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Decade-Long Look-Backs May Be Needed For SEC's MCDC Program

By KYLE GLAZIER



Self-reporting will not automatically result in SEC action, Greenberg said

WASHINGTON — Issuers and underwriters may need to review 10 years of official statements to determine whether they violated their continuing disclosure agreement obligations to file annual financial and operating information by their self-imposed deadlines, securities law experts said Wednesday.

Lawyers with Orrick, Herrington & Sutcliffe explained the SEC's Municipalities Continuing Disclosure Cooperation initiative for issuers, underwriters, and obligors at a webinar presented by the firm and hosted by The Bond Buyer.

The MCDC, announced on March 10, allows issuers and underwriters to get favorable settlement terms if they voluntarily report, by Sept. 10, any time they offered bonds without disclosing failures to meet their continuing disclosure obligations. Under a provision of the SEC's Rule 15c2-12 on disclosure, an official statement must disclose anytime within the last five

years that the issuer failed to meet its annual financial and operating information filing requirement. The SEC has a five-year statute of limitations for seeking civil penalties.

Jeff Higgins, a managing director at the Los Angeles office of compliance and advisory firm BLX, said potential participants in the program would have to do 10-year look backs in some cases, because bonds offered five years ago in 2009 could have misleading official statements if there were disclosure failures in the five years before that. Robert Feyer, an attorney in Orrick's San Francisco office, said the program represents a "carrot and stick" approach by the SEC, offering issuers and underwriters the promise of reduced penalties if they cooperate, but the threat of an enforcement action with no mercy if they do not self-report disclosure failures and are later caught. Issuers would face negligence charges and no financial penalties while underwriters could be assured of a \$500,000 cap on financial penalties for even the largest deals. The program does not apply to individuals, who could still be charged and penalized if the SEC enforcement staff found it appropriate.

Feyer said the SEC is likely to be most concerned with issuers failing to file annual financial and operating documents by their self-imposed deadlines then selling bonds without disclosing that. It may be less concerned with issuers who fail to disclose a rating change, but emphasized that those should be corrected as soon as possible once found.

"If you find a lapse, you need to correct it," he said.

An issuer or underwriter interested in self-reporting has to make its own determination as to whether its

disclosure failures were materially misleading, said Elaine Greenberg, an Orrick attorney in Washington and former head of the municipal securities and public pensions unit at the SEC's Division of Enforcement. A bond insurer downgrade that was undisclosed might be misleading, or it might not. Panelists were also asked the materiality of filing annual financial and operating information a few days late, compared to a few months late.

"It depends on your circumstances," Greenberg said.

She added that issuers or underwriters could choose to play it safe, self-report, but add that they did not think the failure was material, Greenberg said, The SEC might agree that no action is warranted, she said.

"They will be triaging the reports," Greenberg said, suggesting the SEC may get so many voluntary reports that they will have to divide them up into groups of

those that are potentially serious disclosure failures and those there are not.

Market participants have suggested that the SEC should release further guidance on what level of omission is likely to be material, but the SEC historically has not been inclined to do so. The U.S. Supreme Court ruled in 1988, in *TSC Industries, Inc. v. Northway, Inc.*, that information is material if there is a substantial likelihood that a reasonable investor would either consider it important in deciding whether to buy or sell securities or view it as altering the total mix of information available.

SEC officials have not said whether more guidance might be forthcoming in the fewer than four months left in the program.