INTERNATIONAL MUNICIPAL LAWYERS ASSOCIATION

2011 Annual Conference

Chicago, IL

Tuesday, September 13, 2011

Work Session VII

"Municipal Finance from Bankruptcy to Disclosure"

"Issuer Disclosure Procedures"

By Robert Doty

AGFS, Sacramento

© International Municipal Lawyers Association.

This is an informational and educational report distributed by the International Municipal Lawyers Association during its 2011 Annual Conference, held September 11-14, 2011 in Chicago, IL. IMLA assumes no responsibility for the policies or positions presented in the report or for the presentation of its contents.

This presentation reviews issuer disclosure requirements and potential internal policies and procedures that municipal securities issuers and their governing boards and officials may consider and implement to enhance their protections in securities issues. The discussion will include practical ways for local government attorneys to assist in—

(1) identifying and collecting the needed information for new issue disclosure,

(2) ferreting out possible "material omissions," and

(3) drafting effective disclosure

SEC ACTIONS AFFECTING ISSUERS & OFFICIALS—EXAMPLES

- New Jersey
- San Diego
- San Diego Officials
- Miami & Officials
- Maricopa County
- Syracuse
- Orange County, Board of Supervisors & Officials

POTENTIAL STEPS FOR GOVERNING BOARDS

NOTE: There are no standards. The following are discussion points.

- Adopt resolution/ordinance to establish a Disclosure Group and define its responsibilities and authority
    - Affirm issuer's continuing commitment to provide accurate and complete disclosure, as required by SEC Rule 10b-5 and Section 17(a) of the 1933 Act
    - Establish Disclosure Group's responsibilities for developing and implementing issuer's written disclosure policies and procedures ("DP&P")
    - Designate key senior staff to be members of Disclosure Group and give them "clout" to obtain cooperation from other staff
    - Direct Disclosure Group to develop written DP&P for recommendation to governing board

- Provide adequate funding for Disclosure Group, including qualified legal and financial professionals, as appropriate

- Approve DP&P

- Direct Disclosure Group to follow and implement DP&P and direct other staff to cooperate with, and to respond to requests of, Disclosure Group

- Employ qualified legal & financial professionals to assist and advise Group

- DP&P should include:

  - Definition of documents, in addition to official statements, to be reviewed and approved by Disclosure Group, such as official statements, investor information page on issuer's website, rating agency presentations, and continuing disclosure filings [SEC's position (discussed below) is that any information intended for investors is included in issuer's Rule 10b-5 responsibilities]

  - Training for staff on disclosure

  - Clear lines of responsibilities as to which officials must review and approve disclosure documents on behalf of issuer

  - Periodic evaluation of DP&P by Disclosure Group

  - Procedures for ensuring disclosure of material information known to members of governing board, *e.g*., procedures for providing reasonably final drafts of disclosure documents to members of board with time to review and comment

- Evaluate DP&P

- Revise DP&P as appropriate

  - Follow DP&P for all disclosure documents [Potential problems if do not substantially follow DP&P and there is investigation into adequacy of disclosure]

POTENTIAL STEPS FOR KEY ISSUER OFFICIALS

- Disclosure Group should perform all tasks contained in the issuer's Disclosure Policies & Procedures ("DP&P")

- Disclosure Group should review all disclosure documents (initial offering & continuing)

  - Do NOT simply "mark-up" the last disclosure document

- For each offering, develop a plan for disclosure based upon sources of payment and security for payment of securities offered and current material facts and circumstances affecting those sources, securities and the issuer

- Hold working review sessions to review draft disclosure documents page by page

- Seek input from qualified legal & financial professionals

- If issuer does not request or receive consent of auditors to include their audit reports, disclose that no consent was requested or received and no subsequent events review was conducted. This is especially significant for "stale" financial statements (*e.g.*, more than six months old.

- Train key employees on disclosure responsibilities

- For consistency, designate a central knowledgeable party through whom information flows, especially in communications, if any, with analysts

- Ensure disclosure of known material information for securities offered

- Ask questions & substantiate information

- Verify information from original sources

- Check specific information with knowledgeable staff (*e.g.*, insurance information with insurance staff, pension information with pension administrator, employee information with human relations staff, litigation and risk management with lawyers, and overall "problems"/"challenges" with senior management)

- If relying on professionals, pay attention to required steps for reliance (see below)

- DP&P should require representations & certifications from senior staff of issuer on information in disclosure documents for which they are responsible

- DP&P should also require written representations and certifications of information provided by third parties to issuer for inclusion in disclosure document

- If third parties provide information, identify it clearly as such; do not use information from third parties who may not be reliable

- If third parties providing information have interest in the transaction, clarify information, review supporting documentation, ask questions, & disclose the interest

- Seek representations & certifications regarding expert work products (financial feasibility studies and projections, appraisals)—meet with experts to review & discuss; understand the experts' qualifications, independence, use of professional standards, professional opinions regarding reasonableness of assumptions, etc.

- Read, question, confirm and understand draft disclosure document and determine it is accurate and complete, before recommending approval to governing body for distribution to potential investors

FORMAL RELIANCE ON PROFESSIONALS

The Administrative Law Judge in *In the Matter of the City of Miami,* SEC Initial Decision Rel. No. 185 (June 22, 2001), *aff'd* by the Commission, SEC Rel. No. 33-8213, 34-47552 (March 21, 2003), enumerated elements for justifiable reliance on advice of professionals (in the *Miami* action, reliance by the City upon auditors):

> To establish a good faith reliance defense based on the advice of an accountant or an attorney, one must show that she **(1)** made complete disclosure, **(2)** sought the advice as to the appropriateness of the challenged conduct, **(3)** received advice that the conduct was appropriate, and **(4)** relied on the advice in good faith. … The City has not satisfied those elements. …

In the view of the Judge, Miami failed to establish a basis for reliance because, among other things, the auditors relied on the City for information, not the reverse; the City did not make full disclosure to the auditors; the City had not asked for specific advice; and the City had failed to act in good faith—

> Most important, when it took these actions in late March, June, August, and December 1995, the City knew that the information it was providing investors and potential investors did not fully and accurately describe its financial situation at those particular times. It is well-settled case law that a person cannot claim reliance on another when the person knowingly makes fraudulent statements and intentionally omits information about material subjects.

WEBSITES & POST-ISSUANCE COMPLIANCE

NOTE: These subjects are beyond the scope of this presentation, but you should be aware that they are important matters on which local governments should seek professional guidance.

OTHER SOURCES

IMLA Draft Financing Procedures Checklists (2007)

GFOA, "Pocket Guide"—Questions to Ask Before You Approve a Bond Issue (1996)

NFMA Best Practices in Disclosure & White Papers at www.nfma.org

GFOA Best Practices at www.gfoa.org

NABL, Pending Pension Disclosure Project