



August 2014

Finding the Time: SEC Announces Deadline Extension for MCDC Initiative

In this Issue:

For More Information 3

About Polsinelli's Public | Municipal Finance Practice 4

Since 1995, the SEC's Rule 15c-12 has, subject to a few exceptions, required the "post issuance" delivery of certain annual financial and operating information from parties that are obligated to provide for the repayment of tax-exempt bonds (the "Obligated Persons"). Obligated Persons also must provide notices of certain "notice events" within a short period of time after their occurrence. The particular requirements, including the content and timing of reporting and types of notice events, are specifically described in the Obligated Person's continuing disclosure undertaking ("CDU"), which is contained either within a separate document, or within one of the bond documents.

The MCDC is an offer to Obligated Persons and their underwriters to self-report possible violations of the antifraud provisions of the securities laws arising from materially inaccurate statements in offering documents ("Official Statements") relating to compliance with their continuing disclosure obligations and receive lighter penalties. Following is a link to the full text of the initiative: <http://www.sec.gov/divisions/enforce/municipalities-continuing-disclosure-cooperation-initiative.shtml>.

The MCDC follows on the heels of two 2013 administrative proceedings in which the SEC charged an issuer and its underwriter for violations of the antifraud provisions of the federal securities laws arising from misstatements about compliance with continuing disclosure undertakings.¹ In those proceedings, the issuer indicated in an offering document that it had complied in all material respects with its continuing disclosure obligations, when in fact it had never filed the annual disclosure reports required by its prior undertaking. The SEC also concluded that the underwriter conducted

¹ In the Matter of West Clark Community Schools, Securities Act Release No. 9436, Exchange Act Release No. 70057 (Jul. 29, 2013); In the Matter of City Securities Corporation and Randy G. Ruhl, Securities Act Release No. 9434, Exchange Act Release No. 70056, Investment Co. Act Release No. 30632 (Jul. 29, 2013).



inadequate due diligence and, as a result, failed to form a reasonable basis to rely upon the issuer's assertion of its past compliance.

The MCDC focuses on statements made by the Obligated Person in the offering documents ("Official Statements") regarding past compliance with CDUs and whether such statements, if incorrect, could be considered a violation of the anti-fraud provisions of the securities laws. Rule 15c2-12 under the Securities Exchange Act of 1934 provides that a "final official statement" must include a description of any instances in the previous five years in which an Obligated Person failed to comply, in all material respects, with any then-existing CDUs.

The SEC initially imposed a deadline of September 10, 2014 for all self-reporting under the MCDC. In view of the substantial burden of analyzing prior disclosures, numerous industry groups raised concerns with the SEC, urging the agency to extend the deadline, limit the broad scope of the MCDC, and consider its potentially unequal impact on Obligated Persons and underwriters.

On July 31, 2014, the SEC responded by extending the deadline for Obligated Persons to self-report potential violations, to 5:00 p.m., Eastern Time, December 1, 2014. The deadline for underwriters remains unchanged at midnight, September 10, 2014. With respect to underwriters, the SEC also implemented a tiered approach to the maximum potential civil penalties based on the size of the firm. The new tiered approach is:

- For underwriters with 2013 reported total annual revenue of more than \$100 million: \$500,000
- For underwriters with 2013 reported total annual revenue between \$20 million and \$100 million: \$250,000
- For underwriters with 2013 reported total annual revenue of less than \$20 million: \$100,000

Given that the MCDC provides that the financial penalties for underwriters cannot exceed certain amounts based on the

size of the firm, underwriters may have an incentive to disclose all identified instances of an Obligated Person's noncompliance, whether or not material, to resolve any question of the underwriters' liability for failure to conduct reasonable due diligence regarding the Obligated Person's compliance with prior CDUs. Obligated Persons may wish to ask their underwriters to inform them of any self-reporting by such underwriters that concerns the Obligated Person, in order to assist with its own review and compliance.

Recently the SEC announced its first case under the MCDC, in which it entered into a settlement with Kings Canyon Joint Unified School District, in California. Many observers have lamented that the settlement omits description of the specific instances of non-compliance. Therefore, Obligated Persons and Underwriters should not expect to receive any additional specific guidance from the SEC in determining whether material misstatements have been made in the Official Statements that are under review in connection with the MCDC.

Notably, the MCDC covers only Obligated Persons and underwriters. Individuals are not covered by any settlements agreed to pursuant to the MCDC, although the SEC has indicated that its assessments as to whether to recommend enforcement action against individuals, will include case-by-case evaluations of the facts and circumstances, including individual intent and cooperation.

In its recent announcement of the amendment to the MCDC, the SEC indicated that it has learned that some underwriters and Obligated Persons have experienced difficulties in identifying potential violations for periods when filings were made in the Nationally Recognized Municipal Securities Information Repository ("NRMSIR")



real challenges. real answers. SM



system, which pre-dated the current Electronic Municipal Market Access (“EMMA”) system. The amendment represents the SEC’s recognition that parties may use reasonably available sources of information to make good faith efforts to identify potential violations, but may not be able to identify certain violations during the period of the MCDC due to the limitations of the NRMSIR system. This acknowledgment by the SEC of the limitations inherent in searching the now-defunct NRMSIR system should afford some comfort to those who are contemplating participating in the MCDC. If violations are identified by the SEC after the expiration of the MCDC, the SEC has stated that a showing of reasonable, good faith, and documented efforts to find information regarding past non-compliance will affect the SEC’s decision whether to recommend enforcement action and, to the extent enforcement action is recommended, the level of relief.

An organization participating in the MCDC would enter into a “cease and desist proceeding” with the SEC, and among other things, would be required to (1) establish compliance policies and procedures, (2) disclose its settlement with the

SEC for the next five years in offering documents, (3) cooperate with the SEC on any subsequent investigations, (4) correct any prior non-compliance, and (5) provide a compliance certificate to the SEC.

If your organization has benefitted from the issuance of tax exempt bonds, and participated in the preparation of any Official Statements between 2009 and 2014, you should carefully review the disclosure included in those Official Statements to determine whether that disclosure adequately described your prior compliance with your CDUs. If the disclosure was inaccurate, you should discuss with counsel whether the misstatement could be viewed by the SEC as “material” and whether your organization should participate in the MCDC to resolve any potential federal securities law liability. Whether or not your organization elects to participate in the MCDC, identifying any prior instances of non-compliance enables you to make corrective filings and to identify any gaps in your current disclosure policies and compliance procedures.



For More Information

If you have questions regarding this alert, please contact:

- Dana Lach | 312.873.2993 | dlach@polsinelli.com
- Lisa Greer Quateman | 310.203.5303 | lquateman@polsinelli.com
- Timothy J. Reimers | 310.203.5316 | treimers@polsinelli.com
- Jessica Zaiger | 816.572.4419 | jzaiger@polsinelli.com
- Janet Zeigler | 312.873.3679 | jzeigler@polsinelli.com

To contact another member of our Public | Municipal Finance team, click [here](#) or visit our website at www.polsinelli.com > Services > Public | Municipal Finance > Related Professionals.

To learn more about our Public | Municipal Finance practice, click [here](#) or visit our website at www.polsinelli.com > Services > Public | Municipal Finance.



real challenges. real answers. SM



About Public | Municipal Finance Practice

Polsinelli's Public Finance attorneys have a reputation built on innovative work in a wide range of projects financed with public securities for municipal or private borrowers. We regularly serve in all the principal public finance capacities, including as bond, disclosure, borrower's, underwriters' and trustee's counsel in connection with the issuance of billions of dollars of public securities and hundreds of financings for states, cities, local agencies, borrowers, investment banks and trustees.

We are known for understanding our clients' business and having a deep knowledge of the industry we serve, as well as strong working relationships with major public finance market participants and extensive experience with a variety of sophisticated transactions.

About Polsinelli

real challenges. real answers.SM

Polsinelli is a first generation Am Law 100 firm serving corporations, institutions, entrepreneurs and individuals nationally. Our attorneys successfully build enduring client relationships by providing practical legal counsel infused with business insight, and with a passion for assisting General Counsel and CEOs in achieving their objectives. Polsinelli is ranked 18th in number of U.S. partners* and has more than 740 attorneys in 19 offices. Profiled by *The American Lawyer* and ranked as the fastest growing U.S. law firm over a six-year period**, the firm focuses on healthcare, financial services, real estate, life sciences and technology, energy and business litigation, and has depth of experience in 100 service areas and 70 industries. The firm can be found online at www.polsinelli.com. Polsinelli PC. In California, Polsinelli LLP.

* Law360, March 2014

** The American Lawyer 2013 and 2014 reports

About this Publication

Polsinelli provides this material for informational purposes only. The material provided herein is general and is not intended to be legal advice. The choice of a lawyer is an important decision and should not be based solely upon advertisements.

Polsinelli PC. In California, Polsinelli LLP.

