

Public Finance Advisory: Securities and Exchange Commission Adopts Amendments to Rule 15c2-12 Disclosure Requirements

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The Securities and Exchange Commission (the SEC) has adopted amendments to the Exchange Act Rule 15c2-12 (the “Rule”) relating to continuing disclosure requirements for municipal securities. The Rule requires that underwriters in a primary offering of municipal securities reasonably determine that an issuer of municipal securities or an obligated person has undertaken, in a written agreement or contract for the benefit of bondholders, to provide certain continuing disclosure information to the Municipal Securities Rulemaking Board (MSRB). The Rule amendments:

- eliminate certain exemptions for variable-rate demand obligations;
- expand the types of events issuers or obligated persons must undertake to disclose on a continuing basis;
- remove the qualification that certain events need be disclosed only if material; and
- require event notices to be filed no later than 10 business days after the applicable event occurs.

In addition, the SEC has provided additional interpretive guidance to assist underwriters in meeting their obligations under the federal antifraud laws.

The Rule amendments are effective December 1, 2010. The interpretive guidance is effective upon publication in the *Federal Register*. Continuing disclosure agreements entered into prior to December 1, 2010 are not subject to, and will not need to be modified or amended to comply with, the Rule amendments.

Variable Rate Demand Obligation Exemption Removed

Citing market changes such as increased issuance, trading volume, and outstanding dollar amounts, as well as the lack of market disclosure during the recent financial crisis, the Rule amendments remove the variable rate demand obligation (VRDO) exemption from the Rule’s continuing disclosure requirements. The Rule’s continuing disclosure requirements will now apply to both any initial offering of VRDOs and remarketings that are primary offerings² of VRDOs, occurring on or after December 1, 2010 (even if initially issued prior to December 1, 2010).

Expanded Disclosure of Certain Events

The existing Rule requires that issuers or obligated persons undertake to disclose certain events, “if material.” The Rule amendments remove the materiality limitation for the following events, in each case with respect to the securities being offered:

- principal and interest payment delinquencies
- unscheduled draws on debt service reserves reflecting financial difficulties
- unscheduled draws on credit enhancements reflecting financial difficulties
- substitution of credit or liquidity providers, or their failure to perform
- defeasances
- rating changes

Disclosure of Tax Events

The existing Rule only requires that issuers or obligated persons agree to file notices for adverse tax opinions or events affecting the securities’ tax exempt status, if material. The Rule amendments modify this provision to include the issuance by the Internal Revenue Service (IRS) of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB), or other material notices or determinations with respect to the tax status of the security, or other material events affecting the tax status of the security.

Additional Events to be Disclosed

The Rule amendments add four additional events for ongoing “event disclosure” (without regard to materiality, unless noted):

1. tender offers
2. bankruptcy, insolvency, receivership or similar event of the obligated person³
3. the consummation of a merger, consolidation, or acquisition involving an obligated person or the sale of all or substantially all of the assets of the obligated person, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material
4. appointment of a successor or additional trustee or the change of the name of a trustee, if material

Filing Date Deadline for Event Notices

Under the Rule amendments, an issuer or obligated person must agree to file event notices to the MSRB “in a timely manner, not in excess of 10 business days after the occurrence of the applicable event.” Currently the Rule only requires such filings “in a timely manner.”

Additional Interpretive Guidance

The SEC provided additional interpretive guidance regarding municipal underwriters' responsibilities under the antifraud provisions of the federal securities laws. Under the Rule, an underwriter is required to reasonably determine that the issuer or obligated person has undertaken, in a written agreement or contract for the benefit of the bondholders, to provide continuing disclosure documents to the MSRB. Furthermore, the Rule requires disclosure of any instances in the previous five years in which any person identified in the continuing disclosure agreement has failed to comply, in all material respects, with any previous informational undertakings in the continuing disclosure agreement. The SEC has previously stated that in fulfilling this obligation, the underwriters have a responsibility to review the issuer's or obligated person's disclosure documents in a professional manner with respect to the accuracy and completeness of statements made in connection with the offering.⁴

The SEC's additional interpretive guidance states that:

- If the underwriter finds that the issuer or obligated person has on multiple occasions during the previous five years, failed to provide continuing disclosure documents on a timely basis, as required by a previous continuing disclosure agreement, it would be very difficult for the underwriter to make a reasonable determination that the issuer or obligated person would provide such information for subsequent offerings; and
- It is doubtful that an underwriter could meet the reasonable belief standard without affirmatively inquiring as to the filings history and that such reasonable belief should be based on its independent judgment (including obtaining evidence reasonably sufficient to determine whether and when such filings and notices were, in fact, provided) and not solely on representations of the issuer or obligated person as to the materiality of any failure to comply with any prior undertaking.

Endnotes

¹ Full text and discussion of the SEC's Rule amendments and interpretive guidance can be found on the SEC's website at <http://www.sec.gov/rules/final/2010/34-62184a.pdf>.

² A "primary offering" means an offering of municipal securities directly or indirectly by or on behalf of an issuer of such securities, including any remarketing of municipal securities (i) that is accompanied by a change in authorized denomination of such securities from \$100,000 or more to less than \$100,000, or (ii) that is accompanied by a change in the period during which such securities may be tendered to an issuer of such securities or its designated agent for redemption or purchase from a period of nine months or less to a period of more than nine months. 17 CFR 240.15c2-12(f)(7)

³ For purposes of this provision, an event is considered to occur when any of the following occur: the appointment of a receiver, fiscal agent or similar officer for an obligated person in a proceeding under the U.S. Bankruptcy Code or in any other proceeding under state or federal law

in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the obligated person, or if such jurisdiction has been assumed by leaving the existing governing body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan of reorganization, arrangement or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets or business of the obligated person.

⁴ See Securities Exchange Act Release No. 26985 (June 28, 1989), 54 FR 28799 (July 10, 1989)

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