

Underwriter's Counsel Roundtable Intermediate

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OCTOBER 18–20, 2023

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Overview of Session

Setting and managing expectations

Role of underwriter

Rules Governing Conduct and Obligations of Underwriter

2012 SEC Risk Alert

Conduct “Due Diligence”

Underwriter as “Gatekeeper”

Who is your client and conflicts of interest

Role of underwriter’s counsel

Traditional Roles

SIFMA Model Memorandum to Underwriter's Counsel

Due Diligence



Setting and Managing Expectations

- Establish expectations early
- Outside counsel roles and responsibilities
- Role of in-house counsel
- Managing conflicts of interest
- Contents of engagement letter or memo to underwriter's counsel
- Does the engagement documentation include scope of due diligence and opinion responsibilities?
- Does the issuer and/or borrower understand underwriter's counsel role (e.g. devil's advocate?)



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Role of Underwriter

Statutory and regulatory requirements

- Section 17(a) of the 1933 Act
- Section 10(b) of the 1933 Act
- Rule 10b-5
- Section 15(c) of the 1934 Act
- MSRB Rule G-17




SEC Releases

Case Law

Role of Underwriter

SEC Risk Alert – Strengthening Practices for the Underwriting of Municipal Securities (March 2012)



National Examination Risk Alert

By the Office of Compliance Inspections and Examinations¹

In this Alert:

Topic: Duties of broker-dealers engaged in municipal underwriting.

Key Takeaways:

Examiners have observed that some broker-dealers have not maintained, nor did they require the maintenance of, adequate written evidence that they complied with their obligations under Securities Exchange Act Rule 15c2-12 and applicable Commission guidance regarding due diligence and supervision.

This Alert provides a number of examples of effective practices

Volume II, Issue 3 **March 19, 2012**

Strengthening Practices for the Underwriting of Municipal Securities

Background

In the aftermath of the 2008 financial crisis and related economic turmoil, there is greater awareness of the financial vulnerabilities faced by state and local governments. Thus, a current focus of the Commission's National Examination Program ("NEP") is the potential risk to investors in the municipal securities markets. Due to these potential risks, the staff believes it appropriate to examine a range of broker-dealers' municipal securities underwriting activities.

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Role of Underwriter

“In its examinations, the NEP [SEC’s National Examination Program] staff has observed that some broker-dealers may not be engaging in the type or extent of due diligence activities discussed in the Commission’s guidance on the subject. In addition, the NEP has observed instances where municipal underwriters have not maintained, nor did they require the creation and maintenance of, adequate written evidence that they complied with their due diligence obligations, including those under Rule 15c2-12 and applicable Commission interpretive guidance.”

Risk Alert confirmed due diligence as a significant examination focus by the SEC and created a de facto legal requirement that underwriters prove in writing that they performed appropriate due diligence; otherwise it is as though such due diligence didn’t happen.

Role of Underwriter - Gatekeepers

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

-1988 Release by SEC

“Underwriters are critical gatekeepers relied upon by investors to ensure that accurate information is being provided in municipal bond offering documents.”

- Andrew M. Calamari, Director of the SEC’s New York Regional Office, Press Release 2017-77 (April 5, 2017)



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Who is your Client and Conflicts of Interest

In transactions with more than one underwriter identifying the client may be a matter of firm or attorney practice, or of negotiation with the underwriter(s).

The client may be considered the underwriting syndicate as an entity, the managing underwriters or only the senior managing underwriter.

Ideally, the client identification is confirmed in an engagement letter at the beginning of the representation.

All clients of underwriter's counsel may not be identified at the beginning of a transaction, underwriter's counsel may need to address conflicts of interest well after commencement of work on the transaction.



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Role of Underwriter's counsel

Traditional Roles of Underwriter's Counsel

- Advise the underwriter regarding the rules promulgated by the MSRB e.g., MSRB G-17 letters
- Assist the underwriter in conducting its due diligence investigation
 - Review compliance with ongoing disclosure undertakings
 - Review financial statements, underlying security documents, source of credit and security, board minutes
 - Due diligence checklists, memos and calls
- Engage auditors in the deal planning early on
- Draft or review a preliminary official statement (or similar offering document)
- Deliver a 10b-5 assurance letter in connection with the offering document
 - See Model Letter of Underwriters' Counsel (NABL, June 2017)
- Draft a bond purchase agreement
- Draft a Continuing Disclosure Agreement
- Draft Deemed Final Certificates
- Draft Agreed Upon Procedures Letter
- Check that pre-conditions to closing set forth in the bond purchase agreement are satisfied
- Prepare a "blue sky" memorandum
- Review investor presentations
- Review bond documents, closing documents and opinions



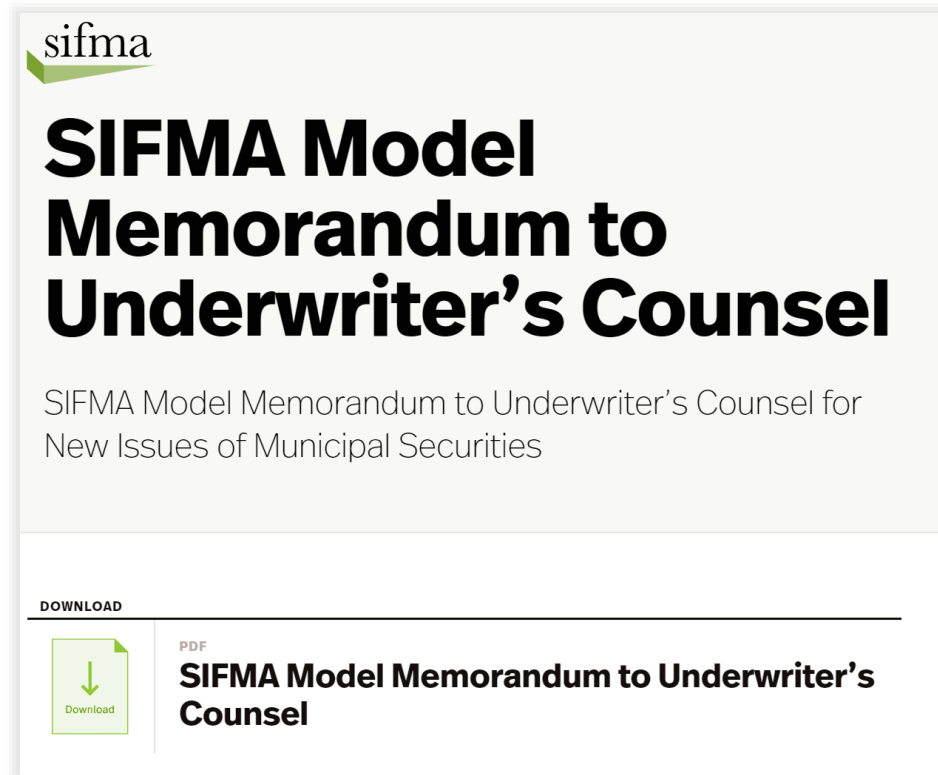
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Role of Underwriter's counsel

Model Memorandum to Underwriter's Counsel, SIFMA, 2018



The screenshot shows a document download interface. At the top left is the SIFMA logo. The main title is "SIFMA Model Memorandum to Underwriter's Counsel" in large, bold, black font. Below the title is the subtitle "SIFMA Model Memorandum to Underwriter's Counsel for New Issues of Municipal Securities" in a smaller, regular font. A horizontal line separates the title area from the download section. Below the line, on the left, is a green square icon with a white downward arrow and the word "Download" underneath. To the right of the icon, the text "PDF" is displayed in a small font, followed by the title "SIFMA Model Memorandum to Underwriter's Counsel" in a larger, bold font.

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Due diligence

- Not defined in federal securities laws
- Shorthand reference to conduct and procedures that, if followed, could establish an affirmative defense against a claim that the underwriter was negligent or intentionally fraudulent
- Do interpretations suggest a “due diligence” obligation or is it just part of the underwriter’s duty to have a “reasonable basis” for belief in the key representations of the offering document before underwriting the offering?
- Goals
 - “Kick the tires”
 - Review underlying basis for tax-exempt status of bonds?
 - Confirm material compliance with prior ongoing disclosure undertakings
- Conducting due diligence
 - Goal is to conduct a “reasonable investigation”
 - Checklists, document review calls, document request memos, final due diligence call, site visit
 - Other ideas?
 - Pros/cons of each?



Due diligence – Specific considerations

Rule 15c2-12 compliance

- Conduct independent review, hire outside consultant, or other?
- Review filings on EMMA to determine compliance
- Due diligence of listed events 15 and 16
 - Identifying material financial obligations:
 - Notes to financial statements
 - Due diligence requests
 - Ask for all financial obligations or only material financial obligations?
 - How do you determine whether any events have occurred that reflect financial difficulty?
 - Are policies/procedures in place addressing listed events 15 and 16?

Other considerations

Practice tips

- Direct, clear and ongoing communication with underwriter about roles/responsibilities (including those with in-house counsel), due diligence status
- Not all engagements are the same
- Understand the law and legal developments relating to obligations of underwriters and how best to ensure that such obligations are met
- Assume SEC will knock on your door
 - Fashion your conduct and follow procedures to minimize such a risk
 - Assist underwriter in creation of a due diligence record that reflects such conduct and adherence to such procedures and conforms to underwriter's needs and expectations

Questions?

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