

■ SECURITIES DISCLOSURE: PROTECTING YOUR LOCALITY'S GOOD NAME IN THE MARKET

You have been preparing your local government for an upcoming bond sale. The offering document is nearly complete, and everything is in place for a successful sale . . . or so you think. Shortly before the bonds are to be sold, the underwriter calls to inform you, as the representative of the issuer, that the underwriting firm will not be able to purchase the bonds.

The firm has concluded that doing so would violate the securities laws because it has reason to believe that your local government will not comply with future continuing disclosure undertakings. It has contacted the NRMSIRs,¹ nationally recognized municipal securities information repositories, and discovered that you have failed to make certain information filings required for a previous bond issue.

Could this happen to you? With continuing disclosure, or the lack thereof, coming under scrutiny by the Securities Exchange Commission (SEC) in recent years, this scenario could possibly become reality for some issuers if they do not take proper steps to ensure their compliance with existing continuing disclosure obligations.

In 2002, the SEC completed a study on continuing disclosure with respect to some 30 municipal transactions. The results of the study reported in *The Bond Buyer*² showed that the NRMSIRs had only 57 percent to 75 percent of the disclosure documents that were required to be filed for these issuers; many of the missing documents were simply not filed by issuers, while other documents had been filed but were misplaced or misfiled by the NRMSIRs.³

In the same year, a similar study conducted by the National Federation of Municipal Analysts revealed that almost 41 percent of the 105 borrowers surveyed did not provide complete in-

formation in the disclosure documents submitted.³

These studies are of interest because, under SEC Rule 15c2-12(b)(5) (the "Rule"), underwriters may not buy or sell municipal securities unless the underwriter has *reasonably determined* that an issuer of such securities will make continuing disclosure of certain financial and operating information after issuing the securities.

The SEC has interpreted the Rule to require an underwriter to investigate and verify an issuer's representation that it will provide continuing disclosure, to the extent that the underwriter can form a "reasonable basis to believe that the representations are true and accurate."⁴

If local governments are not satisfying continuing disclosure obligations covering previous transactions, is it reasonable for underwriters to believe that these localities will satisfy their obligations in future transactions? If the answer is no, then underwriters are not legally permitted to buy their bonds.

With scrutiny by the SEC on the rise, the underwriters of municipal bonds are feeling more pressure to make informed determinations of whether an issuer will comply with future continuing disclosure undertakings. In making these determinations, underwriters will most likely contact NRMSIRs to verify that issuers have met their filing obligations under previous continuing disclosure undertakings.

There are several steps that an issuer can take to prevent continuing disclosure problems from arising and affecting the marketability of its bonds. The most important step is to file continuing disclosure documents! Filing requirements may be satisfied by submitting information to each NRMSIR (and state repository, if applicable) or by making a single submission of information to DisclosureUSA. More information on DisclosureUSA can be found at www.disclosureusa.org.

Managers can take steps to ensure that annual filing deadlines are not missed and also can read any continuing disclosure undertaking(s) to learn

about other circumstances that may require additional filings.

A record of each filing should be kept so that if one document is misplaced or misfiled by the NRMSIRs, evidence is available of the attempt to satisfy filing obligations. To help avoid misfilings, it is important to include a description of the securities to which the filing applies (especially CUSIP numbers) with the disclosure documents.

Endnotes

¹A list of NRMSIRs can be found on the Web site www.sec.gov/info/municipal/nrmsir.htm.

²Lynn Hume, "SEC Scrutiny of Dealers May Rise," *The Bond Buyer* (May 10, 2002), at 1; Lynn Hume, "SEC, NFMA: Many Issuers Fail to Meet Disclosure Obligations," *The Bond Buyer* (June 18, 2002), at 1.

³National Federation of Municipal Analysts press release dated May 23, 2002, at www.nfma.org/publications/disclosure_survey.pdf.

⁴Municipal Securities Disclosure, Exchange Act Release No. 34-34961, *Federal Register*, Vol. 59, No. 221, at 59590 (November 10, 1994).

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