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SEC's Proposed Disclosure Amendments Criticized as too Costly, Burdensome.

PALM BEACH GARDENS, Fla. – The Securities and Exchange Commission's proposed amendments to its Rule 15c2-12, which would create numerous new disclosure obligations for issuers, received more criticism on Thursday as market participants noted a lack of specificity in them and the burdens and costs that they would impose on issuers.

Members of the bond community made their comments during various panels and speeches at The Bond Buyer and Bond Dealers of America National Municipal Bond Summit here.

Ben Watkins, Florida's director of bond finance, during a luncheon speech that touched on regulation generally, as well as the amendments, said that the regulators don't "fully appreciate the costs and burdens they impose on the market."

"From my perspective, the regulatory creep is like kudzu in the South in the summer, it continues perpetually," he said, specifically singling out the SEC's Municipal Advisor Rule, the Municipalities Continuing Disclosure Cooperation initiative, and the recently proposed 15c2-12 amendments.

He added that investment banks "are now an elaborate front for compliance departments" because "they're not free to bank anymore" given the regulations imposed in recent years.

"So much time, effort, and energy goes into compliance that that diverts resources that would otherwise be available to deliver intellectual capital and solutions to the issuer community and for the benefit of the market as a whole," Watkins said.

The proposed amendments to 15c2-12 are designed to achieve a goal most municipal participants have supported – helping rating agencies, analysts and others obtain information about bank loans, private placements and other alternatives to publicly offered tax-exempt bonds that issuers and borrowers are increasingly using that fall outside the current 15c2-12 disclosure requirements.

The first new material event notice category would require an issuer or borrower to file a notice if they incur a financial obligation that is material or a financial obligation has an agreement to covenants, events of default, remedies, priority rights or similar terms "any of which affect securities holders, if material." The SEC has consistently declined to define materiality, contending it's based on facts and circumstances, but the Supreme Court has said a fact is material if there is a substantial likelihood that a reasonable investor would consider it important.

Financial obligations are defined as "a debt obligation, lease, guarantee, derivative instrument or a monetary obligation resulting from a judicial, administrative or arbitration proceeding."

The second new material event category would require a notice to be filed for certain actions or events related to the financial obligation that "reflect financial difficulties" such as a default, event of acceleration, termination event, or modification of terms.

Underwriters would have to reasonably determine that an issuer or borrower has agreed to provide notice of such events in its continuing disclosure agreement (CDA). The proposed amendments, if adopted would apply to CDAs entered into in connection with primary offerings occurring on or after the compliance date for the amendments.

Watkins said that it would be best for the SEC to be specific and "give clear and narrow rules that people can follow rather than saying 'all material financial obligations.'"

The broad definition of material financial obligations puts everyone in the position of wondering what the SEC is talking about and what they need to do, Watkins said.

"You spend your time, effort, energy, and money focused on that rather than complying with the rule," he added.

Jessica Kane, director of the SEC's Office of Municipal Securities, said on a panel before Watkins' speech that the new amendments would use the definition of materiality in the same way it is used in the 14 event notices that are already included in 15c2-12. She added that the determination of what is material is something that an issuer or obligated person is in the best position to make based on the relevant elements and circumstances at the time.

Kane said that the SEC expects materiality "is a concept that issuers are familiar with and know how to apply."

Guy Yandel, executive vice president and co-manager of George K. Baum & Company's muni division, participated on Kane's panel and said he thinks the issue of materiality would be "a little different" in the two new event notices if they were approved.

"In all of the 14 previous events, we could counsel our clients that they shouldn't try to make a materiality call, they should just say what they did," Yandel said. "With these, it's a little more difficult because if you were to try to do that, you'd be uploading garbage contracts that municipalities enter into and I don't think that is the intent."

He added that means issuers are no longer going to be able to fall back and say 'we're just going to disclose everything' but will instead have to make a materiality determination.

Kane encouraged industry comments on the proposed amendments at various times during the panel and specifically pointed out that the amendments' proposing release asks a number of questions about whether the definition of financial obligations is the right definition with the right scope.

Watkins said the Government Finance Officers Association will be commenting on the proposal, adding that, in his view, voluntary industry initiatives and best practices coupled with collaborative efforts among stakeholders is "the best way to go" and should precede regulation and enforcement.

However, the SEC and others like financial analysts are still concerned about a lack of information despite past collaboration, GFOA best practices, and other efforts from market participants and regulators to increase voluntary bank loan disclosure.

Bill Oliver, industry and media liaison for the National Federation of Municipal Analysts, said during a separate panel on Thursday that he thinks the SEC generally did "a pretty good job in terms of defining concerns that credit analysts have in terms of disclosing financial obligations that have an impact on how you calculate debt ratios and also the effect on existing bondholders."

NFMA sent a letter to the SEC in August 2016 urging changes to Rule 15c2-12, including expanding

the list of material events to include bank loans and other debt obligations.

The Bond Buyer

By Jack Casey

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