 1996).

We suggest that the Commission clarify that adopting and then adhering to a reasonable disclosure process[8] will satisfy a governing body member's responsibility, absent knowledge of a material misstatement or omission, when taking action to adopt or approve an offering document. We also suggest that the Commission clarify that whether reliance is reasonable depends on the facts and circumstances, including the experience and expertise of the professionals retained, whether the governing body members have reason to question the accuracy of the information provided by such professionals, and whether the governing body has adopted and has followed procedures for preparing offering documents that are reasonably designed to produce accurate and reliable information.

Scope of Governing Body Responsibility for Secondary Market Disclosure. The SEC has concluded that materially misleading statements in an issuer's secondary market disclosures may violate the antifraud provisions in connection with the issuance and sale of a security because it affects trading on the secondary market.[9] We suggest that the Commission clarify whether members of an issuer's governing body have the same duty to exercise care in approving secondary market disclosures that they have in approving to primary market disclosures (that is, an offering document). In short, do the principles of the Orange County Report extend beyond disclosure documents used in a primary offering? We suggest that the Commission clarify that, although an issuer as entity is liable for misleading disclosure in any disclosure as broadly defined in the 1994 Interpretive Release (that is, any disclosure reasonably expected to reach investors), individual members of a governing body are liable only for secondary market disclosures that they approve with knowledge of, or reckless disregard for, a material misstatement or omission.

Issuer Responsibility for Statements Obtained from Third Parties. All statements in an issuer document are presumed to be statements made by the issuer, but the question is open whether issuers can effectively disclaim this presumption for certain types of information. Most practitioners believe that, if the information in the offering materials concerns third parties and is obtained from sources that are reasonably believed to be reliable, in the absence of any "red flags" that would suggest that the information is false or misleading, the issuer should not have a duty to verify (and may not be in a position to verify) the information. We suggest the Commission clarify that issuers may effectively use disclaimers in the official statement to avoid any implied adoption or verification of information obtained from third parties. A disclaimer should be effective to avoid liability for materially inaccurate or misleading third-party

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[8] Although, with more than 50,000 municipal issuers, it is difficult to generalize about the content of reasonable disclosure processes, *Disclosure Roles of Counsel*, at 80-81, suggests that public officials and their counsel consider the following questions in establishing a basis for reasonable reliance: (1) Have we adopted disclosure processes for preparing Official Statements, and if we have, am I satisfied that such processes have been reasonably designed to produce accurate and reliable information? (2) Do I have a reasonable basis to have confidence in the integrity and competence of the financing team (e.g., financial staff, in-house counsel, outside counsel) that has prepared the Official Statement? (3) Do I know anything that would cause me to question the accuracy of the disclosures or that would indicate that they are misleading? (4) Do I know of any potentially material issues that should be brought to the attention of the financing team or for which I would like further explanation?

[9] City of Miami, Fla., SEC Rel. Nos. 33-8213 (March 21, 2003).

representations, if the issuer neither knows of the defect nor has reason to doubt the accuracy and completeness of the representations.[10]

Issuer Responsibility for Offering Materials in Conduit Financings. It has been a longstanding market practice that the responsibilities of issuers and members of an issuer's governing body are different in conduit offerings (in which the issuer is not obligated to repay the offered securities) than their responsibilities in offerings backed by the issuer's own credit. In conduit offerings, most information contained in the disclosure materials pertains to the third-party conduit borrower, since repayment of the securities will depend entirely on the conduit borrower's ability to meet its payment obligations under the conduit loan, lease, or purchase obligation. Based on the text of the applicable antifraud provisions, a conduit borrower is subject to the same duties under the antifraud provisions of the Securities Act and the Exchange Act as a governmental issuer is in an offering backed by its own credit.[11]

We suggest that the Commission clarify the distinction between the responsibilities of conduit issuers and conduit borrowers and, in particular, confirm that a conduit issuer has no duty to verify the accuracy and completeness of information provided by or pertaining to the conduit borrower, or by or to credit and liquidity facility providers and guarantors, so long as the conduit issuer has negated any implication that it has undertaken to verify the information and has no reason to believe that the conduit borrower's information is inaccurate or misleading.[12]

Summary. Consistent with the suggestions above, we recommend that the Commission offer guidance relating to the roles and responsibilities of issuers, their governing bodies, and designees with respect primary and secondary market disclosure for municipal securities offerings.

Q2. What measures should issuers employ to prevent disclosed financial data in official statements from being materially misleading due to the volatility or seasonality of the data or economic conditions?

Investors often require, and issuers frequently provide, in official statements three to five years of historical financial and operating data in offering documents, so that investors can

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[10] For further discussion of the appropriate use of disclaimers, see below under "Q5. What are the appropriate uses and limitations of disclaimers in official statements?"

[11] See, e.g., Paul S. Maco, Dir. Officer of Municipal Securities, SEC, Points Every Market Participant Should Keep in Mind, Remarks Made Before the Florida Government Finance Officers Association (June 7, 1999) ("Hospital and other conduit borrowers should be aware that the anti-fraud provisions apply to such [continuing] disclosure and stale, misleading disclosure carries with it potential liability under the antifraud provisions."). Therefore, investors can bring claims under the antifraud provisions against conduit borrowers in the same way as they can pursue conduit issuers. See, e.g., Sonnenfeld v. City of Denver, 100 F.3d 744, 746 (10th Cir. 1996) ("Although § 10(b) does not provide an express private cause of action, the existence of an implied private cause of action under § 10(b) and Rule 10b-5 is so well established in the courts that its existence is "beyond peradventure.")

[12] In a conduit financing, where the conduit borrower, underwriters, and their counsel are all involved with checking the accuracy and completeness of the offering document, there would appear to be insufficient public benefit to impose a duty on the conduit issuer to check and cause the conduit issuer, or the conduit borrower, to incur the associated expense.

discern trend lines and make educated assessments about the issuer's future financial prospects.[13] If the data disclosed in an offering document is dated or otherwise fails to disclose known material facts that, unless disclosed, make the disclosed data misleading as to future financial prospects, then the issuer should add data or narrative, or both, to avoid a material misstatement in or a material omission from the offering document. When economic or financial conditions are volatile, as they have been over the last two years, there is a greater risk that the disclosure of historical data alone may be misleading. Accordingly, when disclosing historical financial and operating data, issuers should exercise care that known material trends, demands, commitments, events, and uncertainties are also disclosed if necessary to prevent the disclosed data from being misleading.

Issuers should disclose financial results of operation in comparative form through a recent date if there is a risk that financial results of operation have deteriorated compared to the trend line implied by disclosed annual financial data.[14] The Commission has previously issued a cease-and-desist order against Maricopa County, Arizona, for failing to disclose a material deterioration in financial condition since the date of the most recent financial statements included in its offering document.[15] Issuers may look to Commission forms for registered offerings as guidance to avoid possible staleness of financial disclosure and omissions of known material trends, demands, commitments, events, and uncertainties.[16]

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[13] By way of comparison, the Commission requires that at least five years of selected financial and operating data be provided in registration statements. "The purpose of the selected financial data shall be to . . . highlight certain significant trends in the registrant's financial condition and results of operations . . . . Discussion of . . . any material uncertainties should also be included where such matters might cause the data reflected herein not to be indicative of the registrant's future financial condition or results of operations." Regulation S-K, Item 301 and Instructions to Item 301, notes 1 and 2.

[14] There are ways other than comparative data to show recent financial developments that may be material. These include selected data and narrative, which in certain circumstances may be more practical and effective in disclosing recent events than full comparative data.

[15] In re Maricopa County, Securities Act Release No. 7354 (October 3, 1996).

[16] In general, registration statements must include an interim balance sheet as of a date that is within 130 (for accelerated filers) or 135 days of the expected effective date of the filing, except that interim financial statements for the first three quarters may be filed if the effective date is within 60 (for large accelerated filers), 75 (for other accelerated filers), or 90 days (for all other filers) after fiscal year end. Regulation S-X, Rule 3-2. The Commission has also noted that, "[t]o avoid providing investors with a stale, and therefore potentially misleading, picture of financial condition and results of operations, issuers and obligors need to release their annual financial statements as soon as practical." 1994 Interpretive Release at n. 60. Of course, if financial results of operations since the last disclosed period are not materially different than those that would be predicted by the trend line reasonably inferred from disclosed annual results, disclosure of interim results in an exempt offering would not be required by the federal securities laws.

The rules applicable to corporate issuers and corporate issues must, however, be read in light of the unique aspects of the municipal securities marketplace. The Commission previously has recognized the need for flexibility given the diversity in municipal issuers and municipal issues. Those differences include the size, sophistication, and resources of the issuer. They also include different processes for the collection and dissemination of financial data. Furthermore, different events may require substantial legal, financial, and practical analysis to determine materiality and the best approach to disclosure.

Interim Financial Statements. Even when an issuer discloses in an official statement interim financial statements that are relatively current, it should exercise care to determine whether it knows (and, if so, to disclose) material facts or uncertainties that, unless disclosed, would render the disclosed information misleading.[17] For example, if an issuer's property tax revenue is based on the assessed value of taxable property within its jurisdiction as of a date, or the unfunded accrued actuarial liability of its pension obligations is based on plan assets valued as of a date, that in either case is substantially prior to the date of the offering document, and the issuer knows that property or asset values have declined materially since such earlier date, the issuer should disclose that fact and the likely consequence, if material.

Market Risk. Similarly, if an issuer's financial condition is subject to market risk to an extent that is material, that risk should be disclosed. For example, if an issuer has agreed to post collateral for interest rate swap transactions and the extent of its future unrestricted cash and investments could vary with changes in prevailing market interest rates, that fact and uncertainty should be disclosed, if material. The impact of material facts and uncertainties should be disclosed quantitatively if that can be done accurately and reliably, and otherwise should be disclosed in narrative indicating the direction and general magnitude of the impact.[18]

Fluctuations. Issuers should exercise care to avoid misleading impressions concerning the stability of their financial condition throughout the fiscal year. Many governmental units experience seasonal inflows of tax or utility revenue and outflows of debt service. Consequently, their liquid assets fluctuate throughout the fiscal year. If comparative balance sheet information is disclosed only at the end of fiscal years or interim periods, and if, due to seasonality of cash flow, an issuer's liquid assets have been or are expected to be materially lower at other times in the year, issuers should give consideration to disclosing that fact, including the historical magnitudes of the seasonal swing, if material. Similarly, if the issuer knows of facts or uncertainties (for example, interest rate swap collateral posting or termination risks, dependence on counterparties for cash flow, variable rate demand bond put risks, or commercial paper rollover risks) that could cause its unrestricted liquid assets to be materially reduced, it should disclose those facts and uncertainties, if material.[19]

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[17] In re Maricopa County, Securities Act Release No. 7354 (October 3, 1996), at n. 59.

[18] The Commission has previously cautioned issuers to "assess whether the future impact of currently known facts mandate disclosure . . . . Disclosure of currently known conditions and their future impact is critical to informed decisionmaking." *Id.* In registered offerings, the Commission requires that the registration statement include management's discussion and analysis (MD&A) that "shall focus on material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition. This would include descriptions and amounts of (A) matters that would have an impact on reported operations and have not had an impact in the past, and (B) matters that have had an impact on reported operations and are not expected to have an impact upon future operations." Regulation S-K, Instructions to Paragraph 303(a), no. 3. In registered offerings, registrants must also disclose and quantify market risk, when applicable, in one of three permitted formats. Regulation S-K, Item 305.

[19] NABL is embarking on projects to give guidance to its members on disclosure related to material interest rate swap transactions and disclosure related to variable rate securities. The Commission has previously noted the need to disclose material risks associated with interest rate swap transactions and referred readers to an NFMA publication for guidance regarding that disclosure. *See* 1994 Interpretive Release at n. 57. In a registration statement for a registered offering, issuers must identify in their MD&A "any known trends or any known demands,

Summary. We suggest that the Commission offer guidance to market participants in determining best practices for assessing appropriate and/or additional disclosure in official statements relating to financial data based on trends, demands, events, uncertainties, and related matters.[20]

CURRENT ISSUES RELATING TO PRIMARY OFFERING DISCLOSURE

Q3. How should changes to statements made in a preliminary official statement or final official statement be disclosed to investors?

Use of Preliminary Official Statements and Final Official Statements. The principal document by which municipal bonds are commonly offered to the public is a preliminary official statement.[21] The customary practice of investment bankers and financial advisors is to use the preliminary official statement to provide information on the credit being offered (including recent financial performance), the security provisions, the financial and operating covenants that will be used in the bond offering, and other material information so that the investors may be prepared to make a decision to purchase bonds on the sale date. After the bonds are actually purchased, a final official statement is produced with final information on interest rates, maturities, and other terms specific to the sale.

Rule 15c2-12 reflects this practice. Indeed the preliminary official statement or a draft of the preliminary official statement is normally "the near final official statement" whose review and approval is required by Rule 15c2-12. Furthermore, Rule 15c2-12 clearly recognizes that a near final official statement may, like most preliminary official statements, omit information on such matters as maturities, interest rates, and underwriter compensation.

Updating and Correcting Information. Questions commonly arise as to how disclosure should be made regarding information that should be included in the final official statement but that is not in the preliminary official statement. Examples of information include (1) additional information on the underlying credit, including recent financial and operating information that is requested by investors or that becomes known after the preliminary official statement is released, (2) alterations in or completions of the securities provisions, and (3) in some cases, simply correcting mistakes found in the preliminary official statement.

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commitments, events or uncertainties that will result in or that are reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way." Regulation S-K, Item 303(a)(1).

[20] We note that the above discussion relates specifically to issuer financial disclosure in official statements. Issuers should be free to publish, without such analysis, quarterly or monthly financial information produced pursuant to ordinary internal procedures or a continuing disclosure undertaking. Any attempt to impose upon issuers a responsibility under the antifraud provisions of the federal securities laws to provide, with the release of such interim financial information, the kind of analysis often appropriate in an official statement will delay and inhibit the timely release of such information. Institutional investors and other market participants have made clear that getting such information promptly is more important than requiring any analysis of what it means or what trend it reflects.

[21] There is no legal requirement for a preliminary official statement, although it is market practice to have one in many types of municipal securities transactions.

Appropriate market practice reflects two related factors. First, it is unreasonable to expect an investor who made a preliminary investment decision on the basis of a preliminary official statement to proofread the final official statement to ascertain every change. Based on Rule 15c2-12, an investor would reasonably assume, unless advised otherwise, that all changes between the preliminary and final official statements are of the type permitted by the terms of Rule 15c2-12 to be excluded from the "deemed final" document. Second, the information provided to the investor as of the sale date is the information by which compliance with the antifraud provisions is measured and accordingly that information must be supplemented by the sale date if it is materially misleading or suffers from a misleading material omission.[22]

Today, most preliminary official statements are distributed electronically via emails that contain links to a website containing the offering document. Amendments or supplements to the preliminary official statement can be posted on the same website. In addition, some technology allows the amendment to be distributed to any email address by which the original preliminary official statement was downloaded. Updating and supplementing information contained in a preliminary official statement in many cases can be addressed without the costly practice of a complete reprinting and re-distribution.

Issuers may correct or supplement information in the preliminary official statement by (1) amending (in the case of corrections of statements that were wrong as of their date) or supplementing the preliminary official statement prior to sale or (2) including the corrected or supplemental information in the final official statement, with appropriate emphasis. If material changes to the preliminary official statement are clearly brought to the attention of investors in the final official statement, they have an opportunity to rescind or ratify their decision to purchase, based on the corrected disclosure.

The Commission should not require any single approach to this problem since the facts and circumstances often vary. Minor changes in document definitions, for example, of qualified

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[22] The Commission has cautioned that, because a purchaser of municipal securities can be expected to make its investment decision based on the content of the preliminary official statement, an issuer and an underwriter have duties under the federal securities laws to inform investors of material facts concerning an offering of municipal securities prior to the sale date, if omitted from the preliminary official statement. As part of its 2005 Securities Offering Reform Release, Securities Act Release No. 33-8591 (July 19, 2005), the Commission amplified its views on how the practice of using preliminary official statements in municipal securities offerings fits together with the duties under the federal securities laws to inform investors of material facts concerning an offering of municipal securities. Through interpretive guidance provided in the 2005 Securities Offering Reform Release and through adoption of Rule 159 under the 2005 Securities Offering Reform Release, the Commission made clear that, for purposes of determining whether securities were sold on the basis of materially untrue or misleading statements of fact in violation of Section 17(a) of the Securities Act, information supplied after the date of sale may not be taken into account. As the Commission explained, "Under our interpretation, the time at which an investor has taken the action the investor must take to become committed to purchase the securities, and has therefore entered into a contract of sale, is one appropriate time to apply the liability standards of [Section 17(a) of the Securities Act]." Section 17(a) of the Securities Act provides no private right of action for offerings of municipal securities, but violation of Section 17(a) can subject an issuer or underwriter to an enforcement action by the Commission. Further, material misstatements and omissions in a preliminary official statement or a final official statement can have significant contract law implications for an issuer, an underwriter, and an underwriter's customer. *See generally* Part IV of Securities Act Release No. 33-8591 (July 19, 2005); Robert A. Fippinger, The Securities Law of Public Finance §§ 4:1 *et seq.* (2d ed. 2006).

investments of bond proceeds do not require the kind of highlighting that would be appropriate if the final official statement contained a substantially revised management's discussion of financial performance together with more recent financial statements indicating material adverse changes in operational health. We suggest that the Commission clarify that updates permitted by Rule 15c2-12 do not need highlighting. For updates that cannot be so characterized, we suggest that the Commission encourage all of the following approaches as appropriate practices, depending on the facts and circumstances:[23]

- Preparation and distribution of a pre-sale amendment or supplement to the preliminary official statement. This approach is frequently used when material, adverse changes or corrections to disclosed facts are discovered after the preliminary official statement is released.[24]

- A statement in the final official statement indicating that certain changes have been made, with references to the sections where the changes are noted. This is frequently the proper approach when a number of minor changes have been made that probably do not materially alter the mix of information for investors but are included to ensure that the most accurate and complete information is provided.

- A section variously entitled "Recent Developments", "Recent Events", "Information Supplementing Preliminary Official Statement", or "Changes from the Preliminary Official Statement" that discusses in detail certain specific financial developments or document changes that a reasonable investor might find significant.

- A simple statement that certain changes in the documentation for the transaction have been made and that sections describing such documentation (commonly a summary of documents attached as an appendix) have footnotes, asterisks, or other markers indicating where changes have been made. This permits an interested investor to review those specific sections to see if the changes in the documentation are material without the necessity of re-reading the entire document summaries. This is a common sense way to deal with the common situation where, because of market conditions or investor requests, various

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[23] Circumstances sometimes will necessitate supplementation of the preliminary official statement prior to the sale date (versus highlighting changes in the final official statement), for example, to reflect material, adverse developments. This supplementation may be accomplished through a number of methods, including supplementation through an electronic communication service and supplementation through an amended document distributed to all investors who received the preliminary official statement. For a helpful analysis of how counsel to participants in a securities offering should deal with securities law liability issues when multiple documents are available to be conveyed to purchasers at or before the time of sale of the securities, see Subcommittee on Securities Law Opinions, ABA Section of Business Law, Negative Assurance in Securities Offerings (2008 Revision), 64 Bus. Law. 395 (2009).

[24] The amendment or supplement could take the form of a "wire" if made available to all prospective investors to whom the securities are offered and the issuer clarifies whether it is part of the preliminary official statement for purposes of Rule 15c2-12.

document changes have been made between the date of the preliminary official statement and the sale of bonds.

Anticipatory Language. We suggest that the Commission also encourage the practice under which investors are told in the preliminary official statement that additional or subsequent information is expected to be provided in the final official statement. This may range from more recent operating and financial statistics to updates on litigation or regulatory matters. Again this common sense practice in many cases properly alerts a potential investor to the need to check specific sections of the final official statement. One example is the situation where a final official statement contains subsequent or additional financial or operating information. So long as the reader of the preliminary official statement is reasonably notified that such completions, additions, or changes will likely be made and such information can be easily located, the aims of full and fair disclosure are accomplished with maximum flexibility.

Changes Subsequent to the Final Official Statement. The above practices do not provide complete protection in circumstances in which changes arguably material to an investor's decision have occurred or additional information has become available between the date of the printing of the final official statement and actual closing. Market participants have long had to consider the question of whether subsequent changes are in fact material to an investor's decision and whether the changes require a full re-offering and re-pricing or instead the investor can be informed of such changes, in which circumstances the investor may choose whether to continue with the purchase of the securities. The Commission should encourage any reasonable practice that in such circumstances carries out this purpose, including (1) the recirculation of a revised final official statement, clearly marked and redated to distinguish it from the original final official statement or (2) a brief supplement to the final official statement providing additional or corrected information. If a supplement is clearly written and makes specific reference to the final official statement, there is no reason why this much simpler approach should not be permitted if deemed appropriate by the issuer and underwriter. [25]

Summary. We suggest that the Commission recognize that, given the wide variations of municipal credits and disclosure, there are a variety of appropriate practices relating to updates and amendments that can properly be used to meet the central goal, namely, ensuring that the bond investor has a reasonable opportunity to consider all information material to the investor's decision to purchase.

Q4. What documents are included in the definitions of "preliminary official statement" and "official statement" for purposes of Rule 15c2-12, and must they all be provided to potential customers on request?

Under Rule 15c2-12, brokers, dealer, and municipal securities dealers ("*underwriters*") are required (1) to obtain and review a preliminary official statement before offering municipal

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[25] If the offering is subject to Rule 15c2-12, the underwriters must provide the final official statement to potential customers on request through closing and for a period of time thereafter if the initial distribution of the bonds is still ongoing. It is therefore common for underwriting agreements to require that final official statements be supplemented to reflect material developments during this distribution period, to protect the underwriters from liability for providing a document that is materially inaccurate or misleading when provided.

securities in a primary offering that is not exempt from Rule 15c2-12, (2) to contract to receive a final official statement within seven business days after sale of the securities, (3) to provide the preliminary or final official statement to potential customers on request, and (4) reasonably to determine that an issuer of or obligated person for the securities has undertaken (for the benefit of owners of the securities) to update annually information of the same general type as the quantitative financial information and operating data included in the final official statement. In order to comply with their duties under Rule 15c2-12, underwriters must be able to clearly determine what documents comprise part of the preliminary or final official statement.[26]

Boundaries of Definitions of "Preliminary Official Statement" and "Official Statement". Rule 15c2-12 defines "*final official statement*" in relevant part as "a document or set of documents prepared by an issuer of municipal securities or its representative that is complete as of the date delivered to the Participating Underwriter(s) and that sets forth information concerning the terms of the proposed issue of securities; information, including financial information or operating data, concerning such issuers of municipal securities and those other entities, enterprises, funds, accounts, and other persons material to an evaluation of the Offering . . . . Financial information or operating data may be set forth in the document or set of documents, or may be included by specific reference to documents available to the public on the Municipal Securities Rulemaking Board's Internet Web site or filed with the Commission." The definition does not expressly limit the set of documents to those prepared for distribution to potential purchasers of the securities, nor does it clearly require that all documents in the set be in physical form, even if not available from the MSRB or filed with the Commission.

Rule 15c2-12 defines "*preliminary official statement*" as "an official statement prepared by or for an issuer of municipal securities for dissemination to potential customers prior to the availability of the final official statement." Since paragraph (b)(1) of Rule 15c2-12 requires that the preliminary official statement be deemed final by an issuer of municipal securities as of its date, except for the omission of pricing-related information and ratings, the preliminary official statement must effectively have the same content as the final official statement, except for these omissions. Unlike the definition of official statement, the definition of preliminary official statement limits the term to documents prepared for dissemination to potential customers.

Underwriters frequently have questions as to the boundaries of a preliminary official statement and final official statement for purposes of Rule 15c2-12. For example, are documents filed with the MSRB or contained on an issuer's or obligated person's web site (where they are accessible to investors) part of the preliminary or final official statement if they include "information, including financial information or operating data, concerning" the issuer? Are documents posted on a third-party credit enhancer's web site and referenced in the offering document part of the final official statement? Does the answer depend on whether they are

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[26] The Commission has stated that the implied recommendation that an underwriter makes by participating in an offering implies that the underwriter has a reasonable basis for belief in the truthfulness and completeness of key representations in the disclosure documents used in the offering. Release No. 34-26100 (Sept. 22, 1988). Consequently, underwriters cannot merely treat all documents that could possibly qualify as part of an official statement, because before providing the documents to potential customers on request they would have to evaluate whether the documents include key representations and, if they did, would have to make a reasonable investigation as to the truthfulness and completeness of those representations.

explicitly or implicitly endorsed or otherwise approved in the official statement, or whether they were prepared for use in offering the securities? Are slides included in a "road show" or other presentation to investors part of the preliminary or final official statement? Does the answer depend on whether the investors are provided or permitted to take, retain, access or make copies?

The Commission addressed some of these questions in its 2000 release, Use of Electronic Media:

> For purposes of satisfying its obligations under Rule 15c2-12, a municipal securities underwriter may rely on the municipal securities issuer to identify which of the documents on, or hyperlinked from, the issuer's web site comprise the preliminary, deemed final and final official statements, even if the issuer's web site contains other documents or hyperlinks to other web sites. Hyperlinks embedded within an official statement itself, however, will be considered part of the official statement, even if a municipal securities issuer has not specifically identified the embedded hyperlinked information.[27]

This interpretation subjects underwriters to the risk that an inactive URL reference in an official statement may be automatically converted to an active hyperlink, with the result that referenced documents must also be provided to potential customers on request. If a customer has requested physical offering documents, the underwriter might be obligated to print and provide copies of the referenced web page. At the same time, the interpretation suggests that a municipal issuer participating in a primary offering may provide to investors, and impliedly urge them to rely on, information that is incorporated by reference in (but not connected by an active link or "hyperlink" to) the official statement, but, if it does, an underwriter need not review the referenced information, contract to receive it in sufficient quantity, or provide it to potential customers on request in order to comply with Rule 15c2-12.

We suggest that the Commission clarify that preliminary official statements and final official statements include (and are limited to) the document or documents prepared for dissemination (physically or electronically) to investors in connection with the offering together with any other documents of the issuer or an obligated person expressly incorporated by reference into the document or documents prepared for that purpose. Under this formulation, mere inclusion of an issuer's or obligated person's web site URL, or the URL for EMMA (where information and notices that it has provided to the MSRB are posted), in a preliminary or final official statement would not be treated as an incorporation by reference (whether or not the electronic copy includes an active hyperlink) if the official statement fails to expressly incorporate the document by reference (and, ideally, it would make clear that the referenced or linked information is not intended to be part of the official statement).[28] This interpretation

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[27] Use of Electronic Media, Securities Act Release No. 33-7856 (April 28, 2000).

[28] This portion of the proposed clarification would differ from the Commission's prior interpretation, under which a web site page is deemed incorporated into the prospectus if referenced by an active hyperlink. Since an investor can type a URL into his or her web browser to access a referenced site nearly as easily as clicking on a hyperlink, we believe that whether a referenced document is part of a preliminary or final official statement should be determined by clearly stated intent, rather than by the technical manner in which a URL is provided and may be accessed, especially given the prevailing use of third-party services beyond the issuer's control to make electronic versions of

would exclude investor road show presentations, unless they are incorporated by reference into the preliminary or final official statement,[29] and would also exclude third-party credit enhancer web pages, even if incorporated by reference in the official statement.[30] Finally, when providing these clarifications, the Commission should remind issuers and underwriters that, so long as web site or road show information is readily accessible to investors, issuers have a duty under the antifraud provisions of the federal securities laws to avoid material misstatements and omissions in the information, and underwriters have a duty to review the road show presentation, and should also review web site information, to determine whether either indicates that a key representation made to investors in the preliminary or final official statement or road show information is untrue or misleading.[31]

Summary. Under the proposed clarifications, to comply with Rule 15c2-12 underwriters would be obligated to review and provide website or investor road show content to all potential customers only if the content were expressly incorporated by reference into the issuer's official

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offering documents available to investors (and that may convert an inactive link to a hyperlink without issuer consent or an underwriter's knowledge). The proposed interpretation would also avoid any need to provide annual information and material event notices posted on EMMA (which may be dated and omit discussions of risk factors), if an official statement's reference to emma.msrb.org is inadvertently included as an active hyperlink. Finally, the proposed interpretation would provide a bright line that is easily applied by underwriters, which is appropriate for a technical rule like Rule 15c2-12.

[29] Road show presentations customarily select and repackage information included in a preliminary official statement, so there would be no purpose served by requiring underwriters to provide copies of the road show presentation to potential customers on request. To the contrary, providing the presentation to investors as a separate document would run the risk that it could be passed on to other prospective investors without the preliminary or final official statement, thus failing to apprise investors of risks associated with the investment that are described in the official statement but not in the presentation. In addition, underwriters might be obligated to provide the road show presentation to potential customers even after the final official statement is available, even though the road show presentation might be dated because it fails to reflect pricing information or other subsequent developments.

[30] This exclusion is consistent with the exclusion of bond insurers and providers of letters of credit and liquidity providers from the definition of "obligated person." The Commission added the exclusion in the 1994 Adopting Release because it understood that information concerning such parties would be freely accessible from the parties directly. Consequently, potential customers need not rely on underwriters for access to such information, so Rule 15c2-12 need not require that underwriters provide it to them on request.

[31] As the Commission stated in its 2000 release:

> Municipal securities issuers are reminded that, whether or not the offering of their securities is exempt from Rule 15c2-12, the anti-fraud provisions of the federal securities laws apply to their official statements and other disclosures.

Use of Electronic Media, Securities Act Release No. 33-7856 (April 28, 2000). As the Commission has also noted, different principles apply when determining whether an issuer has responsibility for referenced information under the antifraud principles of the Exchange Act as opposed to whether the information is part of an offering document for purposes of the Securities Act. For antifraud purposes, the inquiry is whether the issuer has "involved itself in the preparation of the information" or "explicitly or implicitly endorsed or approved the information." Commission Guidance on the Use of Company Websites, Exchange Act Release No. 34-58288 (August 1, 2008). The issuer would normally be involved in the preparation of information posted on its web site or provided to the MSRB and, if so, would have responsibility for the information under the antifraud provisions, even if the information were not part of the preliminary or final official statement for purposes of Rule 15c2-12.

statement.[32] We believe this result would be a sensible application of Rule 15c2-12 and would protect investors without unnecessarily burdening underwriters and increasing issuance expenses.

Q5. What are the appropriate uses and limitations of disclaimers in official statements?

Although disclaimers are widely used in official statements prepared in connection with primary offerings of municipal securities, the Commission has not directly addressed or provided advice with respect to their use by issuers, conduit borrowers, trustees, or credit enhancement providers. We suggest that the Commission clarify that official statement disclaimers, in certain instances, may be used to appropriately limit the disclaiming party's liability, provided that (1) the disclaimer is specific and appropriately tailored as to the information disclaimed, (2) the disclaiming party does not know, and is not reckless in not knowing, that the statements disclaimed are materially false or misleading, and (3) the disclaimer does not materially mislead investors as to the disclaiming party's responsibilities under the federal securities laws.

Disclaimers. In 1951, an Opinion of the General Counsel addressed the use of "hedge clauses"[33] by brokers, dealers, investment advisers and others. While the opinion primarily addressed the question as to whether the result of using a disclaimer legend created in an investor's mind a belief that he has given up his legal rights and is foreclosed from a remedy under common law or under federal securities statutes, it also found as follows:

> A legend in common use states in effect that the information is obtained from specified sources and is believed to be reliable but that its accuracy is not guaranteed. Assuming the truth of the representations as to the source of the information and the belief that it is reliable, it is my opinion that the mere use of this legend in connection with a communication supplying information is not objectionable.[34]

The Commission has interpreted Section 14 of the Securities Act and Section 29(a) of the Exchange Act to limit the effectiveness of disclaimers of liabilities in offering documents because, in the Commission's view, such disclaimers would violate the primary public purpose of the antifraud provisions.[35] Nevertheless, as long as a disclaimer is not a general disclaimer of

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[32] The Commission could include in its interpretation an example of language that would avoid an implied incorporation by reference, for example:

> Annual reports and material event notices provided by the issuer to the MSRB may be accessed by means of the MSRB's Electronic Municipal Market Access (EMMA) System at emm.msrb.org. No previously filed report or notice is part of this Official Statement or should be relied upon in deciding whether to invest in the Bonds.

[33] "While the language of these hedge clauses varies considerably, in substance they state generally that the information furnished is obtained from sources believed to be reliable but that no assurance can be given as to its accuracy. Occasionally language is added to the effect that no liability is assumed with respect to such information." *Opinion of General Counsel, Relating to Use of "Hedge-Clauses" by Brokers, Dealers, Investment Advisers, and Others*, Securities Exchange Act Release No. 4593 (1951).

[34] *Id.*

[35] *Disclosure Roles of Counsel*, at 212.

liability, many counsel have encouraged the use of disclaimers in municipal securities official statements,[36] in part due to analogies drawn from Section 11 of the Securities Act in establishing defenses to liability under Section 10(b) of the Exchange Act for "expertised" portions of registration statements and in part to avoid common law liability for implied warranties.

"Expertised" Portions of Official Statements. Section 11(b) of the Securities Act affords underwriters and parties, other than the issuer, a defense with respect to those portions of a registration statement used in reliance on the authority of an expert and does not impose affirmative investigatory responsibilities in those circumstances. Parties are required to prove only that they had no reasonable ground to believe and did not believe that the statements in those portions of the registration statement were materially untrue or incomplete. By analogy, in many instances, participants in a municipal securities offering similarly will rely upon experts and will disclaim responsibility for that section of the official statement. This reliance and the efficacy of the disclaimer, however, has to be reasonable.[37]

1994 Interpretive Release. The Commission did not address disclaimers by issuers or other persons in the 1994 Interpretive Release, but it did address disclaimers by underwriters. In the 1994 Interpretive Release, the Commission stated that, in order to meet their obligations under the antifraud provisions of the federal securities laws, underwriters have a duty "to have a reasonable basis for recommending any municipal securities, and their responsibility, in fulfilling that obligation, to review in a professional manner the accuracy of statements made in connection with the offering." In footnote 103 to the 1994 Interpretive Release, the Commission further noted that "disclaimers by underwriters of responsibility for the information in official statements provided by the issuer or other parties, without further clarification regarding the underwriter's belief as to accuracy, and the basis therefor, are misleading and should not be included in official statements."[38]

2000 Electronic Media and the 2008 Use of Company Website Releases. In 2000, the Commission released an interpretation on the use of electronic media.[39] This guidance was aimed at issuers of all types, including municipal securities issuers, and in particular addressed the issue of embedded hyperlinks and other references to web sites. The Commission stated that

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[36] *Disclosure Roles of Counsel* provides an excellent discussion of the reasons why disclaimers are prevalent in official statements at 211-14.

[37] Participants in a municipal securities offering should review the reports and materials and discuss them with the responsible experts. After these discussions, the parties should consider whether they know, or have reason to know, that the "expertised" information is materially misleading. The parties should also inquire about the qualifications and realm of expertise of the experts and should obtain, if possible, their written consent to the references to them and to the use of their report. *Disclosure Roles of Counsel*, at 209; Robert A. Fippinger, The Securities Law of Public Finance §§ 7:4 *et seq*. (2d ed. 2006).

[38] In response to the 1994 Interpretive Release, The Bond Market Association recommended that underwriters use the following disclaimer: "The Underwriter has reviewed the information in this Official Statement in accordance with, and as a part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriter does not guarantee the accuracy or completeness of such information." Many official statements for negotiated underwritings contain this disclaimer verbatim. Many official statements also contain paraphrases of the 1951 Opinion of the General Counsel.

[39] SEC Interpretation: Use of Electronic Media, SEC Release Nos. 33-7856 (April 28, 2000).

"when an issuer embeds a hyperlink to a web site within the document, the issuer should always be deemed to be adopting the hyperlinked information."[40] In order to eliminate any confusion about whether the issuer has adopted information that is referenced but not hyperlinked, the Commission suggested that the issuer should ensure "that access to the information is preceded or accompanied by a clear and prominent statement from the issuer disclaiming responsibility for, or endorsement of, the information."[41] As summarized in *Disclosure Roles of Counsel*,

> In its Electronic Media Release, the SEC stated that an issuer [of registered securities] may avoid responsibility from material misstatements in and omissions from third-party statements referenced in its disclosure material (other than registration statements filed with the SEC), if the issuer is not involved in the preparation of the statement and has not adopted it by implication. However, in the SEC's view, a disclaimer of responsibility would be ineffective if the third-party statement has effectively been adopted or if the issuer knew or was reckless in not knowing that the statement is materially false or misleading.[42]

This Commission viewpoint was reiterated in its 2008 release, *Commission Guidance on the Use of Company Web Sites*, in which it paraphrased footnote 61 from the 2000 Electronic Media Release:

> With regard to the use of disclaimers generally, as we noted in the 2000 Electronics Release, we do not view a disclaimer alone as sufficient to insulate an issuer from responsibility for information that it makes available to investors whether through a hyperlink or otherwise. Accordingly, a company would not be shielded from antifraud liability for hyperlinking to information it knows, or is reckless in not knowing, is materially false or misleading. This would be the case even where the company uses a disclaimer and/or other features designed to indicate that it has not adopted the false or misleading information to which it has provided the hyperlink. Our concern is that an alternative approach could result in unscrupulous companies using disclaimers as shields from liability for making false or misleading statements. We again remind issuers that specific disclaimers of anti-fraud liability are contrary to the policies underpinning the federal securities laws.[43]

It is clear that the Commission recognizes the appropriateness of disclaimers in municipal securities official statements, albeit in the limited circumstances where the disclaimed information is hyperlinked from third-party websites. Given the widespread and often appropriate usage of disclaimers in official statements, we believe that the Commission should

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[40] *Id.* at n. 57. See below, "Appropriate Circumstances."

[41] *Id.* at n. 59. For further discussion of appropriate ways to handle hyperlinked materials, see the discussion above under "Q4. What documents are included in the definitions of "preliminary official statement" and "official statement" for purposes of Rule 15c2-12, and must they all be provided to potential customers on request?"

[42] *Disclosure Roles of Counsel*, at 211-12.

[43] Commission Guidance on the Use of Company Websites, SEC Release No. 34-58228 (August 1, 2008), at n. 86.

recognize and address the use of disclaimers in other circumstances so as to provide greater guidance to issuers in the preparation of their official statements.[44]

Appropriate Circumstances. *Disclosure Roles of Counsel* provides two circumstances in which disclaimers are appropriate:

- To avoid implied representations that might otherwise be actionable under contract law imposing liability for misrepresentations, even if not intentional or reckless (which is the standard for securities law claims).[45]

- To avoid any implied adoption of third-party information that is passed on to investors (and therefore to prevent "justifiable reliance", which is an element of a private right of action under Section 10(b) of the Exchange Act, on the representation as a statement made by the disclaiming party).[46] Although underwriters have a duty to check on key representations, it is not clear that issuers have a similar implied duty to check on third-party representations unless the issuer (a) "adopts" the representations as its own, (b) implies that it has checked the representations or (c) knows or has a reason to suspect that the representations are materially inaccurate or misleading.

Of these two circumstances, it is clear that the second circumstance, dealing with third-party information, is most troubling to issuers. For example, if a local governmental entity's employees participate in a state retirement plan, the local governmental entity's official statement will necessarily rely on information provided to it by the state or the state pension plan. Similarly, a top ten employer list included in an official statement may rely on information provided by a local chamber of commerce. Credit enhancers typically prescribe "approved" disclosure about themselves from which issuers are not permitted to deviate. While there is a difference in the degree of materiality of this information, there is no difference in the degree of reliance on information supplied by a third party.

We believe that the use of disclaimers, coupled with source references, will clearly identify those portions of an official statement that are under the direct control of the issuer (such as its financial statements), and those portions for which it must rely on third parties (such as population and other demographic information).

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[44] We note that this year marks the 10th anniversary of the request by Jeffrey S. Green, the General Counsel of The Port Authority of New York & New Jersey, at the Second Annual Municipal Market Roundtable in 2000, "I think the SEC needs to permit reasonable disclaimer language so that you can clearly segregate what information is market-based information and what information is marketing information for the municipality."

[45] For example: "This Official Statement does not constitute a contract between or among the Issuer, the Underwriter and any purchaser of the Bonds." *Disclosure Roles of Counsel*, at 214, n. 42.

[46] For example: "The information herein concerning the Borrower has been provided by the Borrower, and the Issuer makes no representation concerning the accuracy of completeness of such information." *Disclosure Roles of Counsel*, at 214, n. 43. Also: "The Issuer has not made any investigation into the accuracy or completeness of the statements concerning the Borrower included in this Official Statement." *Disclosure Roles of Counsel*, at 214, n. 44.

Summary. We suggest that the Commission clarify that official statement disclaimers may be used to appropriately limit the disclaiming party's liability with respect to information provided by third parties, provided that the disclaimer is specific and appropriately tailored as to the information disclaimed, and the disclaiming party does not know, and is not reckless in not knowing, that the statements disclaimed are materially false or misleading.

OTHER ISSUES OF INTEREST

In addition to the issues described in more detail above, NABL also believes the following issues can benefit from SEC clarification:

Disclosure Regarding MD&A. Management's discussion and analysis ("MD&A") provides a useful narrative in corporate disclosure of recent developments for a reporting company[47] and may serve to do the same in the municipal market as well. For municipal issuers following accounting principles set by the Governmental Accounting Standards Board, MD&A became a component of many issuer financial reports following implementation of GASB Statement No. 34 in the early 2000s. Not all municipal issuers or conduit borrowers follow GASB (either because, like many nonprofits, they follow principles set by the Financial Accounting Standards Board or because they follow some sort of state-prescribed principles of accounting), and those that do may vary in quality.[48] In light of the disparities between corporate and municipal sources of revenues and expenses, competition, and other factors affecting financial results of operations and condition, we suggest that the Commission apprise municipal securities issuers of the circumstances (through examples) in which MD&A is important to good disclosure and the types of information that it should address.[49]

Disclosure of General Financial Market Risk or General Industry Risk. A municipal issuer should be able to assume that a potential investor understands the nature of general financial market risk factors, as well as industry-wide risk factors. With respect to registered offerings, the Commission has directed that "risk factor" disclosure focus simply on significant, issuer-specific risks that are concisely stated.[50] In light of the Commission's guidance for registered offerings, we suggest that the Commission offer guidance with respect to a municipal

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[47] Item 303 of Regulation S-K prescribes the MD&A content in securities filings made by companies whose securities are required to be registered under the Securities Act and the Exchange Act.

[48] See, for example, Disclosure Quality of Management Discussion and Analysis (MD&A): Evidence from Large Florida Cities, Municipal Finance Journal Vol. 30, No. 3, Fall 2009.

[49] The Commission could consider questions like the following: (1) What core elements of MD&A, if any, are of particular prominence in light of the antifraud provisions of federal securities law? (2) Are there instances in which MD&A discussion is a requisite under the antifraud provisions? (3) Does a well prepared MD&A section provide certain common topics? (4) What are important considerations for MD&A relating to a general obligation credit secured by a promise to levy adequate taxes to pay debt service?

[50] Item 503(c) of Regulation S-K provides as follows: "Where appropriate, provide under the caption "Risk Factors" a discussion of the most significant factors that make the offering speculative or risky. This discussion must be concise and organized logically. Do not present risks that could apply to any issuer or any offering. Explain how the risk affects the issuer or the securities being offered. Set forth each risk factor under a subcaption that adequately describes the risk. . . ."

issuer's responsibility for the disclosure of general financial market risk or general industry risk regarding the securities being offered.

Contents of Disclosure in Final Official Statement. We suggest that the Commission confirm statements from the 1994 Adopting Release that "[t]he definition [of final official statement] does not set its own form and content requirements on the financial information and operating data to be included.... Instead it provides the flexibility that many commenters asserted is necessary in determining the content and scope of the disclosed financial information and operating data, given the diversity among types of issuers, types of issues, and sources of repayment."

Prior NABL Comments. For suggested clarifications regarding disclosure in offerings of variable rate demand securities backed by letters of credit and the ability of brokers and dealers to underwrite municipal offerings by issuers that have violated prior continuing disclosure undertakings, see NABL's comment letter on the 2009 Proposing Release.[51]

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[51] NABL's comment letter can be found on the Commission's web site (www.sec.gov/comments/s7-15-09/s71509-28.pdf).

GLOSSARY OF TERMS USED IN STATEMENT

Certain capitalized terms used frequently in this statement are defined in this section of the statement.

"1988 Proposing Release" means Securities Exchange Act Release No. 34-26100 (September 22, 1988).

"1989 Adopting Release" means Securities Exchange Act Release No. 34-26985 (June 28, 1989).

"1994 Interpretive Release" means Securities Act Release No. 33-7049 (March 9, 1994).

"1994 Proposing Release" means Securities Exchange Act Release No. 34-33742 (March 9, 1994).

"1994 Adopting Release" means Securities Exchange Act Release No. 34-34961 (November 10, 1994).

"2009 Proposing Release" means Securities Exchange Act Release No. 34-60332 (July 17, 2009).

"Commission" or **"SEC"** means the United States Securities and Exchange Commission.

"*Disclosure Roles of Counsel*" means *Disclosure Roles of Counsel in State and Local Government Securities Offerings* (3rd Edition 2009).

"EMMA" means the MSRB's Electronic Municipal Market Access system, as provided by Rule 15c2-12.

"Exchange Act" means the Securities Exchange Act of 1934, as amended (as codified at 15 USC §§ 78a *et seq.*).

"MSRB" means the Municipal Securities Rulemaking Board.

"Orange County Report" means the Report on Investigation in the Matter of County of Orange, Cal., SEC Rel. No. 34-36761 (Jan. 24, 1996).

"Rule 15c2-12" or the **"Rule"** means 17 CFR § 240.15c2-12.

"Rule 10b-5" means 17 CFR § 240.10b-5.

"Securities Act" means the Securities Act of 1933, as amended (as codified at 15 USC §§ 77a *et seq.*).

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APPENDIX B

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APPENDIX C

CHARACTERISTICS AND IMPORTANCE OF DEMAND SECURITIES[20]

1. General Characteristics. Demand securities are nominally long-term debt securities, but with two distinguishing characteristics that allow them to be priced as if they were short-term debt securities: (a) they must be repurchased on demand of the investor (generally on one week's or same-day notice) for a price equal to their principal amount plus accrued interest, and (b) their interest rate is reset frequently (generally daily or weekly) to maintain a market value equal to the repurchase price. To avoid retirement of the demand securities when tendered for repurchase on demand, the issuer or conduit borrower engages a broker-dealer as "remarketing agent" to use its best efforts to sell the tendered demand securities and to reset the interest rate on the demand securities. Except in very unusual circumstances, remarketing agents are able to resell all tendered demand securities to other investors or on occasion to purchase them as inventory.

2. Credit/Liquidity Enhancement. Most demand securities are purchased and held by tax-exempt money market mutual funds (MMFs). To qualify for purchase by MMFs, demand securities must have high long-term and short-term ratings and must satisfy the credit requirements of the MMF. To attain the requisite ratings and credit quality, most demand securities are supported by external credit and/or liquidity facilities.

3. Importance of Market for Demand Securities. Demand securities are an important part of the municipal securities market, because they enable issuers to access short-term interest rates without either repeating the issuance expenses associated with new issues or the higher interest rates associated with tax-exempt debt held by banks. Many issuers desire to issue a portion of their debt securities at short-term interest rates because those rates are generally lower than long-term rates, and because they hold a sufficient amount of short-term investments to hedge against increases in short-term interest rates.

a. **Avoidance of Repeated Issuance Costs.** Without access to a viable demand securities market, issuers could access short-term rates only by issuing and continuously rolling commercial paper or other short-term securities. Many issuers must follow expensive and time-consuming procedures to issue debt in compliance with state law. In addition, they must perform additional procedures to assure that each new issue of debt securities is tax-exempt. If issuers were required to issue back-to-back short-term securities (rather than demand securities) to obtain long-term financing at short-term interest rates, they would be forced to repeat these procedures periodically, thus increasing the effective cost of their borrowings compared to those associated with demand securities.

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[20] For additional background on demand securities, see (a) the September 23, 2009 comment letter that NABL submitted in connection with the amendments to Rule 15c2-12 that became effective on December 1, 2010 (www.nabl.org/library/documents/1113) and (b) J. Hobson Presley, "The Disclosure Dilemma for VRDOs Secured by a Letter of Credit", *The Bond Lawyer* (Summer 2011) (www.nabl.org/uploads/cms/documents/bond_lawyer_summer_2011.pdf).

b. **Avoidance of High Bank Rates.** Many issuers who wish to borrow at short-term interest rates do not have the credit (or cannot make the disclosure of their credit) required to access municipal securities markets directly, but do have sufficient credit to secure a bank loan. However, if banks were to make and hold tax-exempt loans to municipal issuers, in most circumstances they would lose the interest expense deduction associated with a ratable amount of their deposit accounts, which would effectively decrease their after-tax yield compared to the yield enjoyed by a non-bank investor. As a result, issuers who cannot directly access the short-term municipal securities market on their own credit also cannot borrow at equivalent rates from banks. They can and do, however, efficiently access the short-term market by selling demand securities to non-bank investors and using their bank's letter of credit to provide for payment of the demand securities.

c. **Importance of Demand Securities to MMFs.** Municipal issuers do not issue enough tax-exempt short-term securities, and their issuances are too seasonal and long in duration, to supply tax-exempt MMFs with an adequate supply of eligible investments. MMFs therefore depend on demand securities to complete and manage their portfolios. If the market for demand securities were to become inefficient and issuers were forced to issue long-term securities in their place, the supply of eligible investments to tax-exempt MMFs could become inadequate.

4. Importance of Liquidity to Demand Security Market. The efficiency of the market for demand securities is largely dependent on the ability of remarketing agents to efficiently place tendered demand securities with other investors, or to be confident enough in their ability to do so to be willing to buy tendered demand securities for their own inventory if they are not able to remarket tendered demand securities on the day of purchase. If, due to regulatory uncertainty or unwarranted regulatory burdens, remarketing agents are not able to readily remarketed tendered demand securities and are unwilling to purchase them for their own inventory, then demand securities would be regularly put to banks under letters of credit or liquidity facilities. Banks charge a substantially higher interest rate to hold demand securities purchased under a letter of credit or liquidity facility. If demand securities are regularly put to and held by banks, issuer borrowing rates would increase. In addition, if banks believed that they would be more likely to perform under their commitments to purchase tendered bonds, it is likely that they would charge more for their commitments under letters of credit and liquidity facilities. These resulting increased borrowing costs in turn would likely dissuade some issuers from issuing demand securities. In addition, any such increased risk of bank purchases of demand securities would add stress to the banking system. Consequently, the Commission should be careful not to unnecessarily regulate or otherwise interfere with the ability of remarketing agents to remarket demand securities.