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Reports and Resources

Disclosing Risk Factors in Municipal Securities Offerings

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INTRODUCTION

This paper explores legal and practical considerations in (a) identifying and disclosing risk factors in primary offerings of municipal securities and, in some circumstances, related secondary market disclosure and (b) developing policies and procedures for disclosing risk factors. The goal of the paper is to assist members of the National Association of Bond Lawyers when they advise municipal securities issuers[1] and underwriters.

This paper first discusses the legal framework involved when analyzing risk factor disclosure issues, then outlines possible procedures for identifying, evaluating, and disclosing risk factors generally. Finally, in an appendix, the paper offers considerations related to some common risk factors.

This paper is not intended to provide an exhaustive treatment of risk factor disclosure or risk factor examples, and it should not be read to make any suggestion of, or establish any presumption as to, best practices in connection with municipal securities disclosure.

1. LEGAL REQUIREMENTS AND CONSIDERATIONS

Material facts must be disclosed by issuers in primary offerings[2] of municipal securities to comply with the antifraud provisions of federal and state securities laws. Depending on the offering, material facts may include material risk factors. In advising issuers, counsel can look to legal precedent addressing the antifraud provisions, as well as the rules applicable to registered securities offerings, for guidance in deciding if, when, and how risk factors should be disclosed in a primary offering.[3] Adequate disclosure of risk factors can reduce an issuer's exposure to monetary damages and governmental enforcement actions alleging violations of the antifraud provisions.

a. What's the Risk? Why Risk Factors Are Included in Offering Documents

(i) Antifraud Provisions, Generally

All issuers, including municipal securities issuers, must comply with the antifraud provisions of the federal and state securities laws when they make disclosures in primary offerings or when they make other public statements that are accessible to, and likely to be relied upon by,

[1] This paper uses the term "issuer" to refer both to the actual issuer of municipal securities and other entities that are material to an offering and about which financial or operating data must be disclosed in an offering document that complies with SEC Rule 15c2-12(f)(3), 17 C.F.R. § 240.15c2-12 (the "*Rule*"), including borrowers in conduit offerings and other "obligated persons" referred to in that Rule. In most cases, the principles discussed in this paper also apply to direct offerings of securities by non-profit entities entitled to the exemption from registration afforded by Section 3(a)(4) of the Securities Act of 1933 (referred to herein as the "*Securities Act*"), 15 U.S.C. § 77c(a)(4) (2018).

[2] As used herein "primary offerings" refers to offers to sell securities to the public by or on behalf of the issuer, and "secondary market" refers to sales of securities outside of a primary offering that do not involve the issuer. For a discussion of what constitutes a primary offering, see "Transmittal of NABL's Suggestions for Interpretive Guidance Update, May 14, 2010" and "Additional NABL Comments for Interpretive Guidance Update, September 2, 2011."

[3] To help manage legal risks or for other reasons, issuers may choose to disclose facts relevant to investment risks even when not required by law, so long as the inclusion of those facts would not mislead a reasonable investor.

investors and the trading markets, including continuing disclosures. Whether such statements are made within offering documents or are accessible elsewhere, they may not misstate or make any misleading omission of a material fact. In addition, in primary offerings and other securities transactions by issuers, issuer statements may not operate as "a fraud or deceit upon the purchaser." The federal laws setting forth these antifraud provisions are described below.

In primary offerings of municipal securities, issuers may not (a) employ any "device, scheme, or artifice to defraud," (b) obtain proceeds by means of "any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading," or (c) engage in any transaction which operates as a "fraud or deceit" upon the purchaser.[4] These provisions require that issuers disclose risk factors, if material, in primary offerings when other disclosed facts and readily available information about the issuer or the offering do not adequately apprise investors of material investment risks.

Whether or not involved in a primary offering, an issuer of municipal securities may not employ, in connection with the purchase or sale of any security, any manipulative or deceptive device or contrivance that contravenes a rule promulgated by the U.S. Securities and Exchange Commission ("SEC") as necessary or appropriate in the public interest or for the protection of investors.[5] Under SEC Rule 10b-5 ("Rule 10b-5"),[6] promulgated under the Securities Exchange Act of 1934,[7] an issuer may not engage in a practice barred by clause (a) or (c) of the preceding paragraph or make a statement or omission described in clause (b) of that paragraph, even if not made in a securities transaction involving the issuer.[8] As interpreted by case law, if an issuer statement is accessible to and likely to be relied upon by investors and the trading markets, it is made in connection with the purchase or sale of securities.[9]

Since municipal securities are exempt securities under federal securities laws, issuers have no statutory duty to affirmatively make statements that may be relied upon by investors and the trading markets. However, if and when they do speak, they may not mislead investors by omitting material facts.[10] Statements made by issuers in primary offerings clearly are statements that may be relied upon by investors and the trading markets. In addition, issuers regularly make statements outside primary offerings that are likely to be relied upon by investors, including filings made on the Municipal Securities Rulemaking Board's ("MSRB") Electronic Municipal Market Access system ("EMMA") and some issuer website postings.

The current SEC view, especially in the enforcement context, is that such statements (like those in offering documents) are subject to the Rule 10b-5 antifraud provisions. Nevertheless, in light of the differing circumstances in which primary offering and secondary market statements

[4] Securities Act § 17(a), 15 U.S.C. § 77q(a).
[5] Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b).
[6] 17 C.F.R. § 240.10b-5 (2023).
[7] 15 U.S.C. § 78a *et seq.,* referred to herein as the "*Exchange Act.*"
[8] Rule 10b-5, 17 C.F.R. § 240.10b-5.
[9] *See* Fredric A. Weber, Notes from the Editor (on "Connection" and "Circumstances"), THE BOND LAWYER, Fall 2019, at 3-5 discussing and summarizing case law with respect to whether statements were made "in connection with" the purchase and sale of a security.
[10] *See In re Boston Sci. Corp. Sec. Litig*., 686 F.3d 21, 27-28 (1st Cir. 2012).

are made, risk factors generally may be omitted from secondary market statements without misleading investors, absent special circumstances, as discussed below.[11]

Issuers can be liable to investors and subject to SEC enforcement actions for violating Rule 10b-5 if their conduct is intentional or reckless.[12] In addition, issuers in primary offerings or other direct transactions with investors can be subject to SEC enforcement actions for violating Section 17(a)(2) or (3) of the Securities Act, if their conduct is negligent or worse.[13] Under the Securities Act, an antifraud action can be based on a fraudulent or deceitful transaction in addition to a misstatement or misleading omission of a material fact.[14]

(ii) Facts

Misleading omissions are actionable under Rule 10b-5 only if the omissions are of material facts. Material facts must be disclosed if their omission would mislead a reasonable investor as to the risk associated with an investment.

"Fact" is not defined by the Exchange Act or SEC rules, nor is it a term of art. Consequently, it should be construed in accordance with common usage, the legislative history of Section 17(a)(2) of the Securities Act and the regulatory history of Rule 10b-5. In common usage, a "fact" is "something that has actual existence," "an actual occurrence," or "a piece of information presented as having objective reality."[15]

Similarly, "factor" is not defined by SEC rules, nor is it a term of art, so it, too, should be construed in accordance with common usage. In common usage, a "factor" is "something that helps produce or influence a result; one of the things that cause something to happen."[16] "Risk factors" are therefore "facts" that indicate or result in "risks" or may cause a particular "risk" to be considered material with respect to that credit.

As a technical matter, risks themselves, as opposed to the facts that give rise to them (i.e., risk factors), are not "facts," so need not be independently disclosed to comply with the antifraud provisions. "Risk factors," on the other hand, like other facts, may not be omitted from statements relied upon by investors, if material and if the omission would make the statements misleading. Consequently, disclosure of generic risks by themselves is neither adequate nor required[17] in statements made to investors, but disclosure of material risk factors, i.e., facts indicating risk of a certain type or magnitude, is required if their omission would make the statements misleading. For example, the tendency of a geographic area to experience severe

[11] This conclusion is in contrast to requirements for annual reports required to be filed on Form 10-K by corporate issuers. *See infra* Part 1.b.i.
[12] *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976); *Aaron v. SEC*, 446 U.S. 680 (1980); *Sundstrand Corp. v. Sun Chemical Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977) ("Reckless conduct may be defined as 'highly unreasonable [conduct], involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care' which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it.").
[13] *See Aaron*, 446 U.S. at 700–02.
[14] Securities Act § 17(a)(3), 15 U.S.C. § 77q(a)(3) (2018).
[15] *Fact*, MERRIAM-WEBSTER, https://www.merriam-webster.com/dictionary/fact (last visited Feb. 24, 2021).
[16] *Factor*, MERRIAM-WEBSTER, https://www.merriamwebster.com/dictionary/factor (last visited Feb. 24, 2021).
[17] Disclosure of risks may be required to explain the consequences of material risk factors.

flooding may be a factor that would make the generic risk of casualty losses from natural disasters material.

(iii) Materiality

A fact is material "if there is a substantial likelihood that a reasonable [investor] would consider it important,"[18] and, in the case of an omitted fact, "if there is a substantial likelihood that the information would have been viewed by the reasonable investor as having significantly altered the total mix of information made available."[19] In determining whether a risk factor is material, the indicated probability that an event will occur must be compared to the anticipated magnitude of the event.[20]

Facts that are common knowledge to a reasonable investor need not be disclosed to investors, because disclosing such facts would not significantly alter the total mix of information available to them.[21] For example, reasonable investors should know that a state economy could encounter a recession, or that an earthquake, forest fire, hurricane, tornado, or other force of nature could devastate a community. Similarly, an issuer is not required to disclose factors indicating a generic risk, unless the factors indicate that the risk is materially more likely to occur to or have a greater impact on the issuer (or issuers in the same sector) than to, or on, issuers generally.

Facts that indicate an issuer's greater or lesser vulnerability to risks, including commonly known risks, may need to be disclosed, if material and required to avoid a misleading impression.[22] See "How to Assess and Disclose Risk Factors—Practical Considerations—Developing Risk Factor Disclosure—Identifying the Risks and Risk Factors" below for additional discussion.

(iv) Misleading Omissions "In Light of the Circumstances"

An omission of a material risk factor from an offering document or other statement that is subject to the antifraud provisions (e.g., an EMMA filing) is actionable only if the omission makes the statement misleading in light of the circumstances under which it is made. In the circumstances under which statements are made in a primary offering, it is likely that the omission of a material risk factor would be misleading.

Offering documents typically include several years of the issuer's comparative financial and operating data and invite investors to purchase the issuer's securities at a specified price. Investors infer an issuer's financial prospects, including future financial performance, from this data. The disclosure of comparative historical data, therefore, may be interpreted by investors to

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[18] *TSC Industries, Inc. v. Northway*, Inc., 426 U.S. 438, 449 (1976).
[19] *See Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 38 (2011); *Basic, Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988).
[20] *Basic, Inc.*, 485 U.S. at 231–32; SEC, Comm'n Statement and Guidance on Pub. Co. Cybersecurity Disclosures, Securities Act Release No. 10459, Exchange Act Release No. 82746, 83 Fed. Reg. 8166 (Feb. 26, 2018).
[21] *See, e.g.*, *In re Donald J. Trump Casino Sec. Litig. – Taj Mahal Litig.*, 7 F.3d 357, 377 (3d Cir. 1993) (omission of economic downturn in Northeast U.S. was not material, because known to investors); *Rubinstein v. Collins*, 20 F.3d 160, 168 n.30 (5th Cir. 1994) ("General economic information, such as that the mineral exploration business is inherently risky, need not be disclosed as such information is already included in the 'total mix of information.'").
[22] *See, e.g.*, *Rubinstein*, 20 F.3d at 170 (an issuer must disclose "material, firm-specific adverse facts that affect the validity or plausibility of" a disclosed prediction, not mere generic risk factors).

imply future results. Investors may assume, and the data may imply, that the trends indicated by the comparative data will continue unless otherwise stated. In these circumstances, if a material risk factor relating to such data were omitted, the offering document would imply that the securities are more valuable than is the case and worth the initial offering price. Consequently, in light of the circumstances in which offering document statements are made, the omission of a material risk factor would likely be misleading.[23] In addition, any such omission could result in a fraudulent or deceitful transaction, if the securities are offered at prices that exceed their value. If an omission of a material fact, including a material risk factor, is misleading, deceitful, or fraudulent, the issuer would be exposed to a risk of liability under the antifraud provisions.[24] Consequently, when engaged in primary offerings, issuers should disclose material facts that indicate a material risk to the continued realization of financial and operating results, among other possible material risk factors.

When statements are made outside of a primary offering (e.g., EMMA filings and website postings between offerings), the omission of a material risk factor is not likely to be misleading, absent special circumstances, at least if the statements include cautionary language to avoid implied disclosures, as explained in later sections of this paper.[25]

EMMA filings typically are made to comply with an issuer's contractual continuing disclosure undertakings. The undertakings require issuers to recount historical results and events, but typically do not require that they forecast future prospects or estimate the value of their securities. Similarly, issuers often post historical data on their websites to inform interested parties (e.g., citizens or customers) and may also maintain investor information pages. In either case, when issuers are not engaging in securities transactions with investors (i.e., unlike in primary offerings), neither EMMA filings nor website postings imply that they include all facts material to an investment in the issuer's securities. Accordingly, continuing disclosure filings may omit material risk factors or other material facts without necessarily being misleading to investors (unless inclusion of such material risk factors or other material facts is needed to prevent an express statement in the continuing disclosure filing from being misleading).[26]

To make clear that EMMA filings and website postings do not impliedly disclose all material facts, issuers could include cautionary language to that effect. Like offering documents, annual EMMA filings and issuer website postings often include several years of the issuer's

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[23] *See Silverstrand Inv. v. AMAG Pharm,* 707 F.3d 95,103 (1st Cir. 2013) (omission of a material risk factor from an offering document is actionable if the issuer knew that the risk factor existed and could materially adversely affect the issuer's present or future business expectations).

[24] *See, e.g.*, *State of Illinois*, Securities Act Release No. 9389, Admin. Proc. File No. 3-15237 (Mar. 11, 2013) (in offerings of general obligation bonds, the state omitted to disclose material information regarding the structural underfunding of its pension systems and the resulting risks to its future ability to meet competing obligations; the SEC stated that the materiality of omitted information about Illinois's unfunded pension obligations was so great that it altered the total mix of information available to bond purchasers); *Jo M. Ferguson*, Securities Act Release No. 5523, Admin. Proc. File No. 3-4528 (Aug. 21, 1974) (failure to disclose that two prior feasibility studies were unfavorable).

[25] See Jay Clayton & Rebecca Olsen: *The Importance of Disclosure for our Municipal Markets*, U.S. SEC. & EXCH. COMM'N (May 4, 2020), https://www.sec.gov/news/public-statement/statement-clayton-olsen-2020-05-04 for support that cautionary language included in secondary market disclosures "will reduce legal and other risks."

[26] See *City of Harrisburg, Pa.*, Exchange Act Release No. 69515, Admin. Proc. File No. 3-15316 (May 6, 2013) applying the principle that information will be examined in the context of the "total mix" of information available in the market place.

comparative financial and operating data. Absent cautionary language, in some cases the disclosure of comparative historical data, or the disclosure of a current year budget, may be mistakenly interpreted by investors to imply future results. As in primary offerings, municipal issuers can reduce their exposure to liability by disclosing material risk factors, if any, that could affect implied future results. In disclosure outside of the primary offering context, municipal issuers also may negate unintended implications from comparative historical data about future results by including general cautionary language.[27] For example, when disclosing historical data outside of a primary offering, an issuer can explain that the data are not provided to be, and are not necessarily, indicative of future results and are not provided to inform investors of all material facts, but rather provided to satisfy a contractual obligation (in the case of a contractually mandatory disclosure EMMA filing) or to inform the issuer's citizens or customers (in the case of a website posting). Similarly, when disclosing a current or future year budget, an issuer can explain that it is provided because of its relevance to the issuer's authority to make expenditures, not as a forecast (or indicator) of actual financial performance. Carefully crafted cautionary statements can help clarify the circumstances under which statements are made, so that the omission of material risk factors is not misleading.

The circumstances in which secondary market disclosure is made may differ from the above example if the issuer is engaged in securities transactions with investors (e.g., rolling publicly sold commercial paper, engaging in a tender or exchange offer, or, possibly, remarketing demand securities). In those circumstances, issuers should not omit material risk factors, if any, from secondary market statements on which investors are likely to rely, unless the risk factors are adequately disclosed in a separate document made available to investors. The circumstances in which secondary market statements are made may also differ if they include express forecasts or other forward-looking statements, in which case an issuer may consider the inclusion of appropriate risk factors with such statements. Issuers may, of course, include a discussion of risks and risk factors in continuing disclosure filings, even when not legally required and contrary to prevailing practice.

(v) Bespeaks Caution Doctrine

Issuers may be able to avoid antifraud liability for forward-looking statements if they include risk factors or other discussions of risk that satisfy the judicially-created "bespeaks caution" doctrine. The bespeaks caution doctrine has been endorsed by all federal appeals circuits (except the Court of Appeals for the D.C. Circuit) and by the U.S. Supreme Court in dictum.[28] Its

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[27] Jay Clayton & Rebecca Olsen: *The Importance of Disclosure for our Municipal Markets*, U.S. SEC. & EXCH. COMM'N (May 4, 2020), https://www.sec.gov/news/public-statement/statement-clayton-olsen-2020-05-04.

[28] *Virginia Bankshares, Inc. v. Sandberg,* 501 U.S. 1083 (1991); *Omnicare Inc. v. Laborers Dist. Council Const. Indus. Pension Fund*, 135 S.Ct. 1318 (2015); *In re XM Satellite Radio Holdings Sec. Litig.*, 479 F. Supp. 2d 165 (D. D.C. 2007)*; Romani v. Shearson Lehman Hutton,* 929 F.2d 875 (1st Cir. 1991); *Iowa Pub. Emps.' Ret. Sys. v. Global,* 620 F.3d 137 (2d Cir. 2010); *Luce v. Edelstein*, 802 F.2d 49 (2d Cir. 1986); *In re Donald J. Trump Casino Sec. Litig. – Taj Mahal Litig.*, 7 F.3d 357 (3d Cir. 1993); *Gasner v. Board of Sup'rs of Dinwiddie, VA,* 103 F.3d 351 (4th Cir. 1996); *Rubinstein v. Collins,* 20 F.3d 160 (5th Cir. 1994); *Huddleston v. Herman & MacLean*, 640 F.2d 534 (5th Cir. 1981); *Mayer v. Mylod*, 988 F.2d 635 (6th Cir. 1993); *Harden v. Raffensperger, Hughes & Co., Inc*, 65 F.3d 1392 (7th Cir. 1995); *Moorhead v. Merrill Lynch, Pierce, Fenner & Smith, Inc.,* 949 F.2d 243 (8th Cir. 1991); *In re Worlds of Wonder Sec. Litig.,* 35 F.3d 1407 (9th Cir. 1994); *In re Apple Computer Sec. Litig.,* 886 F.2d 1109 (9th Cir. 1989); *Grossman v. Novell, Inc.,* 120 F.3d 1112 (10th Cir. 1997); *Salzberg v. TM Sterling/Austin Associates, Ltd.,* 45 F.3d 399 (11th Cir. 1995).

application to municipal securities was strengthened by a 2020 statement by SEC officials that supports the effectiveness of cautionary language in avoiding unintended implied statements.[29] Under the bespeaks caution doctrine, forward-looking statements made in good faith are not actionable under the anti-fraud provisions if they are accompanied by meaningful cautionary language like risk factors.[30] The proposition of the bespeaks caution doctrine is that meaningful cautionary statements provide context for projections and other forward-looking statements such that, when all the statements are properly read in the context of all disclosures, the forward-looking statement is not considered misleading.[31]

Although not applicable to municipal securities, the Private Securities Litigation Reform Act created a statutory safe harbor from the antifraud provisions for forward-looking statements that are identified as such and accompanied by "meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement."[32] The legislative safe harbor was based on the judicially created bespeaks caution doctrine and SEC Rule 3b-6.[33] In 2012, the SEC proposed expanding this safe harbor to include municipal securities.[34] In 2020, the SEC's Fixed Income Market Structure Advisory Committee of the SEC recommended the same action.[35] Given the judicially created "bespeaks caution" doctrine, however, cautionary statements can be effective even without such legislation.

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[29] Jay Clayton & Rebecca Olsen: *The Importance of Disclosure for our Municipal Markets*, U.S. SEC. & EXCH. COMM'N (May 4, 2020), https://www.sec.gov/news/public-statement/statement-clayton-olsen-2020-05-04. The SEC Office of Municipal Securities indicated in the context of voluntary disclosures concerning COVID-19 that "[w]e recognize that the issue of liability often is raised when voluntary disclosures—or the expansion of required disclosures—are considered. Nonetheless, each issuer, in many cases in consultation with legal counsel, will have to assess this risk in the context of its particular circumstances." *Id.*

[30] *See, e.g.*, *In re Apple Computer Sec. Litig.,* 886 F.2d 1109, 1113 (9th Cir. 1989) (a forward-looking statement "contains at least three implicit factual assertions: (1) that the statement is genuinely believed, (2) that there is a reasonable basis for that belief, and (3) that the speaker is not aware of any undisclosed facts tending to seriously undermine the accuracy of the statement; a projection or statement of belief may be actionable to the extent that one of these implied factual assertions is inaccurate."). *See also*, Clayton & Olsen, *supra* note 26, at n.13 (citing Robert A. Fippinger's summary of the "bespeaks caution" doctrine with apparent approval); Robert A. Fippinger, The Securities Law of Public Finance, §8:3.4[B] (3d. ed. 2019).

[31] *See, e.g.*, *Rubinstein*, 20 F.3d at 167 ("In essence, predictive statements are just what the name implies: predictions. As such, any optimistic projections contained in such statements are necessarily contingent. Thus, the "bespeaks caution" doctrine has developed to address situations in which optimistic projections are coupled with cautionary language – in particular, relevant specific facts or assumptions affecting the reasonableness of reliance on and the materiality of those projections. To put it another way, the "bespeaks caution" doctrine reflects the unremarkable proposition that statements must be analyzed in context.").

[32] Securities Act § 27A, 15 U.S.C. § 78u-5 (2018).

[33] 17 C.F.R. § 240.3b-6 (2023).

[34] U.S. SEC. & EXCH. COMM'N, REPORT ON THE MUN. SEC. MKT. (2012) https://www.sec.gov/news/studies/2012/munireport073112.pdf.

[35] U.S. SEC. & EXCH. COMM'N, FIXED INCOME MKT. STRUCTURE ADVISORY COMMITTEE, RECOMMENDATION REGARDING TIMELINESS OF FINANCIAL DISCLOSURES IN THE MUNICIPAL SECURITIES MARKET (2020), https://www.sec.gov/spotlight/fixed-income-advisory-committee/fimsac-muni-financial-disclosures-recommendation.pdf.

To be effective, cautionary statements should disclose material risk factors tailored to the issuer's circumstances,[36] rather than merely describing general risks.[37] Cautionary statements will not in and of themselves shield misstatements or omissions of known material facts, whether historical, present or expected.[38] The premise of the bespeaks caution doctrine is that statements, which might otherwise constitute misrepresentations regarding expected future performance due to unknown factors, may be rendered immaterial if cautionary statements, when read in context, adequately disclose risk or otherwise negate implied representations about future prospects. Therefore, cautionary statements may shield statements that might otherwise constitute misrepresentations regarding expected future performance, if they negate implied representations about future prospects or disclose risks so well as to make the omitted facts immaterial.[39]

b. Regulation S-K

The SEC is authorized to prescribe the content of registration statements, prospectuses, and periodic reports for registrants.[40] The SEC adopted Regulation S-K[41] ("Reg. S-K") to establish line item requirements for the content of those documents. Municipal securities are exempt from registration with the SEC and the periodic reporting requirements applicable to registrants, so issuers are not subject to these line item disclosure requirements.[42] Because Reg. S-K is inapplicable to issuers, there is little specific guidance for what facts must be disclosed in offerings of municipal securities, what risk factors are deemed material for municipal securities offerings, or, if material, how they should be disclosed. Consequently, in the absence of other disclosure

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[36] *In re Donald J. Trump Casino Sec. Litig. – Taj Mahal Litig.*, 7 F.3d 357 (3d Cir. 1993).

[37] In at least one circumstance, general descriptions of risk have been determined to be effective. In *Luce v. Edelstein,* 802 F.2d 49 (2d Cir. 1986) the court determined, without providing detail as to the particular facts and disclosures at issue, that alleged misrepresentations as to potential cash and tax benefits of a partnership investment were not actionable, because the offering document stated that its projections were "necessarily speculative in nature," that "[no] assurance [could] be given that these projections [would] be realized," and that "[a]ctual results may vary from the predictions and these variations may be material," which statements, the court, said "clearly 'bespeak caution'". Where the alleged misrepresentations are sufficiently balanced by cautionary language, it may be found that no reasonable investor would be misled about the risks of the offered security. *See In re Britannia Bulk Holdings Inc*., 665 F. Supp. 2d 404, 413 (S.D.N.Y. 2009) (citing *P. Stolz Family Partnership L.P. v. Daum*, 355 F.3d 92, 96–97 (2d Cir. 2004)). *See also Ponsa-Rabell v. Santander Sec. LLC*, 35 F.4d 26 (1st Cir. 2022) (Santander was not under any duty to repeat information already known or readily accessible to investors in connection with sales of Puerto Rico municipal bonds).

[38] *See, e.g.*, *Dolphin and Bradbury, Inc. v. SEC*, 512 F. 3d 634 (D.C. Cir. 2008) (a general warning about the risk of lease renewals did not excuse the omission of known plans of the major tenant not to renew); *Iowa Pub. Emps.' Ret. Sys. v. Global*, 620 F.3d 137 (2nd Cir. 2010) (general risk factors about future financial performance did not excuse failure to disclose that company risk management protocols did not apply to certain employee trades; *The Greater Wenatchee Reg'l Events Ctr. Pub. Facilities Dist.*, Securities Act Release No. 9471, Admin. Proc. File No. 3-15602 (Nov. 5, 2013) (disclosure of general risks is not substitute for disclosing issuer-specific material risk factors); and *City of San Diego, Cali.*, Securities Act Release No. 8751, Exchange Act Release No. 54,745, Proc. Admin. File No. 3-12478 (Nov. 14, 2006) (disclosure of general risks is not substitute for disclosing issuer-specific material risk factors).

[39] *See, e.g.*, *SEC v. Merchant Capital, LLC,* 483 F.3d 747, 768 (11th Cir. 2007) ("cautionary language, specifically tailored to several of the risks faced by the debt purchasing business, rendered the projections immaterial as a matter of law, even if they were misrepresentations").

[40] Securities Act §§ 7(a)(1), 10(c), 15 U.S.C. §§ 77q(a) (2018), 77j(c); Exchange Act § 13(a), 15 U.S.C. § 78m(a) (2018).

[41] 17 C.F.R. § 229.10 *et seq.* (2023).

[42] Securities Act § 3(a)(2), 15 U.S.C. § 77c(a)(2).

guidance, many issuers look to Reg. S-K for informal guidance on how to comply with the antifraud provisions in municipal securities offerings, including particularly conduit securities offerings supported by corporate credits and, to a lesser extent, content that is not credit-specific.[43]

(i) Risk Factors

"Risk factors" are facts that indicate a risk may be present or may arise or may be greater than otherwise inferred. In the absence of contextualizing facts, risks are merely concepts that cannot be weighed as to materiality. For example, the possibility that a bond might not be paid is a risk but not a fact. The fact that a bond obligation is subject to appropriation is a risk factor because the risk of non-payment arises from the fact of the subject to appropriation limitation.

Reg. S-K, Item 105 requires registrants to disclose "the material factors that make investments in the registrant or offering speculative or risky."[44] Reg. S-K was amended in 2005 as part of securities offering reform to apply Item 105 to annual reports in addition to registration statements, and to require disclosure of material changes in risk factors in quarterly reports, except for asset-backed securities.[45] Reg. S-K was amended again in 2020 to expand the risk factors that registrants must disclose from "the most significant factors" to "the material factors" that make an investment risky or speculative.[46]

Item 105 requires registrants to disclose material risk factors (using the format described in the following paragraph) only if they make an investment in securities "risky" or "speculative." Nevertheless, in its most recent amendments to Reg. S-K, the SEC made clear that material risk factors must be disclosed even when Item 105 does not require a "Risk Factors" section, presumably because they do not make an investment risky or speculative.[47] Consequently, a material risk factor should be disclosed in primary offering documents when its omission would make an offering document misleading or the offering deceitful, even if the securities are investment grade and not "risky" or "speculative."[48]

Item 105 provides that required risk factors must be written in plain English and appear under a caption titled "Risk Factors." In addition, it provides that they must be organized logically (with each risk factor set forth under a sub-caption that adequately describes the "risk") and concisely explain how each disclosed risk affects the securities being offered. Item 105 discourages the inclusion of risks that apply generically to any offering. If generic risk factors are nevertheless included, it requires that they be segregated at the end of the risk factor section under the caption "General Risk Factors." If the Risk Factors section exceeds 15 pages, Item 105 requires a concise, bulleted or numbered summary (totaling two pages or less) of the principal factors to be included in the forepart.[49] Finally, when applied to an offering document rather than an annual

[43] Offering documents of registered for-profit businesses in similar industries may be instructive in offerings of private activity bonds.
[44] 17 C.F.R. § 229.105(a).
[45] Securities Offering Reform, Securities Act Release No. 8591, Exchange Act Release No. 52056, 17 C.F.R. pts. 200, 228, 229, et. al. (July 19, 2005), https://www.sec.gov/rules/final/33-8591fr.pdf.
[46] Securities Act Release No. 10825 (Aug. 26, 2020), https://www.sec.gov/rules/final/2020/33-10825.pdf.
[47] Securities Act Release No. 10825, at n.280, https://www.sec.gov/rules/final/2020/33-10825.pdf.
[48] Securities Act § 17(a)(3), 15 U.S.C. § 77q(a)(3) (2018); Exchange Act § 10(b); Rule 10b-5, 17 C.F.R. § 240.10b-5.
[49] 17 C.F.R. § 229.105(b).

report, Reg. S-K, Items 501 and 502 require that (a) risk factors immediately follow the summary section, if one is included, or the cover page or inside cover page pricing information section of the offering document and (b) a cross reference (with page number) be included on the cover page, prominently or otherwise highlighted, and in a table of contents inside the front or back cover.[50]

(ii) Uncertainties

In addition to the required disclosure of "risk factors" and associated "risks," two items of Reg. S-K require registrants to disclose "uncertainties." In presenting summary financial information, registrants must discuss or refer to "any material uncertainties" that might cause the information "not to be indicative of the registrant's future financial condition or results of operations."[51] Registrants must also include management's discussion and analysis of financial condition and results, focusing specifically 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."[52]

c. State Blue Sky Laws

Most states have adopted securities (or "blue sky") laws modeled on the Uniform Securities Act of 1956.[53] Some states have adopted amendments recommended by the Uniform Law Commission in 1985, 1988, and 2002.[54]

Like the federal Securities Act, state blue sky laws generally require securities offerings in the state to be registered, unless exempt. Also like the federal Securities Act, they generally exempt offerings by states, political subdivisions, and their agencies and instrumentalities.[55] In addition, federal law pre-empts state registration requirements for "covered securities," including municipal securities that are exempt under Section 3(a)(2) of the Securities Act unless issued by an issuer within the state.[56]

State blue sky laws generally contain the same antifraud provisions as Rule 10b-5 for securities offered in the state and similarly do not exempt any securities from the provisions.[57] Although federal law pre-empts certain blue sky registration requirements, it does not pre-empt state antifraud provisions.[58] Consequently, if, and when, risk factors are required to be disclosed by the federal antifraud provisions, they are likely also required by relevant state blue sky laws, among other possible disclosure requirements.

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[50] 17 C.F.R. §§ 229.501, 229.502.
[51] 17 C.F.R. § 229.301.
[52] 17 C.F.R. § 229.303.
[53] UNIF. SEC. ACT (NAT'L CONFERENCE OF COMM'RS ON UNIF. STATE LAWS 1956), https://www.nasaa.org/wp-content/uploads/2021/10/1956-Uniform-Securities-Act-with-NASAA-Updates-and-Commentary.pdf.
[54] *Uniform Securities Act*, WIKIPEDIA, https://en.wikipedia.org/wiki/Uniform_Securities_Act (last updated July 24, 2022).
[55] UNIF. SEC. ACT §§ 301, 402(1) (NAT'L CONFERENCE OF COMM'RS ON UNIF. STATE LAWS 1956).
[56] Securities Act, §§ 18(a), 18(b)(4)(E), 15 U.S.C. §§ 77r(a), 77r(b)(4)(E) (2018).
[57] UNIF. SEC. ACT, §§ 101, 402.
[58] Securities Act, §18(c)(1), 15 U.S.C. §§ 77r(c)(1).

Violations of state antifraud provisions can result in criminal penalties and, if intentional or negligent, actions by investors for rescission or damages.[59] Consequently, issuers can be liable under state law for damages caused by negligent misleading omissions of material risk factors, even though they would not be liable in a private damage action under federal law unless the omissions were reckless.

d. Additional Disclosure Requirements of Underwriters and Municipal Advisors

When offering municipal securities in a primary offering, brokers, dealers, and municipal securities dealers have duties to analyze and review risks associated with the securities under SEC and MSRB diligence, suitability, and disclosure requirements. Under rules established by the MSRB, underwriters have a duty to investors to review and understand material risks (not merely risk factors) and to disclose to customers the risks associated with the bonds they sell when the underwriters offer municipal securities. Municipal advisors may also have comparable duties when they participate in preparing offering documents for and associate themselves with competitive offerings.

(i) Duty to Review; Evaluation

According to the SEC, municipal securities underwriters have a duty to review offering documents for possible misstatements and misleading omissions of material facts.[60] Certain SEC statements suggest that the duty applies to omissions of material risks as well as facts.[61]

According to the SEC, an underwriter makes an implied recommendation about the securities it is underwriting, including a representation that it has a reasonable belief in the truthfulness and completeness of the "key representations" made in disclosure documents, and must exercise reasonable care to evaluate the accuracy of "statements" in the disclosure documents.[62] By referring to "key representations" and "statements," rather than "facts," the SEC may have signaled that it believes misleading omissions of material "risks," not merely omissions of material "facts," are actionable, if made without requisite care. Consistent with this possibility, the SEC's Division of Examinations (formerly the Office of Compliance, Investigations, and Examinations) has noted that many underwriting firms employ offering approval procedures under which supervisors or committees review the "financial and risk disclosures" in final official statements.[63]

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[59] UNIF. SEC. ACT, § 410(a).
[60] Exchange Act Release No. 26100, 17 C.F.R. pt. 240 (Sept. 28, 1988) https://www.sec.gov/rules/proposed/1988/34-26100.pdf.
[61] *Id.* ("a thorough, professional review by underwriters of municipal offering documents could encourage appropriate disclosure of foreseeable risk").
[62] *Id*.
[63] *National Examination Risk Alert–Strengthening Practices for the Underwriting of Municipal Securities*, SEC OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS, Mar. 19, 2012, https://www.sec.gov/about/offices/ocie/riskalert-muniduediligence.pdf.

(ii) Regulation Best Interest

When broker-dealers offer municipal securities to retail customers in primary offerings or otherwise recommend an investment in the securities, they must understand the associated risks and the customer's risk profile, and reasonably believe that the recommendation is in the customer's best interest, in order to comply with Regulation Best Interest.[64] To do so, they may rely upon the issuer's disclosure of risk factors made in accordance with existing disclosure requirements.

Under Regulation Best Interest, when making a recommendation of any securities transaction to a "retail customer," a broker, dealer, and associated employee must act in the best interest of the customer.[65] A "retail customer" is one who would purchase the security "primarily for personal, family, or household purposes."[66] The best interest obligation is satisfied if, among other requirements, in making the recommendation the person exercises reasonable diligence, care, and skill to (a) provide the customer, in writing prior to, or at the time of, the recommendation, full and fair disclosure of all material facts relating to conflicts of interest that are associated with the recommendation,[67] (b) understand the potential risk associated with the recommendation,[68] and (c) have a reasonable basis to believe that the recommendation is in the best interest of the customer based on the customer's investment profile and the potential risks, rewards, and costs associated with the recommendation.[69] A retail customer's "investment profile" includes the customer's "risk tolerance."[70]

Disclosable conflicts of interest may include recommending a municipal security underwritten by the broker-dealer, but:

> "broker-dealers may rely on the existing disclosure regime governing securities issuers to disclose the risks associated with any issuer, security or offering, and it is not our intent to require the broker-dealer to duplicate or expand on those disclosures"[414]

"414. *See, e.g.,* Item 503(c) of Reg. S-K (requiring disclosure of the "most significant" factors that make an offering "speculative or risky," as well as an explanation of how each risk "affects the issuer or the securities being offered"). *See also* Form 10-K (requiring a description of the 503(c) risk factors that are "applicable to the registrant"). In some cases, [Self-Regulatory Organization] rules applicable to recommendations of particular securities may also require disclosure of risks." [71]

(iii) MSRB Rule G-19

When broker-dealers offer municipal securities to customers other than retail customers, and when municipal securities dealers offer municipal securities to any customer, they must have

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[64] Rule 15l-1, 17 C.F.R. § 240.15l-1 (2023).
[65] Rule 15l-1(a)(1), 17 C.F.R. § 240.15l-1(a)(1).
[66] Rule 151-1(b)(1), 17 C.F.R. § 240.151-1(b)(1).
[67] Rule 15l-1(a)(2)(i), 17 C.F.R. § 240.15l-1(a)(2)(i).
[68] Rule 15l-1(a)(2)(ii)(A), 17 C.F.R. § 240.15l-1(a)(2)(ii)(A).
[69] Rule 15l-1(a)(2)(ii)(B), 17 C.F.R. § 240.15l-1(a)(2)(ii)(B).
[70] Rule 15l-1(b)(2), 17 C.F.R. § 240.15l-1(b)(2).
[71] Exchange Act Release No. 86031, 84 Fed. Reg. 33,318, 33,360 n.414 (June 5, 2019) (to be codified at 17 C.F.R. pt. 240).

a reasonable basis to believe that the recommended transaction is "suitable for the customer."[72] To do so, they must understand the material risks associated with the securities. An issuer's risk factor disclosure can assist them in complying with this requirement.

MSRB Rule G-19 imposes three main obligations on a broker, dealer or municipal securities dealer: reasonable-basis suitability, customer-specific suitability, and quantitative suitability.[73] Under the "reasonable-basis" obligation, a broker, dealer or municipal securities dealer must have "a reasonable basis to believe, based on reasonable diligence, that the recommendation is suitable for at least some investors."[74] Under the "customer-specific" obligation, a broker, dealer or municipal securities dealer must have "a reasonable basis to believe that the recommendation is suitable for a particular customer based on that customer's investment profile."[75] This requirement does not apply, however, to transactions with customers that a broker, dealer or municipal securities dealer reasonably believes is a "sophisticated municipal market professional" or "SMMP."[76] Under the "quantitative suitability" obligation, a broker, dealer or municipal securities dealer must have "a reasonable basis for believing that a series of recommended transactions, even if suitable when viewed in isolation, are not excessive and unsuitable for the customer when taken together in light of the customer's investment profile."[77]

(iv) MSRB Rule G-47

When selling municipal securities to a customer other than an SMMP, a broker, dealer, or municipal securities dealer must disclose to the customer, at or prior to the time of trade, all material information known about the transaction and material information about the security that is reasonably accessible to the market, including "facts that are material to assessing the potential risks of the investment."[78] Issuers assist underwriters in complying with these requirements when they disclose material risks in the issuer's offering documents.[79]

(v) MSRB Rule G-17

MSRB fair dealing rules also require underwriters to disclose associated risks when offering municipal securities to their customers. Under MSRB Rule G-17, in the conduct of its municipal securities or municipal advisory activities, each broker, dealer, municipal securities dealer, and municipal advisor "shall deal fairly with all persons and shall not engage in any

[72] MSRB Rule G-19.
[73] MSRB Rule G-19, Supplemental Material .05.
[74] MSRB Rule G-19, Supplemental Material .05(a).
[75] MSRB Rule G-19, Supplemental Material .05(b).
[76] MSRB Rule G-48(c). A "sophisticated municipal market professional," or "SMMP," as applied to underwritten securities transactions, is a customer that (i) is a person or entity with total assets of at least $50 million or a bank, savings and loan association, insurance company, registered investment company, federally or state registered investment adviser, (ii) has affirmatively indicated that it (A) is exercising independent judgment in evaluating (x) the recommendations of the dealer and (y) the quality of execution of the customer's transactions and (B) has timely access to material information that is available publicly through established industry sources, and (iii) the dealer reasonably believes is capable of evaluating investment risks and market value independently, both in general and with regard to the particular transactions. MSRB Rule D-15.
[77] MSRB Rule G-19, Supplemental Material 0.5(c).
[78] MSRB Rule G-47(a); MSRB Rule G-48(c); MSRB Rule G-47, Supplementary Material .01.a.
[79] MSRB Rule G-47, Supplementary Material .03.c.

deceptive, dishonest, or unfair practice."[80] In order to meet their obligations under MSRB Rules G-17 and G-19, underwriting firms "must analyze and disclose to customers the risks associated with the bonds they sell, including, but not limited to, the bond's credit risk."[81]

(vi) Municipal Advisors

According to the SEC, if a dealer municipal advisor (i) associates itself with a competitive offering of municipal securities, (ii) has access to issuer data, and (iii) participates in drafting the disclosure document, the dealer municipal advisor has an obligation to "inquire into the completeness and accuracy of disclosure" that is comparable to an underwriter's duty in a negotiated offering.[82]

2. HOW TO ASSESS AND DISCLOSE RISK FACTORS – PRACTICAL CONSIDERATIONS

Determining which risk factors, if any, should be included in an offering document should be a collective effort by the issuer, its counsel, its municipal advisor, if any, and with input from the underwriter and its counsel, if any (the "financing team"). There is no one "standard" process for evaluating and disclosing risk factors, and materiality is not tied to a set formula.

In pursuing this process, the financing team should consider the overriding purpose of risk factors: to inform investors about facts that make an investment in the offered securities potentially speculative or risky or that evidence a material risk that the issuer's financial condition and results of operation may decline.

a. Adoption of Written Policies and Procedures

If an issuer has adopted written policies and procedures for its primary and secondary market disclosure, such policies and procedures may address the process for identifying, evaluating, and disclosing risk factors. Thoughtful policies and procedures benefit issuers in at least two important ways. They (1) reduce the chances of making a material misstatement or misleading omission in disclosure and (2) help to establish a defense of reasonable care against actions for misstatements and omissions that may still occur, all of which facilitate compliance

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[80] MSRB Rule G-17.

[81] *MSRB Reminds Firms of Their Sales Practice and Due Diligence Obligations When Selling Municipal Securities in the Secondary Market*, MUN. SEC. RULEMAKING BD. (Sept. 20, 2010), https://www.msrb.org/MSRB-Reminds-Firms-Their-Sales-Practice-and-Due-Diligence-Obligations-When-Selling-Municipal-0.

[82] Exchange Act Release No. 26100, at n.92 (Sept. 22, 1988). *See* Complaint, *SEC v. City of Rochester, N.Y., Rosiland Brooks-Harris, Capital Markets Advisors, LLC, Richard Ganci, and Richard Tortora*, No. 22-cv-6273 (W.D.N.Y. June 14, 2022) (alleging the municipal advisor had knowledge of the Rochester City School District's (the "District") extreme financial distress prior to the release of an offering document containing outdated financial statements for the District and failing to disclose the District was experiencing unusual financial distress). *See also Peacock, Hislop, Staley & Given, Inc. and Larry S. Given*, Securities Act Release No. 7353, Exchange Act Release No. 37777, Admin. Proc. File No. 3-9139 (Oct. 2, 1996), *County of Nevada, City of* Ione*, Wasco Public Financing Authority, Virginia Horler, and William McKay*, Securities Act Release No. 7503, Exchange Act Release No. 39612, Admin. Proc. File No. 3-9542 (Feb. 2, 1998).

with federal securities laws.[83] Several recent SEC orders highlight the importance of formal policies and procedures. In the SEC's cease and desist order concerning City of Harrisburg, Pennsylvania ("*Harrisburg*"), Harrisburg's efforts in creating formal policies and procedures to ensure the accuracy of its financial statements were stated to be a contributing factor to the SEC's willingness to settle the administrative proceeding.[84] Similarly, the presence of formal disclosure policies and procedures were stated to be a contributing factor in the SEC's settlement with the State of Illinois.[85] Both SEC orders emphasized the importance of formal written disclosure policies and procedures. *Crafting Disclosure Policies*, published by NABL in 2015, describes a suggested process for developing disclosure procedures, including review of information, in detail.

b. Developing Risk Factor Disclosure

The financing team should carefully consider what risks and risk factors, if any, to disclose in an offering document, because risks associated with different types of obligations and credits vary greatly, as does susceptibility to such risks among issuers and securities issues.

Securities law liability can attach if disclosures from an issuer's last deal are duplicated without carefully considering whether such disclosures are appropriate for the current transaction. This practice triggered liability for underwriters in the *Bradbury* administrative action.[86] According to the SEC's description of the facts, "Bradbury told O'Neill that the transaction was of the same type as the previous transaction; that investors were already lined up; and that what needed to be done was to prepare documents, including an [official statement], modeled on those that were forwarded" and that the transaction was on a tight time-frame and that counsel should start with a disclosure document from an earlier transaction.[87] The risk disclosures were nearly identical between both offering transactions, despite there being key factual differences between the two (specifically, that a major tenant had given notice of its intent to vacate the premises serving as collateral for the transaction). Accordingly, the D.C. Circuit Court found that the underwriters acted recklessly in offering bonds that failed to disclose particular and critical information regarding the tenant notice.[88]

The financing team should consider a process that (a) identifies the risks, (b) identifies facts (risk factors) that may contribute to or indicate the risk, (c) evaluates the identified risk factors for materiality, and (d) determines how and where to disclose the material risk factors in the offering document.

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[83] *See* NAT'L ASS'N OF BOND LAWYERS, CRAFTING DISCLOSURE POLICIES (2015), https://www.nabl.org/DesktopModules/Bring2mind/DMX/Download.aspx?PortalId=0&TabId=176&EntryId=1008, for a further description of the purpose and benefits of having formal disclosure policies and procedures.
[84] *City of Harrisburg, Pa.*, Exchange Act Release No. 69515, Admin. Proc. File No. 3-15316 (May 6, 2013).
[85] *State of Illinois*, Securities Act Release No. 9389, Admin. Proc. File No. 3-15237 (Mar. 11, 2013).
[86] *See Dolphin & Bradbury, Inc. & Robert J. Bradbury*, Securities Act Release No. 8721, Exchange Act Release No. 54143, Admin. Proc. File No. 3-11465 (July 13, 2006). *See also Dolphin & Bradbury Inc. v. SEC*, 512 F.3d 634 (D.C. Cir. 2008).
[87] *See id.*
[88] *See Dolphin & Bradbury*, 512 F.3d at 643.

(i) Identifying the Risks and Risk Factors

Risk Factors and Risks. Risk factors can include a variety of facts, including facts that already exist (for example, the location of an issuer along the coast) and facts that are anticipated by the issuer such as plans and cost estimates (for example, plans for addressing the impact of global warming and sea level rise).

Risk factors should not simply suggest a risk *may* exist, if the issuer knows facts indicating that the risk does exist and is material. For example, if an issuer pledges a particular revenue stream as security for its revenue bonds and has not taken action to perfect that pledge, merely disclosing the resulting risk (that the issuer's contractual obligations could be adversely affected in a bankruptcy proceeding that it could initiate) is no substitute for also disclosing information that would enable investors to evaluate the risk (for example, disclosing that if the issuer were to become involved in a bankruptcy proceeding, the pledge would likely be voidable), if the risk is material in light of the issuer's creditworthiness.

Many potentially significant risk factors are common knowledge to reasonable investors. Such risk factors, as a general matter, need not be disclosed to comply with the antifraud provisions.[89] A reasonable investor may not, however, know the extent to which an issuer is susceptible to one or more of these risks. If facts indicate that an issuer is materially more susceptible than a reasonable investor would surmise, those facts could significantly alter the total mix of available information and therefore could be material. For example, if a town is closely surrounded by forests and has encountered years of severe drought that resulted in devastating forest fires in nearby areas of the state, those facts could be material and likely should be disclosed, even if the generic risk of forest fires is not. Similarly, a risk factor that applies to all securities within a specific sector in a state, for example public school bonds, while not issuer-specific, may be material and should be disclosed, if not common knowledge to investors.

When novel developments affect an entire industry or sector, issuers should assess the specific impact on their operations and discern what information is material to an offering. With COVID-19, for example, changes were occurring almost daily, many of which materially adversely impacted issuers. When issuers consider how much disclosure is needed in an offering document, there is a tension between how much of the widely disseminated news must be disclosed in addition to issuer-specific information.

Any fact that indicates a meaningful risk to an investment in an issuer's securities could be material, regardless of whether it affects the likelihood of payment by the issuer. Material risk factors could include, for example, risks to the tax-exempt status of securities,[90] risks regarding

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[89] *See Ponsa-Rabell v. Santander Sec. LLC*, 35 F.4th 26 (1st Cir. 2022) (Santander was not under any duty to repeat information already known or readily accessible to investors in connection with sales of Puerto Rico municipal bonds: "[i]t is not a material omission to fail to point out information of which the market is already aware.") (citing *Baron v. Smith*, 380 F.3d 49, 57 (1st Cir. 2004)) (citing *In re Donald Trump Casino Sec. Litig.*, 7 F.3d 357, 377 (3d Cir. 1993)).

[90] *See Neshannock Township Sch. Dist*., Securities Act Release No. 8411, Exchange Act Release No. 49600, Admin Proc. File No. 3-11461 (Apr. 22, 2004) (failure to disclose fact indicating material risk to tax exempt status of securities).

the liquidity of auction rate securities,[91] facts that affect how a remarketing agent may periodically remarket variable rate demand bonds,[92] or a bond insurer's option to accelerate payment in the event of an issuer default. Similarly, in structured credit financings (including mortgage revenue, student loan, and prepaid energy bond offerings), material risk factors may have nothing to do with the issuer's independent creditworthiness.

Appendix A to this paper includes for reference certain considerations related to various risk factors, including those related to the credit or credit risk, those related to the type of obligation being issued, and those related to particular circumstances the issuer may be experiencing at the time. While Appendix A is not a comprehensive discussion of the entire universe of risk factors, it can be referred to for examples of the practical application of considerations discussed herein.

Materials to Review. Risks and risk factors can be identified through review of the issuer's previously issued offering documents, recent audited financial statements, prior continuing disclosure notices, if any, and its responses to "due diligence" questions. Additionally, risks and risk factors also can be identified by third-party (including rating agency) subject matter review, industry sources (e.g., National Federation of Municipal Analysts and Government Finance Officers Association publications), publicly available information for similar types of credits and obligations, disclosure documents for comparably situated issuers, and senior official or governing body review, among other methods.

As a deal progresses, due diligence materials, including risk management programs, legal and tax due diligence questionnaires, budgets, board and governance committee minutes, and information or materials provided to rating agencies can be helpful in determining risks and risk factors. To the extent a rating agency asks any questions related to the credit or the financing structure, the financing team should consider whether the questions indicate a material risk. Disclosure policies and procedures may be helpful in identifying the sources of material and information to review when developing or reviewing risk factor disclosure in primary offerings and, where applicable, secondary market disclosure.

(ii) Evaluation for Materiality

As noted above in Part I, Reg. S-K, Item 105 requires registrants to disclose risk factors only if they are material *and* make an investment risky or speculative, but the antifraud provisions may require more. Consider, for example, a risk factor that, if disclosed, would lead investors to believe that a municipal security should be valued as if "A" rated, rather than "AAA" or "Aaa" rated, and that securities in the two rating categories are priced differently by the market. If the risk factor is omitted from the issuer's offering document, the omission likely would violate the antifraud provisions, even though the security being offered is, in the judgment of the rating agencies and a reasonable investor, neither risky nor speculative. Consequently, material risk factors should be disclosed in offering documents even when the securities being offered are well-

[91] *SEC v. Morgan Keegan*, 678 F.3d 1233, 1244 (8th Cir. 2012).
[92] *See Bear, Stearns & Co. Inc.,* Securities Act Release No. 8684, Exchange Act Release No. 53888, Admin. Proc. File No. 3-12310 (May 31, 2006) and *Deutsche Bank Trust Co. Americas*, Securities Act Release No. 8767, Admin. Proc. File No. 3-12526 (Jan. 9, 2007).

rated and neither risky nor speculative (although better rated, less risky securities are, of course, less likely to have material associated risk factors).

Materiality is measured by importance to the hypothetical "reasonable investor," rather than actual investors, so the SEC can bring enforcement actions under the antifraud provisions even when an omitted fact is not important to actual investors. Consequently, when advising clients about the disclosure of risk factors, counsel may wish to take into account inherent uncertainties about whether the SEC would consider the risk factor disclosure sufficient to avoid a violation of the antifraud provisions.

Omitted facts are material only if they would significantly alter the total mix of information made available to investors. The total mix would not be altered by omitting a risk factor of common knowledge to a reasonable investor. For example, it is a fact that the value of fixed rate debt securities decreases when prevailing market interest rates increase, and that the longer a municipal security's term, the greater the decrease. Nevertheless, although this risk factor should be important to investors who may wish to liquidate securities prior to their maturity, it need not be disclosed when offering securities to investors, because it should be known to a reasonable investor and, consequently, would not significantly alter the total mix of available information about the securities. As noted above, Reg. S-K Item 105 discourages the disclosure of risks that apply generically to any offering.

Misleading omissions of material facts may occur in offerings of general obligation bonds as well as revenue obligations.[93] General obligation bonds, especially if issued by a development district, may be more susceptible to risk than revenue bonds issued by an established municipality and backed by revenue from the sale of essential services without competition. Accordingly, the type of security (general obligation or revenue) should not dictate whether to disclose material risk factors. In practice, a risk factors section is more commonly included in offerings of revenue obligations than in offerings of general obligation bonds. That practice may reflect fewer material risks to the payment of general obligation bonds or it may reflect a desire not to imply that securities are riskier than they are by including a section devoted to risks. See "Name of the Risks Section" below. Nevertheless, material risk factors, if any, like other material facts, should be disclosed in offerings of all securities, regardless of whether they are general obligations or revenue obligations. See "Placement of Risk Factors in Primary Offerings" below.

When issuers offer securities by means of an offering document, the document must comply with the antifraud provisions, regardless of whether the securities are offered to the public generally or only to accredited investors or qualified institutional buyers.[94] Whether an omitted risk factor or other fact is material depends on whether it would be significant to a reasonable investor, as opposed to actual investors. Consequently, an omitted fact's materiality should not be affected by whether an offering is made to the public generally or only to institutional investors. If an offering of securities is restricted to institutional investors (as opposed to high net worth individuals), however, the informed nature of the restricted audience to which the offering is

[93] *See, e.g.*, *State of Illinois*, Securities Act Release No. 9389, Admin. Proc. 3-15237 (Mar. 11, 2013).
[94] *Cf. FINRA Regulatory Notice 10-22: Obligation of Broker-Dealers to Conduct Reasonable Investigations in Regulation D Offerings*, FIN. INDUST. REG. AUTH. (Apr. 15, 2010) https://www.finra.org/rules-guidance/notices/10-22.

addressed could affect the type of risk factor that would alter the "total mix" of information available to the offerees and, therefore, should be disclosed. If securities are offered only to institutional investors, as a practical matter the omission of a risk factor known to institutional investors generally, even if not known to reasonable retail investors, presents less risk to an issuer. Institutional investors would be less able to establish reliance on the omission in an action for damages. The omission might also be less likely to result in an SEC enforcement action, especially in view of the exception afforded to required underwriter disclosures to SMMPs by MSRB Rule G-47.

Determinations of materiality are mixed questions of fact and law, so they cannot be resolved solely by legal counsel. Through discussions with potential investors, underwriters and dealer municipal advisors are generally in a better position to understand what facts are important to actual investors. Counsel, on the other hand, may be better versed in the types of facts that the SEC considers important to a reasonable investor. Since actual institutional investors are the closest approximation to a reasonable investor, issuers may consult the financing team (including both underwriters or municipal advisors and legal counsel) in making judgments as to the materiality of certain risk factors.

(iii) How and Where to Disclose Risks

Placement of Risk Factors in Primary Offering Documents. As discussed above, Reg. S-K regulates the placement, in addition to the content, of risk factor disclosure in non-exempt offerings. Because nearly all offerings of municipal securities are exempt from registration with the SEC and, therefore, from Reg. S-K, these requirements are generally inapplicable to municipal securities offerings. Rather, the placement of risk factors is dictated, if at all, by the antifraud provisions.

The location of risk factors in an offering document is less important than the clarity with which they are disclosed. However, courts have noted that disclosure documents may violate the antifraud provisions when material facts are buried in unsuitable parts of the document.[95] Courts have also found risk factor disclosures to be adequate when combined in a separate risks section, especially when prominent.[96] Accordingly, risk factors should be located near the facts that they qualify or in a separately labeled risk factor section. Risk factors should not, however, be buried

[95] *See In re Donald J. Trump Casino Sec. Litig. – Taj Mahal Litig.*, 7 F.3d 357, 369-71 and 369 n.12 (3d Cir. 1993) (citing *TSC Industries, Inc.*, 426 U.S. at 448–49 (risk disclosure might not have been adequate if buried in the offering document) (*dictum*)).

[96] *See, e.g.*, *Gasner v. Bd. of Sup. of Dinwiddie, Va.,* 103 F.3d 351, 358-59 (4th Cir. 1996). This litigation arose as a result of the financial failure of an anaerobic composting facility constructed by a private firm for the purpose of processing the solid waste of a county. Bonds issued to finance the purchase and installation of equipment for the facility were defaulted when the venture failed. Plaintiffs asserted that the Official Statement misrepresented the anaerobic composting technology by labeling it as "proven," and that the issuer omitted to state that the facility would receive only a one-year experimental operating permit. The court upheld the district court's dismissal of the case because the Official Statement was "replete with cautionary language" including a Risk Factors section that stated, among other things: "there can be no guaranty that the [project] will be completed … or that once operational it will generate sufficient revenues to meet operational costs and repay principal and interest …." The court reasoned that these Risk Factors were not "vague, boilerplate disclaimers" but rather were "tailored precisely to address the uncertainty surrounding repayment of the Bonds."

within paragraphs of generic risks that are not material to the issue. It is prudent to include cross-references between facts and related risk factors when they appear in separate sections.

Cases upholding the adequacy of risk factor disclosure typically have dealt with disclosures in registered offerings, where the risk factors were placed in a separate "Risk Factors" section near the front of the offering document in accordance with Reg. S-K. For that reason, and because the SEC is more likely to accept the adequacy of risk factor disclosure if risk factors are located in a manner consistent with Reg. S-K, issuers of risky or speculative investments can minimize their exposure to liability if they look to Reg. S-K requirements for the placement of risk factors in their offering documents. For offerings of other securities, disclosure can safely occur in a risks section located elsewhere in the document or in other sections in proximity, or cross-referenced, to the express or implied statements that the risk factors qualify.

Name of the Risks Section. As discussed above, Reg. S-K requires risk factors to be disclosed in primary offering documents in a section titled "Risk Factors," but only if a risk factor makes an investment in the offered securities risky or speculative. This requirement, too, is inapplicable to exempt municipal securities offerings. However, as in the placement of risk factors, issuers can minimize their exposure to liability in offerings that involve risky or speculative investments if they locate risk factors in a section entitled "Risk Factors" as provided by Reg. S-K. For other offerings that involve material risk factors, a risks section can be titled "Bondholders' Risks" or "Investment Considerations," for example, and issuers are free to adopt such titles that do not imply greater or lesser risks to an investment than is the case.

Concise; Plain English. Although Reg. S-K requires risk factor disclosure in registered offerings to be written in plain English and to observe certain page limits, as described above, no such limitations are imposed by Rule 10b-5. Nevertheless, the use of plain, concise English may be probative of whether purchasers were given adequate, and clear, facts with which to make an informed decision.[97] Policies and procedures could consider a framework that incorporates a plain English approach to risk factor review.

CONCLUSION

There are numerous considerations that issuers of municipal securities, underwriters and their lawyers should evaluate when (a) identifying and disclosing risk factors in primary offerings of municipal securities and, in some circumstances, related secondary market disclosure and (b) developing policies and procedures for doing so. This paper is not intended to provide an exhaustive treatment of risk factor disclosure or risk factor examples, and it should not be read to make any suggestion of, or establish any presumption as to, best practices in connection with municipal securities disclosure.

[97] *See, e.g.*, *Basic Inc. v. Levinson*, 485 U.S. at 231 (citing *TSC Industries, Inc.*, 426 U.S. at 448-49) (noting that the Supreme Court, when considering the materiality standard, had observed that bringing an overabundance of information into a document may mislead holders, burying them in "an avalanche of trivial information").

Appendix A

Example Risk Factors Considerations

The following chart presents selected common risks associated with an investment in municipal securities of different types as well as examples of risk factors that may evidence or give rise to such risks and, if material, should be disclosed in primary offerings. The risks and risk factors include those that may apply to all types of securities and issuers, those related to the type of securities, and those related to the credit (i.e., sector) of the issuer. The risks and risk factors are not a comprehensive list and do not purport to suggest language that may or should be used to disclose the risks and risk factors, when applicable, but rather are meant to provide illustrative examples of risks and risk factors to assist practitioners when advising clients about disclosure policies and procedures and the disclosure of risk factors.

Risks Related to All Securities

Certain risks may arise regardless of the type of undertaking supporting payment of the securities being offered, other features of the securities, or the sector in which the securities are offered. The table below provides illustrative examples of risks and risk factors that may apply to any type of securities and sector.

Type of Risk	Risk	Example Risk Factors	Observations
Contract enforcement	Bondholders may not have an adequate remedy to enforce the bond contract.	- The issuer enjoys sovereign immunity from suit. - The enforceability of the bond may be limited to available constitutional and statutory remedies. - The bond is not subject to acceleration. - No trustee or other representative has been appointed to act for bondholders. - The issuer may undergo a state receivership proceeding if it becomes insolvent, which could delay or frustrate bondholder remedies. - The issuer is authorized to petition for an adjustment of its debts under Chapter 9 if it becomes insolvent, which could similarly delay or frustrate remedies.	Risk disclosure may include a description of limitations of the ability of the trustee/bondholders to exercise remedies under the bond documents and particular constitutional and statutory limitations, so as to qualify the otherwise inferred effect and value of the bond contract, depending on the strength of the credit. For the same reason and under the same conditions, risk disclosure around the ability of the issuer to commence a bankruptcy proceeding, and the status of any statutory lien and treatment of special revenues, should be considered, when they could have a substantial impact on how bondholders would fare in a proceeding. To the extent there are any deal-specific factors that may limit the bondholders' ability to recover, those may be disclosed as risk factors as well.

Type of Risk	Risk	Example Risk Factors	Observations
Interest rate swap risk	The swap (a) may not effectively hedge the issuer's exposure to variable interest expense, especially if the other party becomes insolvent, and (b) may result in a substantial liquidity burden to meet collateral posting obligations or settle the swap on early termination.	- The rates payable on the bonds and the swap are set differently, could differ, and could result in net issuer payment obligations that exceed the fixed rate on the swap. - The swap may be terminated upon an event of default or other termination event, including a reduction of the issuer's rating below "X," and if terminated the issuer could be required to pay the value of the swap to the other party upon X days' notice. - The issuer must post collateral if the value of the swap to the other party exceeds $X (or a lower amount if the rating of the issuer is reduced). - The issuer is exposed to the credit risk of the swap counterparty if prevailing interest rates increase substantially.	If an issuer uses an interest rate swap with variable rate securities to achieve a synthetic fixed rate financing and a loss of the swap's effectiveness or collateral posting requirements could be material, consideration should be given to disclosing associated risk factors.
Non-investment grade and non-rated securities	Bondholders' ability to recover could be limited, risky or adversely affected by the creditworthiness and ability of the issuer to continue operating.	- There is little liquidity in the secondary market for non-investment grade securities of the type offered. - The ability of the issuer to complete the project and earn sufficient revenue to operate and pay debt service is limited or at risk due to specified conditions.	If the market for secondary trading of the securities is smaller and less liquid than for investment grade securities, purchasers of the bonds may be unable to liquidate their holdings in the event of issuer financial reversals, and may need to be able to bear the risks of their investment for an extended period.

Type of Risk	Risk	Example Risk Factors	Observations
		- No rating for the bonds has been applied for or received.	If the issuer applied for a rating and did not receive one, or received one and decided not to use the rating, consideration should be given to disclosing the underlying reasons of whether a rating was not applied for (and why) or not received, or, in certain circumstances, disclosing that it was applied for but not received or used.
Rapidly evolving public health risks	Rapidly evolving public health crises may adversely affect the ability of the issuer to generate revenues to operate and pay debt service and may result in increased short-term borrowings.	- It is difficult to predict, plan for, and adjust to rapidly evolving contagion. - In the recent COVID-19 pandemic, the issuer incurred additional operating costs in specified amounts (of which specified amounts were offset by federal aid), a specified increase in short-term debt, and a specified decline in average annual operating revenue due to reductions in available workforce, stay-at-home orders, government-mandated closures and other uncontrollable events. - Due to a continuing pandemic, the issuer has budgeted reduced revenues or increased operating expenses (or both) by specified amounts in the current fiscal year.	Public health events and rapidly evolving risks may have drastic, potentially unknown, effects on an issuer's budget and ability to plan for future operations. Consideration should be given to disclosure around actual effects of the particular event, including budget changes, delays (particularly for new construction projects), potential future adverse impacts on the issuer or the project to the extent quantifiable (with appropriate cautionary language), any relief measures provided or mitigation measures taken, and other specific effects on the issuer or the project being financed.

Type of Risk	Risk	Example Risk Factors	Observations
Climate change	Issuer revenues, expenses, and debt burden could be adversely affected by consequences of climate change or other material disasters.	- The issuer is located in an area with particular environmental risk, including, but not limited to: • locations prone to extended drought and fire risk • low-lying flat coastal areas that are prone to flooding and storm surge • areas surrounded by forests which have not undergone periodic controlled burns to manage fire risk • areas subject to earthquakes, hurricanes, tornados or other increasingly extreme weather events and, if applicable, has incurred specified losses in recent years in prior such events - The issuer has estimated substantial specified capital and operating costs of improvements to make its infrastructure sustainable. A specified substantial part of the issuer's economy is dependent on the mining of fossil fuels.	Climate change and environmental risk factors encompass a wide range of risks including weather and natural disaster risks and environmental risks specific to the land or project financed. Such risk factors will be specific to the issuer and particularly the geographical location. In addition to disclosing the climate change and environmental risks themselves, part of the risk analysis includes the issuer's or management's approach to such risks and the financial impact they may have on the issuer's future health, availability or cost of any mitigation programs or federal or state mitigation or disaster relief funds, and other studies or programs aimed at combating climate change. There may also be risks associated with bonds that are labeled or have a designation of "green," including features of the issuance that contribute to the "green" designation and any reporting requirements related to the project.

Type of Risk	Risk	Example Risk Factors	Observations
Cybersecurity	The operations and data of the issuer could become the target of a cybersecurity attack, which could interrupt revenue, result in losses, and increase liability and expenses.	- The issuer has been the subject of a cyberattack, which resulted in specified consequences. - The issuer relies on third-party software defenses, which have been breached in other applications. - The issuer has received a third-party report of system weaknesses and is in the process of addressing them. - The issuer does not have cybersecurity insurance, policies and procedures, or training or mitigation programs for cybersecurity issues.	Consider how to comply with a duty to disclose material cybersecurity risks without drawing attention to cybersecurity weaknesses that may attract cyber criminals.

Risks Related to Type of Securities

Certain risks arise by virtue of the type of undertaking supporting payment of the securities being offered (e.g., tax-supported, revenue, credit enhanced) or other features of the securities (e.g., demand options, variable rates). The table below provides examples of risks and risk factors related to type of securities and their features.

Type of Securities	Risk	Example Risk Factors	Observations
Revenue bonds	Bondholders may not enjoy the benefits of the lien on revenues.	- Pledged revenues are not segregated so as to enable identification of pledged collateral against which remedies may be exercised under state law. - The pledged revenues are not "special revenues," as a result of which enforcement of the pledge may be stayed by a bankruptcy filing, and the pledge is not made by statute, and therefore is inapplicable to post-petition revenues in bankruptcy. - The pledge has not been perfected so as to be enforceable against a hypothetical judicial lien creditor and withstand the strong-arm clause in bankruptcy, as a result of which bondholders will not enjoy the benefit of the absolute priority rule in a plan of adjustment.	If facts peculiar to the transaction indicate that bondholders may not realize the benefits of a disclosed "pledge" of revenues (priority to the extent of pledged collateral) if the issuer becomes insolvent, consideration should be given to disclosing the risk factors, if material.
	Regulations may limit revenue or increase expenses and adversely	- Rate increases must satisfy a stipulated standard, or be approved	If payment of the bonds is supported by revenue from an existing or planned enterprise (e.g., airport,

Type of Securities	Risk	Example Risk Factors	Observations
	affect net revenues available to pay debt service.	by another governmental authority, or are otherwise limited by law. - The issuer must incur an estimated $X million in additional capital or annual operating expenses (or both) under a consent decree or to comply with environmental regulations. - Construction of the project has not yet received all regulatory approvals, and a delay in approvals could increase the cost of the project and delay its production of revenue. - Operation of the system must comply with specified regulations or licensure requirements, which could change and limit revenue or increase expenses in the future.	hospital, power plant) and regulations could affect completion of a revenue-producing project or otherwise affect net enterprise revenue, consideration should be given to addressing the regulatory regime and current status of regulatory oversight and compliance, if material.
General obligation bonds – General	The collection of sufficient taxes to pay debt service could be impaired if growth of the value of taxable property within the issuer slows or reverses in comparison to tax-supported debt and expenses.	- The rate at which the issuer may impose taxes to pay debt service is capped at a specified rate. - Tax rate increases may be reversed by referendum, which could preclude the issuer from being able to honor its obligation to levy a sufficient debt service tax. - The issuer's tax base must increase substantially to repay borrowings	Risk factor disclosure related to general obligation bonds will depend on the issuer-specific tax and debt issuance laws, and center around the process and the ability (or inability) of the issuer to increase tax rates to generate sufficient revenues to pay debt service on the particular series of bonds being issued and also all other outstanding general obligation bonds.

Type of Securities	Risk	Example Risk Factors	Observations
		to finance issuer infrastructure, which is subject to specified risks. - A major taxpayer or employer has discontinued operations within the issuer, or the value of taxable property is dependent on future coal mining or oil and gas production, which may be impaired by climate change regulation.	Risk factor disclosure may also depend on trends or developments relating to the maintenance or growth of the issuer's tax base and economic and demographic developments in the area.
General obligation bonds – Pension and Other Postemployment Benefits ("OPEB")	Future increases in pension and OPEB costs could increase future funding obligations and reduce revenue available to pay debt service.	- The issuer expects to have to increase annual contributions substantially to meet all expected plan costs. - The issuer has defined benefit plans that are currently underfunded. - The issuer recently increased salaries, or changed plan entitlements, or took other action expected to result in substantial future pension costs that are not reflected in the issuer's most recent financial statements. - The issuer is committed to, but does not, fund other post-employment benefits, which could rise substantially if healthcare costs and lifespans continue to increase at recent paces.	Pension and OPEB risk factors will depend on the type of plan, funding status and future contribution requirements, including any state statutory requirements relating to pension liability funding, as well as any recent changes that have not yet been reflected in the latest actuarial report.

Risks Related to a Particular Sector

Certain risks arise due to the particular type of issuer or type of project being financed. The table below provides illustrative examples of risks and risk factors related to selected sectors. Each sector is unique, and the table below is not meant to cover every possible sector or to list all common risks that they present.

Type of Sector	Risk	Example Risk Factors	Observations
Transportation	Certain revenues, such as toll revenues or airport landing fees, may decline or not increase sufficiently to pay operating expenses and debt service.	- Traffic has failed to grow as previously predicted due to increased remote work, and may not regain projected numbers if work at central places does not fully revive. - Governmental units have retained authority to improve and expand competing thoroughfares, which if exercised could draw traffic from the toll road. - Travel has slowed due to certain factors, which could permanently adversely affect business and leisure travel and could reoccur in similar or different forms with like effect.	Risks can vary depending on location, the type of project, the type of transportation sector (road, bridges, air, train), and the type of financing (revenue, general obligation, availability payments, etc.). Consideration also should be given to the issuer's particular economic and demographic trends in addition to relevant traffic trends. Additionally, to the extent the project being financed depends solely on revenues generated by traffic or use of the facility, consideration should be given to disclosing what happens when levels of traffic or use are not sufficient to generate such revenues – what mitigation measures, if any, are in place to ensure sufficient revenues?

Type of Sector	Risk	Example Risk Factors	Observations
Higher education	Applications for admissions and acceptances could decline or limit tuition growth to maintain admissions, in either case adversely affecting revenue available to pay operating expenses and debt service.	- Tuition has increased at a specified substantially higher rate than inflation in recent years. - State funding of higher education has declined at a specified substantial rate as a percentage of total expenses in recent years. - Students graduate with a specified average debt burden that compares unfavorably with the experience at competing schools. - The issuer competes with other schools in the area. - Attendance and dormitory occupancy and revenue have been adversely affected to a specified extent by the COVID pandemic, which could worsen or reoccur in a similar or different form. - Student applications, including by international students, has declined due to travel restrictions. - The issuer is dependent on gifts and distributions of endowment income to a specified extent, and financial market fluctuations may adversely affect endowment income, gifts and other funds available for debt service.	Higher education issuers face increasing pressure due to recent pandemic, increased costs, and a smaller rising generation. Issuers are having to change entire education models, adapt to remote and online learning modules, and create new ways to attract new students and keep current students. Risk factors could address risks associated with economic and demographic trends in student populations and any methods that management have undertaken to ensure or improve admissions and revenue generation, if material.

Type of Sector	Risk	Example Risk Factors	Observations
Healthcare	The highly-regulated healthcare industry could be adversely affected by changes in regulations or third-party payor practices, resulting in lower net revenues available to pay debt service.	- The issuer is subject to a wide variety of federal and state regulatory actions and legislative and policy changes by those governmental and private agencies that administer Medicare, Medicaid, and other payors and are subject to actions by, among others, accrediting bodies, the Centers for Medicare and Medicaid Services, the U.S. Department of Justice, State Attorneys General, and other federal, state, and local government agencies. - The future financial condition of the issuer could be adversely affected by, among other things, changes in the method and amount of payments to the issuer by governmental and nongovernmental payors, the financial viability of these payors, increased competition from other health care entities, the costs associated with responding to governmental inquiries and investigations, demand for health care, other forms of care or treatment, changes in the methods by which employers purchase healthcare for employees, capability of management, changes in the structure of how healthcare is	Healthcare issuers face a regulatory environment that is affected by political factors (e.g., healthcare reform) and market factors relating to the healthcare insurance industry. Risk factors should include specific recent or expected changes that are likely to affect the issuer's bottom line.

Type of Sector	Risk	Example Risk Factors	Observations
		delivered and paid for, future changes in the economy, demographic changes, availability of physicians, nurses, and other healthcare professionals, increased labor costs and malpractice claims and other litigation.	
Housing	Single family housing – defaults in underlying residential mortgages may adversely affect the issuer's ability to pay debt service.	- Residential mortgage markets have been adversely affected by changes in economic conditions leading to increased delinquencies in mortgage payments. - Prepayments of underlying residential mortgages may result in early redemption and historically have increased as prevailing interest rates decrease. - A downgrade in the credit rating of GNMA, Fannie Mae or Freddie Mac (i.e., the sovereign credit rating of the United States), likely would result in a downgrade on the bonds, if the underlying mortgage certificates are guaranteed by those entities.	Both single family and multifamily housing bonds depend on individuals and families buying or renting homes or apartment units. Demographic and economic factors that fluctuate over time can have a significant effect on home purchase trends, mortgage default rates, rental rates and rental demand. New construction of multifamily housing may present a riskier investment given recent increases in materials and construction costs and supply chain limitations and resulting cost overruns.

Type of Sector	Risk	Example Risk Factors	Observations
	Multifamily housing – failure to construct and operate or manage an apartment complex on time and within budget may adversely affect the ability of the issuer to generate net cash flow and make debt service payments.	- Failure to complete construction of new apartment complexes on time and on budget will delay the receipt of net revenue needed to pay debt service. - The bonds are payable only from net revenues generated by the project. - Multifamily occupancy rates in the area are at a specified level, or other projects have been announced, which could adversely impact the issuer's ability to fill the building once completed at levels sufficient to provide net revenue to pay debt service. - The issuer's ability to generate revenues depends on its ability to locate and rent to eligible tenants.	

Appendix B

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