
House Financial Services Municipal Bonds Market Hearing.

House Financial Services Subcommittee on Oversight and Investigations

Examining the Role of Municipal Bond Markets in Advancing and Undermining Economic, Racial and Social Justice

Wednesday, April 28, 2021

Witnesses

- William Fisher, Chief Executive Officer, Rice Capital Access Program
- Gary Hall, Partner and Head of Investment Banking (Infrastructure and Public Finance), Siebert Williams Shank & Co., LLC
- Chelsea McDaniel, Senior Fellow, Activest
- Jim Nadler, Chief Executive Officer, Kroll Bond Rating Agency
- Chris Parsons, Professor of Finance, University of Southern California

Opening Statements

Chairman Al Green (D-Texas)
In his opening statement, Green said the hearing will assess the municipal bond markets as a driver of discrimination and examine material disparities and the cost of capital raising for Historically Black Colleges and Universities (HBCUs). Green said this hearing will show how the municipal bond markets can also drive positive change and fiscal justice. He mentioned research that shows HBCUs, on average, face higher fees when compared to similarly situated non-HBCUs. He said the disparities in fees were attributable to racial discrimination and that the cost disparities were magnified in states where anti-Black racial resentment is the most severe. Green said all of these findings are deeply personal and profoundly troubling and noted that he looks forward to discussing solutions.

Ranking Member Andy Barr (R-Ky.)
In his opening statement, Barr said the municipal bond markets provides a reliable source of capital and a stable avenue for investors to put their money to work for the public good. He added that the muni market is a strong way for issuers to finance their operations. He continued that the pandemic weighed on the economic wellbeing of states and localities as typical sources of revenue declined. To respond, he said Congress established the Municipal Liquidity Facility (MLF), and shortly thereafter, the muni market stabilized. Barr said everyone can agree our infrastructure needs improvement and that municipal bonds are a key source for financing those plans. He said significant tax increases would not help, rather we should look for ways to incentivize and mobilize private capital. Barr said he hopes to find a way to improve the municipal bond market and ensure equitable access for issuers, specifically highlighting the importance of restoring the ability of issuers to advance refund tax-exempt municipal debt. He said discrimination in the municipal bond market is illegal and should

not occur, and hopes the Committee works to ensure this does not persist.

Testimony

William Fisher, Chief Executive Officer, Rice Capital Access Program

In his testimony, Fisher said HBCUs play a vital role in higher education that is not easily recognized or appreciated by the capital markets, and that the lack of understanding forces higher interest rates which cause investments in physical facilities, student support initiatives, and academic programs to suffer. He added that the negative impact of expensive debt impacts not only the institution and its students, but the local community as well. Fisher applauded the creation of the HBCU Capital Financing Program as a tool for providing access to low cost borrowing and creating a path to financial stability. He urged consideration of the HBCU Capital Financing Advisory Board's recommendations to increasing the borrowing capacity of the Program and expand the use of the program to include operating lines of credit. He said these provisions would further secure the HBCUs' "place" in America and higher education.

Gary Hall, Partner and Head of Investment Banking (Infrastructure and Public Finance), Siebert Williams Shank & Co., LLC

In his testimony, Hall explained his career in the municipal bonds market having served as an issuer, lawyer, and banker. He also emphasized his firms' and his personal longstanding connections with HBCUs as an alumnus, parent, and benefactor. He emphasized that municipal bonds are a critical funding source for infrastructure in America for bridges, roads, schools, health care facilities, higher education facilities, airports, and seaports our communities rely on. Hall also thanked the Congress for their decisive action in passing the CARES Act and authorizing the Federal Reserve's Municipal Liquidity Facility, stating that this swift action helped stabilize the tax-exempt market last March during a period of heightened market stress. Hall said that after decades of underinvestment, the entire U.S. faces an extraordinary infrastructure deficit, if which this trend continues, will only lead to additional delays of investment in and maintenance of critical public projects. He added that the "burden of crumbling infrastructure" will fall disproportionally on low-income and minority communities. While he raised questions regarding the data and methodology underpinning Parson's study, Hall added that there is certainly more that can be done to assist HBCUs with accessing the capital markets more cost-effectively going forward. Specifically, he noted SIFMA's support for authorizing triple tax exemption for HBCU-sponsored debt. Hall continued by outlining additional SIFMA-supported policies that would help provide incentives to rebuild the nation's infrastructure such as: 1) preserving the tax exemption for interest earned by investors on state and local bonds; 2) reinstating the tax exemption on the advance refunding of municipal bonds; 3) expanding private activity bonds (PABs); 4) reinstating a direct pay bond program; and 5) expanding the small issuer exception so that states and municipalities have a variety of additional tools to finance their local projects. He commended the work of the Subcommittee and encouraged lawmakers to consider the previously suggested proposals. Hall concluded by commending the work of the Subcommittee, encouraging lawmakers to consider these proposals, and reiterating SIFMA's and its members' commitment to fostering not only a culture of diversity and inclusion within our industry, but also investing in diverse communities nationwide and increasing the availability of financing for critical local infrastructure projects.

Chelsea McDaniel, Senior Fellow, Activest

In her testimony, McDaniel said she plans to present a high level sectoral view of postsecondary education institutions in the context of the larger municipal finance market. She noted that as a result of longstanding policies born out of the segregation era, there have been social and environmental risks emerging within public entities, like local governments and schools. McDaniel stressed that these need to be updated. She continued by saying the cost of ignoring these fiscal justice risks is growing within government entities. She noted three examples of the growing materiality: predatory inclusion in higher education loans, outsized pricing among HBCU bonds, and postsecondary schools "racing" to become federally recognized Hispanic-Serving Institutions (HSIs) to capitalize off the growing Latinx student population. Finally, McDaniel said that from a credit perspective, Minority-Serving Institutions (MSIs) are much stronger municipal investments than Predominantly White Institutions (PWIs) and recommended three solutions to counter the fiscal justice risks in the postsecondary market: accounting for equity research, social justice bonds, and investment in physical assets.

Jim Nadler, Chief Executive Officer, Kroll Bond Rating Agency
In his testimony, Nadler began by saying ten years ago, some might have argued the last thing the world needed was another rating agency to serve the muni market. He said last summer, however, his agency achieved a milestone when the Federal Reserve deemed KBRA to be one of only four major rating agencies whose ratings could be used by issuers accessing the central banks emergency Municipal Liquidity Facility window. He commended Congress support in being integral to allow credit rating agencies to participate in government bond programs. Nadler continued that bond investors are increasingly interested in the social impact of their investments, and in the municipal bond market, investors need to understand how state and local government issuers plan to address economic, racial, and social justice within their communities. He supports efforts to improve the quality of disclosure on these topics from all levels of municipal government, as well as improving diversity and inclusion in municipal roles and recalibrating municipal responses to economic, racial and social justice issues. He added there is an increasing interest in thorough climate-related disclosures and he believes climate risk should be incorporated in all ratings where it is relevant. He concluded that municipal stakeholders will continue to drive decisions on changes that need to be made, and that analyzing municipal managers' responses to stakeholder preferences and the implications on credit is the role of a credit rating agency.

Chris Parsons, Professor of Finance, University of Southern California
In his testimony, Parsons said economists have long been interested in discrimination and racial disparities in wages, job placement, home ownership, mortgage rates, access to capital and dozens of other areas. He said the challenge is that comparing differences in average outcomes between groups by gender, race, and age may not always "paint a complete picture". He said studying municipal bonds, however, provides good insight into the issue. He explained that when you buy a bond all that should matter is the financial return, and there is a well-accepted way of measuring an issuer's bond ratings. He asserted that his findings demonstrated that HBCUs pay 20 percent more in fees to underwriters, and that when HBCU-issued bonds are traded, it takes about 23 percent longer to find a willing buyer. Parsons concluded with one possible policy tool available to help remediate the challenges identified in his study: affording investors of HBCU-issued bonds tax exemption from state and local taxes. He said this policy would remove the tax disadvantages an investor living in, for example, New York or California currently faces when potentially investing in an HBCU-issued bond from another state.

Question & Answer
Discrimination Against Minority Serving Institution Issuers

Green asked witnesses if they believe these circumstances relating to HBCUs paying more on average than non-HBCUs indicates institutionalized discrimination. Parsons said the results of their findings are consistent with investors, not institutions and that their paper does not address that idea. McDaniel said it seems that way, judging by the outcomes of the studies. Fisher said yes, when discussing institutional investors. Hall said he has not studied that, and what he saw in the study with taste-based discrimination is not consistent with his experience in the marketplace and does not reflect the growth that has occurred since the study took place. He said he cannot conclude that there has been institutional racism.

Rep. Emanuel Cleaver (D-Mo.) asked witnesses if they believe socioeconomic factors like poverty, income inequality, and availability of affordable housing all factor in on a risk of a municipality and their ability to get significant bonding, or if race is not a factor at all. Hall said a lot of considerations are taken into fact when regarding the municipal bond market, but Socioeconomic background are not as important as is the economic power in terms of the tax base.

Rep. Alma Adams (D-N.C.) mentioned the data which showed HBCUs pay more to issue bonds than similarly-situated non-HBCUs. She asked how to quantify this cost in the years to come. Parsons said if the total cost is shown as 20-30 basis points, then it is in the hundreds of thousands of dollars and can be quantified a number of ways whether it represent a few professors or a few scholarships. He said he wanted their study to be able to look at the decisions to issue bonds that were not taken since every study is conditional on bonds that successfully went to the market. Parsons said no one can observe the cost to HBCUs that were not able to go to the market, and his intuition was that cost is significantly larger for those HBCUS.

Adams asked if there are solutions to address these fee disparities between HBCUs and non-HBCUs. Hall said the study mentions the notion of expanding the tax base for HBCUs, which SIFMA supports, by having triple tax exemption for HBCUs so that states who issue, like North Carolina, would be attractive to issuers in New York where the state income tax is high. Additionally, he suggested having a direct pay program similar to Build America bonds, allowing the HBCUs can access the taxable market, which has a wider investor base, thereby increasing the demand for HBCU bonds and closing their overall costs. McDaniel suggested looking at different factors that are not typically folded into the credit worthiness assessment of muni bonds.

Barr asked if provisions in the Investing in Our Communities Act would lower interest rates and help municipalities and issuers. Hall said yes, that the ability to refund existing debt with lower tax exempt debt is vital and needs to be reinstated.

Rep. Rashida Tliab (D-Mich.) said the Federal Reserve has been unwilling to facilitate meaningful emergency assistance for state and local governments and asked how Congress should step in to fill this gap and foster long term investments in communities. Parsons pointed to the findings with HBCUs, and stated his support for the triple tax exemption as being “almost a free market solution to a problem”. He said the issue is the market is too small, and the exemption opens up the market to other states.

Credit Ratings and Evaluating Bond Deals

Barr asked what criteria goes into signing a bond and what factors are considered to be material. Nadler said materiality is key and when thinking about a bond rating and a credit rating you need to make sure what you are analyzing does have an impact on the fiscal health of that entity, whether it is a city or a state. Nadler said they found disclosure to be the most important aspect. He added there are other aspects that impact the liquidity of a bond moving forward that may not necessarily impact credit worthiness today but would still be interesting to investors. He supports more disclosures that align with investor preferences and give insight around liquidity.

Rep. Chuy Garcia (D-Ill.) said that much of what goes into credit ratings is outside of an issuers control, like if Puerto Rico was devastated by a hurricane, and noted that communities of color tend to be hit hardest by these shocks. He continued by asking if ratings firms consider criteria like this. Nadler said ratings firms do not do a good job of consideration. He said it is important to have competing ideas and enough research out there for investors. He added that rating agencies “get into a rut" and look at the same things every time, but should be reimagining cities and states as they grow and evolve.

Rep. David Kustoff (R-Tenn.) asked when evaluating a muni bond deal, what factors are the most important that impact the cost of capital for the issuer. Hall said they have to evaluate the credit underpinnings of the investor and the actual size of the issuance, and whether or not it would be very liquid in the market. He said that liquidity is an important factor as it relates to the resonance of the bond in the market and these are all taken into consideration when evaluating the risks.

Municipal Liquidity Facility (MLF)
Barr said he was surprised that after supporting the MLF, there was not as much uptake, and that throughout the pandemic the municipal bond market proved to be fairly resilient. Barr asked Nadler where he sees the bond market moving in the future, and if the state and local governments bailouts were really necessary on top of MLF. Nadler said they were also surprised by uptake as it relates to the committee and believed it had to do with how quickly muni market moved back to some normalcy. He said that although recovery has been great and faster than anticipated, there were structural issues prior to the pandemic that will be exacerbated and cause unevenness moving forward post-pandemic.

Rep. Sylvia Garcia (D-Texas) asked about the Municipal Facility saying it did not work, there were high penalty fees, and it initially excluded many Black cities in America. Garcia asked if it is still needed and what changes would need to be made. Hall said at the time the program was enacted, there were $500 billion allotted to the program, which is larger than the entire muni market. He said it was a "shock and awe" program to make sure investors knew the Fed was behind them in the muni bond market. Hall said after the MLF program came in, the muni bond market had the largest issuance during a month time span ever in history. He said the overall benefit to the marketplace was stability, but now the market is extremely resilient so it is not necessary, but having the ability to stand it up as an emergency back stop is important.

Importance of Muni Bonds
Kustoff asked about the importance of muni bonds as a tool for individuals in their financial planning and saving for retirement. Hall said these products give citizens the ability to invest in their own communities. As a long-term investment vehicle, he said muni bonds offer a significant return and that benefit is evident from the fact that over 50 percent of the market is held by "mom and pop households."

Higher Education Issuances
Kustoff also Hall what the market is like for higher education issuances and how that compares to other types of available debt in the market. Hall said key components of higher education is the size of the endowment, student mix, and different sources of revenues the institution has. He said there has been peak demand for social impact bonds in the current market, making higher education and even K-12 attractive investments.

Oversubscription
Rep. Michael San Nicholas (D-Guam) said he endorses a triple tax exemption status for HBCUs and mentioned another solution that would allow land grant institutions to classify as agencies with Federal backing similar to government sponsored enterprises, to help drive down interest costs. He asked what a typical oversubscription is that would be helpful. Hall said creating peak competition for bonds drives yields downwards. He said the good news is the market has had many regulatory changes, and one of the important features is the expanded inclusion of municipal advisors to have a defined fiduciary role. Hall said they are crucial to the underwriting process because when there is oversubscription, municipal advisors ask the underwriters to lower yields and reduce that

subscription, which helps ensure oversubscription goes to the benefit of the issuer.

Public Banks

Tliab asked if a public bank would be more likely to consider other factors beyond profitability in issuing bonds compared with a private bond underwriter. McDaniel said yes, and an advantage is that muni banks allow cities to recapture the local tax revenues, keeping the money within the community. Parsons said public banks serve a role when the private markets are failing or struggling.

For more information on this hearing, please click here.

MBFA Meets with Key Hill and Administration Staff Promoting Muni Priorities.

The Municipal Bonds for America Council hosted a "virtual fly-in" for Steering Committee members over the past week. The meetings focused on municipal bonds in the context of infrastructure financing and proved productive as both Congress and the Administration have begun to take concrete steps towards the introduction of a massive infrastructure package.

The MBFA met with senior staff representing:

- U.S. Department of Transportation Office of Intergovernmental Affairs
- Senator Debbie Stabenow (D-MI)-Member of Senate Finance Committee
- House Ways and Means Minority Tax Counsel
- Rep. Brad Schneider (D-IL)-Member of House Committee on Ways and Means

The recent introduction of the ***LIFT Act*** in the House and companion Senate bills helped to guide the conversations, however, the conversations went beyond the legislation and included:

- Restoration of tax-exempt advance refundings;
- Expansion of PABs including ESG;
- Raising the BQ debt limit; and
- Reinstatement of direct-pay bonds exempt from sequestration.

This event is part of the ongoing MBFA effort to ensure Congress includes municipal bond financing in any federal infrastructure package. We plan to host future fly-ins as legislation continues to progress, including in-person events in DC.

If you would like to get more involved with the MBFA, please contact Brett Bolton at brettbolton@munibondsforamerica.org

Bond Dealers of America

May 14, 2021

Accelerating the Settlement Cycle: SIFMA

Leading the Move to T+1

Accelerating the settlement cycle, as we all know from experience, is a complex and significant undertaking.

Working closely with members and other key stakeholders, SIFMA is collaborating with ICI and DTCC to outline key steps to shorten the cycle for secondary market transactions, identifying priority issues that need to be addressed and conducting the necessary due diligence and resolution of these critical issues. Discussions with our members began last year and we aim to complete this analysis on next steps to achieving T+1 by the end of Q3 2021. Shortly after that work, we will develop a definitive timeframe for moving to T+1. In addition to efforts to shorten the settlement time, we will assess what it may take to further accelerate the settlement cycle beyond T+1 and explore the role that emerging technologies could play.

Learn more about this important initiative:

- Blog Post: A Shorter Settlement Cycle: T+1 Will Benefit Investors and Market Participant Firms by Reducing Systemic and Operational Risks
- Press Release: SIFMA, ICI and DTCC Leading Effort to Shorten US Securities Settlement Cycle to T+1
- Video: Accelerating Settlement: A Conversation with SIFMA and DTCC

SEC's Amended Advertising Rules for Investment Advisers: Compliance Date Countdown Begins - Day Pitney

The U.S. Securities and Exchange Commission's (SEC) amended Marketing Rule became effective on May 4, 2021, kicking off the 18-month countdown to the November 4, 2022 compliance date. All investment advisers registered or required to be registered with the SEC will be required to conduct their advertising and solicitation activities in compliance with the amended rule no later than the compliance date. The Marketing Rule is a substantial revision of Rule 206(4)-1 under the Investment Advisers Act of 1940, as amended (the Advisers Act), commonly referred to as the advertising rule, which incorporates elements of former Rule 206(4)-3 (the cash solicitation rule, which has been repealed) to create a single unified rule that modernizes the regulatory framework for advertising and solicitation practices conducted by SEC-registered investment advisers.

The new Marketing Rule reflects advances in technology, changes in investor expectations and diversification of the investment industry over the past 60 years. Specifically, the new Marketing Rule:

- Updates how advertisements are defined
- Removes the current per se prohibitions and replaces them with seven general principles covering all advertisements
- Identifies standards for performance information and track-record presentations
- Covers not only advisory clients but also investors in private funds
- Permits testimonials and endorsements for which cash and noncash compensation is received

Because the Marketing Rule integrates prior SEC no-action letters and staff guidance with respect to the old advertising and cash solicitation rules, the SEC is expected to withdraw those superseded no-action letters and other prior staff guidance at the end of the implementation period. The SEC is maintaining a list of Marketing Compliance Frequently Asked Questions here, which we expect will be updated over the next year and a half as investment advisers grapple with the challenges of drafting policies and procedures in order to comply with the Marketing Rule. It is important to note that while an adviser may come into compliance with the Marketing Rule at any time after May 4, 2021, compliance is an “all or nothing” proposition. Phased-in compliance is not an option.

What Is an Advertisement?

Under the new Marketing Rule, the definition of “advertisement” includes two prongs, which capture the types of communications previously covered by the advertising and cash solicitation rules.

Offering Investment Advisory Services

The first prong of the new definition of advertisement includes any direct or indirect communication an investment adviser makes to more than one person, or to one or more persons if the communication includes hypothetical performance, that either

- offers the adviser’s investment advisory services with regard to securities to prospective clients or investors in a private fund advised by the investment adviser or
- offers new investment advisory services with regard to securities to current clients or investors in a private fund managed by the investment adviser.

The scope of what constitutes an advertisement under this first prong is limited by a few notable exclusions, including the following communications, which are excluded from the definition of advertisement: (i) extemporaneous, live, oral communications; (ii) information contained in statutory or regulatory notices, filings, or other required communications; (iii) communications that include hypothetical performance that is provided in response to an unsolicited request for such information; or (iv) a communication that includes hypothetical performance that is provided to a prospective or current private fund investor in one-on-one communications.

Compensated Testimonials and Endorsements

The second prong of the new definition of advertisement draws from the old cash solicitation rule by encompassing any endorsements or testimonials for which an investment adviser directly or indirectly pays cash or noncash compensation (e.g., directed brokerage, awards, gifts, referrals, reduced advisory fees or fee waivers).

An endorsement is defined as being any statement that either (i) indicates approval or support, (ii) directly or indirectly solicits a client to be the adviser’s client, or (iii) refers any client to a private fund managed by the investment adviser. The definition of a testimonial includes statements made by a current client or investor in a private fund that (i) is about a client experience, (ii) directly or indirectly solicits any client to become a client of a private fund, or (iii) refers any client to the private fund. Compensated endorsements and testimonials will satisfy the definition of advertisement whether the communication is made orally or otherwise to one or more persons.

Testimonials and Endorsements Are Now Permitted

The new Marketing Rule permits the use of testimonials and endorsements, subject to compliance with the following four conditions:

Disclosure: The investment adviser must clearly and prominently disclose or have a reasonable belief that the person giving the testimonial or endorsement will disclose (i) that the testimonial was given by a current client or investor (or by a person other than a current client or investor); (ii) whether cash or noncash compensation was provided, and the material terms of the compensation arrangement; and (iii) any material conflicts of interest on the part of the person giving the testimonial or endorsement resulting from the adviser's relationship with such person and/or the compensation arrangement. In a departure from the old cash solicitation rule, the new Marketing Rule does not require the promoter or solicitor to deliver a written disclosure document to the client if an endorsement or testimonial is given orally or to obtain a signed and dated acknowledgment from the client confirming receipt of the required disclosures. In another departure from the old cash solicitation rule, these disclosures may be made by either the investment adviser or the solicitor. However, if the adviser is relying on the promoter to disclose the required information, the adviser may want to consider retaining the traditional written disclosure system as a best practice.

Written Agreement: The adviser must have a written agreement with any promoter or solicitor providing a testimonial or endorsement that describes the scope of the agreed-upon activities and the terms of compensation for the activities; however, no written agreement is needed where the promoter is an affiliated person of the adviser or if the promoter receives minimal or no compensation (i.e., under $1,000 or the equivalent value in noncash compensation during the preceding 12 months).

Disqualification: An investment adviser must not compensate a person for a testimonial or an endorsement if the adviser knows or should know that the person giving the statement is an "ineligible person" at the time the statement is disseminated. A person is ineligible if he/she is subject to any disqualifying SEC action or disqualifying event. Actions that occurred prior to the effective date of the Marketing Rule will not disqualify a promoter, provided that the action would not have disqualified such person under the former cash solicitation rule. A disqualifying SEC action includes an SEC opinion or order barring, suspending or prohibiting a person from acting in any capacity under the federal securities laws. A disqualifying event includes certain criminal convictions and orders, including those of other governmental agencies, such as the Commodity Futures Trading Commission, that occurred within 10 years prior to the person's disseminating a testimonial or endorsement.

Oversight: The investment adviser must have a reasonable basis for believing that the testimonial or endorsement complies with the Marketing Rule. The written agreement requirement is part of the investment adviser's oversight and compliance obligations, but it does not by itself establish a reasonable belief of compliance. We recommend that advisers adopt policies and procedures that are reasonably designed to monitor compliance with the Marketing Rule.

Exemptions From Certain Requirements for Testimonials and Endorsements

De Minimis Compensation: A testimonial or endorsement for no compensation or for compensation not exceeding $1,000 will be exempt from the written agreement requirement and the disqualification provisions, but the investment adviser must comply with the disclosure and oversight requirements.

Affiliated Persons of Adviser: An adviser's partners, officers, directors, employees and affiliates, and such affiliates' respective partners, officers, directors and employees, are not required to comply with the disclosure or written agreement requirements, but the investment adviser must comply with the oversight and disqualification requirements.

Broker-dealers: A testimonial or endorsement from a broker-dealer making a recommendation pursuant to Regulation Best Interest or to a non-retail customer as defined by Regulation Best Interest does not need to comply with certain disclosure requirements and will be exempt from the disqualification requirements if the broker is not subject to statutory disqualification under Section 3(a)(39) of the Securities Exchange Act of 1934. However, the written agreement and oversight requirements apply.

Third-Party Ratings

The new Marketing Rule permits the use of third-party ratings in an advertisement, provided that the adviser has conducted certain diligence pertaining to the preparation of the rating and provides disclosure to assist a potential client in evaluating the rating. A third-party rating is defined in the Marketing Rule as a rating or ranking of an adviser provided by a person who is not a related person of the adviser and who is in the business of providing rankings or ratings. The adviser is required to have a reasonable basis for believing that any questionnaire or survey used in connection with obtaining the rating was fair. A survey's methodology will be considered fair when it is structured in a way that makes it equally easy for a participant to provide either favorable or unfavorable responses. In addition, the investment adviser must clearly disclose (i) the date on which the rating was provided and the time period on which the rating was based, (ii) the identity of the third party who created the rating, and, if applicable, (iii) any compensation paid by the adviser to the person creating the rating. Such disclosure must be at least as prominent as the third-party rating itself.

Performance Advertising/Track Record or Predecessor Performance

The Marketing Rule renders general guidance for the use of gross, net, hypothetical, related and extracted performance information by investment advisers. Performance results must include performance information for one-, five- and 10-year periods with equal prominence; however, investment advisers to private funds are exempt from the time period requirements.

Gross Performance and Net Performance

Gross performance should not be used unless net performance is presented with at least equal prominence and in a format designed to easily compare it to net performance. In addition, net performance must be calculated over the same time period as gross performance and with the same calculation methodology.

Hypothetical Performance

In a significant change from prior SEC guidance, hypothetical performance is permitted, provided that the adviser (i) adopts and implements procedures reasonably designed to ensure that the performance is relevant to the likely financial situation and investment objectives of the intended audience and (ii) provides certain information underlying the hypothetical performance, including the criteria used and assumptions made in curating such specific performance data and the risks and limitations of using and relying on hypothetical performance data.

Extracted Performance

Using performance results of a subset of a portfolio is allowed only if the adviser provides (or promptly makes available) the performance results of the total portfolio.

Related Performance

Performance results cannot be cherry-picked from portfolios. Advisers must include performance results from all related portfolios with investment policies, objectives and strategies substantially similar to those being offered in the advertisement (unless the excluded related performance information would not result in materially higher performance results and does not alter the presentation of any time periods).

Track Record or Predecessor Performance

Predecessor performance (or track records from a prior firm or portfolio) are prohibited in advertisements, except in limited circumstances. First, the information must be derived from the adviser's directly managed account at a prior firm. Second, the prior account must have been sufficiently similar to the present account in a relevant way that makes the extrapolation fair. If there were other accounts managed by the adviser in a substantially similar manner, these accounts must also be included in the advertisement. Finally, the advertisement must contain all relevant disclosures, including that the performance results displayed are from and were achieved for a prior entity.

An investment adviser may use predecessor performance only if the predecessor and current investment advisers are appropriately similar with regard to their personnel and accounts and the advertisement has other relevant disclosures required under the Marketing Rule. In addition, the adviser must have access to the books and records attributable to the predecessor performance and must be able to provide them if the SEC requests such books and records.

Prohibition on Statements Regarding SEC Approval of Performance Results

Advertisements cannot include any language, express or implied, that the calculation or presentation of performance results in the advertisement has been reviewed or approved by the SEC.

General Prohibitions Under the New Marketing Rule

The Marketing Rule expands upon the existing blanket prohibition against advertisements containing any untrue, misleading or false statements of material facts with a new, more detailed principles-based approach. The new approach features seven broadly prohibited practices. An investment adviser may not disseminate any advertisement that

i) makes an untrue statement of a material fact or omits a material fact necessary to make the statement not misleading;

ii) makes a material statement of fact that the investment adviser does not have a reasonable basis for believing it will be able to substantiate;

iii) includes information that would be reasonably likely to cause an untrue or misleading implication or inference to be drawn concerning a material fact;

iv) discusses any potential benefits without providing fair and balanced treatment of any associated material risks or limitations;

v) references specific investment advice provided by the investment adviser that is not presented in a fair and balanced manner;

vi) includes or excludes performance results or presents performance time periods in a manner that is not fair and balanced; or

vii) includes information that is otherwise materially misleading.

These categories draw broadly from historic fiduciary duty and anti-fraud principles. The prohibitions generally apply to any statements that could mislead clients through untrue or material misstatements or those which are not presented in a fair and balanced manner, and they prohibit including them in advertisements.

Other Changes

In connection with the Marketing Rule, the SEC made corresponding amendments to the Books and Records Rule (Rule 204-2 under the Advisers Act) and to Form ADV. Under the amendments to the Books and Records Rule, advisers will be required to maintain more detailed documentation regarding their advertisements and their arrangements for testimonials and endorsements. Form ADV will require advisers to respond to questions regarding their marketing practices, specifically whether the adviser's advertisements contain performance results, hypothetical performance, testimonials, endorsements or third-party ratings, and whether the adviser provides compensation in connection with the use of testimonials, endorsements or third-party ratings.

Day Pitney Alert

by Erik A. Bergman, Peter J. Bilfield, Eliza Sporn Fromberg & Joty Mondal

May 5, 2021

Muni-Bond Investors Need Straight Talk About Climate-Change Risk.

Most municipal-bond issuers aren't discussing their vulnerability to the environment and the SEC should make them

In February, the Security and Exchange Commission's acting chair directed its Division of Corporate Finance to enhance climate-related disclosures by public companies. The acting chair has also appointed a senior policy adviser for Climate and ESG — a new role at the agency.

While much of the SEC's efforts in increasing climate-related risk disclosures will focus on publicly traded corporations, the $4 trillion municipal bond market is equally important for the agency to address. These bonds typically have maturities of 15- to 30 years — long enough for the material risks of climate change to impact municipal cash flows. Furthermore, municipal bonds trade infrequently, so it is difficult for investors to sell these positions at reasonable prices if adverse climate events actually occur.

Yet current disclosures on climate-related risks are minimal by most municipal bond issuers, even those that have recently experienced severe flooding and wildfires. Therefore, the SEC should work together with the Municipal Securities Rulemaking Board (MSRB) to require more extensive disclosures on the material climate risks of municipal bonds as well as the efforts by municipal issuers to mitigate these risks.

Since municipal bonds typically have long maturities, they are highly vulnerable to adverse changes in climate changes, even if they do not materialize for a decade or longer. Much of the revenue underlying these bonds comes from infrastructure projects and commercial properties, which are likely to be impacted by severe climate events. Yet, unlike many public companies, municipal issuers cannot easily respond to these climate risks by moving their facilities to higher ground or cooler geographies.

Most purchasers of municipal bonds own them until maturity. That's why municipal bonds are generally considered to be a "buy-and-hold" market. For example, a 2012 study conducted by the SEC found that about 99% of outstanding municipal securities did not trade on any given day in 2011. Because municipal bonds are not actively traded, they often do not have publicly quoted prices — which makes them difficult to price accurately.

Municipal bonds are extremely popular with retail investors because the interest paid on these bonds is generally exempt both from federal- and state income taxes. Municipal bonds are particularly attractive to retail investors in states with high income-tax rates such as California and New York. The biggest holders of municipal bonds are mutual funds catering to individual investors — such as the Vanguard Group of mutual funds, with more than $200 billion in municipal bonds.

Retail investors are attracted to municipal bonds not only because of their tax exemptions but also because of their low default rates. Over the decade ending in 2018, the average default rate for investment-grade bonds was 0.10%, as compared with a default rate of 2.28% for corporate bonds with similar ratings. Nevertheless, a 2019 analysis by investment firm BlackRock concluded that, if emissions of warming gases were not controlled over the next decade, more than 15% of the current S&P National Municipal Bond Index would be tied to metropolitan areas likely to suffer material economic losses from climate change.

Given the low liquidity and long maturities of municipal bonds, full disclosure of climate-related risks is crucial for preventing unsophisticated retail investors from becoming locked into bonds vulnerable to climate change. Yet offering documents for municipal bond issuers currently contain low levels of climate-related risk disclosures.

Examining 590 U.S. counties with populations over 100,000, a recent Brookings Institution study found that the offering statements of just 10.5% of municipal revenue bonds mentioned climate change. Yet these bonds are based on revenues from specific physical projects — such as tunnels, roads and treatment facilities — that would likely suffer from adverse climate events. Even worse, the Brookings study found that only 3.8% of general obligation municipal bonds mentioned climate change. But most municipalities issuing these bonds derive the bulk of their revenues from taxes on real estate, whose value would materially decline in the event of more hurricanes or wildfires.

Consider the revenue bonds issued in 2020 by the City of Phoenix Improvement Corporation, maturing in 2045. The offering statements for these bonds do not mention risks related to “climate change”, “drought” or “heat”. Yet Phoenix, Ariz. is already hot, and is one of the fastest-warming big cities in the US. According to a study from Climate Central, the average number of 100-degree days per year for Phoenix will increase to 132 by 2050 — likely leading to a water crisis.

One consequence of these low disclosure levels is that municipal bond markets aren’t pricing in climate-related risk. For example, compare the municipal bonds recently issued by Middletown Unified School District and Red Bluff Unified Elementary School, both in California. Both bonds mature in 2048 with AA ratings and similar pricing. Yet the risk of serious property damage from wildfires is more than five times higher in Middletown than in Red Bluff.

In response to the increased attention to climate risk, rating agencies have been moving in the right direction by publishing reports on how they are factoring climate risk into their assessment of the long-term financial position of municipalities. These reports have focused on the ability of municipal issuers to absorb the fiscal shocks caused by damages and lost revenues related to climate events. However, these are complex issues for the rating agencies to solve alone, due to the long-term nature of the problem and the lack of reliable data.

To enhance climate-risk disclosures, the SEC should amend its rules for underwriters of municipal bonds to require more detailed information on past climate events and the probabilities of future climate events. Such amendments should win support from the Government Finance Officers Association, which has recently recommended that local governments develop better disclosures about the primary environmental risks applicable to municipal bonds.

Since many municipal issuers have already experienced severe hurricanes, wildfires and other weather-related events, they can easily estimate the private and public damages imposed by such events as well as the costs of any preventive measures already taken. The latter would include the building of sea walls, the construction of carbon capture facilities and the adoption of any strategies to reduce greenhouse gas emissions.

Disclosures on adverse climate events in the future are more challenging. Since climate models do not typically produce an exact result, the offering statements for municipal bonds should contain a range of likely scenarios along with their probabilities of occurring. For each scenario, investors should be told about the scope of the adverse climate events and their impact on the assets supporting the municipal bonds — the dedicated assets for a revenue bond and the tax base for a general obligation bond.

In addition, to facilitate searches on climate risks and comparisons among municipal issuers, the MSRB should require that all offering statements for municipal bonds be filed in a singular, machine-readable format. At present, analysts must pull climate risks by hand from these disclosure documents.

Addressing the risks posed by climate change to municipal bonds should be a high priority for the SEC under the Biden administration. Given the illiquidity and long duration of municipal bonds, it is critical for investors that the SEC enhance the disclosures on climate risk in the municipal bond market.

MarketWatch

By Robert C. Pozen

March 30, 2021

SEC Should Force Municipal Issuers to Disclose Climate Risk, Says Former Fidelity President.

The SEC has taken action in recent months to increase public companies' disclosure of climate risk.

But no such movement exists in the long-term municipal bond market, despite being particularly exposed to climate risk.

Robert C. Pozen, Senior Lecturer at MIT and former president of Fidelity Investments, writes at MarketWatch:

> Current disclosures on climate-related risks are minimal by most municipal bond issuers, even those that have recently experienced severe flooding and wildfires. Therefore, the SEC should work together with the Municipal Securities Rulemaking Board (MSRB) to require more extensive disclosures on the material climate risks of municipal bonds as well as the efforts by municipal issuers to mitigate these risks.
>
> Since municipal bonds typically have long maturities, they are highly vulnerable to adverse changes in climate changes, even if they do not materialize for a decade or longer. Much of the revenue underlying these bonds comes from infrastructure projects

> and commercial properties, which are likely to be impacted by severe climate events. Yet, unlike many public companies, municipal issuers cannot easily respond to these climate risks by moving their facilities to higher ground or cooler geographies.
>
> […]
>
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by CivMetrics Staff | Apr 21, 2021

SIFMA Amicus Brief: BofI Holdings, Inc. v. Houston Municipal Employees Pension System

SUMMARY

Court:
U.S. Supreme Court (pet. for writ of cert.)

Amicus Issue:
Whether unsubstantiated public allegations about an issuer or its business, without any additional corroborating disclosure or event, reveal to an efficient market the 'truth' for purposes of establishing loss causation under Dura (as held by the Sixth and Ninth Circuits, in direct conflict with the Eleventh Circuit).

Counsel of Record:
Simpson Thacher & Bartlett LLP

Jonathan K. Youngwood
Craig S. Waldman
Joshua Polster
Daniel Owsley

Other Amici:
U.S. Chamber of Commerce

Read the Amicus Brief.

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ACCESS COMMUNITIES

What Happens When the Recently Enacted NY LIBOR Statute Meets the Trust Indenture Act?

Many corporate trustees have been concerned about what happens when the U.S. Dollar LIBOR ("LIBOR") cessation finally occurs (now set for June 30, 2023 for 1-month, 3-month, 6-month and 12-month USD LIBOR settings, among others). There appeared to be some relief on April 6, 2021 when LIBOR legislation was signed into law in New York state (the "NY LIBOR Legislation"), which is designed to facilitate a smooth transition to alternative benchmark rates. Promulgation of the NY LIBOR Legislation was motivated by uncertainty surrounding the future of some $223 trillion in contracts and financial products pegged to LIBOR as of the end of 2020, many of which are governed by New York law and do not contain fallback provisions to transition to an alternate benchmark upon the cessation of LIBOR.

While the NY LIBOR Legislation, on its face, appears to be an effective stopgap measure, the Trust Indenture Act of 1939 (the "TIA"), specifically Section 316(b) of the TIA, raises questions about the enforceability of the NY LIBOR Legislation under the TIA. Specifically, although the NY LIBOR Legislation provides some clarity for indenture trustees who are troubled about governing documents, including indentures, that are silent about LIBOR cessation, the NY LIBOR Legislation simultaneously triggers concerns under TIA Section 316(b), reminiscent of some of the issues highlighted in the 2017 decision of the Second Circuit Court of Appeals in *Marblegate Asset Management, LLC v. Education Management Finance Corp. ("Marblegate").*

In broad terms, the NY LIBOR Legislation provides that, in the case of many New York law-governed contracts that reference LIBOR and that do not have adequate fallback provisions to determine what happens when LIBOR ceases ("Legacy Contracts"), a new "benchmark rate" recommended by the appropriate authorities (e.g., the Secured Overnight Financing Rate ("SOFR")) will, by operation of law, be used for such contracts in lieu of LIBOR.

Since New York law governs a majority of corporate indentures, as well as many other financing documents, the NY LIBOR Legislation will have a broad impact and cover many underlying securities and financings. In the case of indentures qualified under the TIA (and, to an extent, indentures which are not so qualified for private placement issues or municipal bonds, both of which often incorporate the TIA to varying degrees), TIA Section 316(b) provides that "the right of any holder of any indenture security to receive payment of the principal of and interest on such indenture security … shall not be impaired or affected without the consent of such holder." Accordingly, if bondholders or other parties to financings are negatively impacted by the rate change (to SOFR or otherwise) under the NY LIBOR Legislation and challenge such a change as a violation of Section 316(b) (or the 316(b) analogous language), it is far from clear that the NY LIBOR Legislation would survive the challenge.

The New York City Bar Association (the "NYCBA") issued a report supporting the NY LIBOR Legislation, in which it commented on the TIA issue. The NYCBA acknowledged the issue, supporting a minor amendment to the TIA and concluding that "… whether or not the TIA is amended … New York should proceed with a legislative solution that can be applied to the many transactions not subject to the TIA."

The well-documented judicial record of prejudiced and disgruntled bondholders that seek, with some success, to be made whole through litigation is a prominent source of anxiety for issuers and corporate trustees related to LIBOR's phase-out. This is reminiscent of *Marblegate*, as well as other cases which speak to the required consent of affected bondholders, where the issue of changes to bond terms without bondholder consent was relevant. While the Second Circuit Court of Appeals ultimately ruled against the bondholders objecting to changes in *Marblegate*, a recent New York case (*CNH Diversified Opportunities Master Account, L.P. v. Cleveland Unlimited, Inc. ("CNH"))*, arguably created contrary precedent for unhappy bondholders to convince a court that an amendment or transaction violated their rights as creditors or was unlawful under state or federal law, notwithstanding the *Marblegate* ruling. It remains unsettled, perhaps to be further clarified by a court, whether *CNH* has indeed created an opportunity for such bondholders. In any case, even though the NY LIBOR Legislation presents different issues under Section 316(b) than were involved in *Marblegate* and *CNH*, the mere mention of Section 316(b) and how it may be interpreted by the courts in relation to LIBOR will be of concern to indenture trustees.

Presumably, New York lawmakers had TIA Section 316(b), *Marblegate* and *CNH* in mind when drafting the New York LIBOR Legislation; hence the legislation's "Safe Harbor Provision." Specifically, the Safe Harbor Provision provides that no person shall have any liability arising out of the use of a recommended benchmark replacement or the implementation of benchmark replacement conforming changes. That said, it remains to be seen how, or if, the Safe Harbor Provision would apply to a dispute arising under the TIA and if the Safe Harbor Provision will adequately protect corporate trust banks acting as trustees and agents.

Accordingly, while the NY LIBOR Legislation provides some comfort, federal statutes such as the TIA might provide bondholders with an avenue to object should they feel aggrieved. Other considerations under federal law, such as the contracts clause of the U.S. Constitution (which prohibits states from passing laws impairing contract obligations), also exist but are beyond the scope of our focus here.

The NY LIBOR Legislation provides relief only for Legacy Contracts governed by the law of New York. A significant number of contracts, including indentures, however, are governed by the laws of other jurisdictions. Due to the existence of Legacy Contracts governed by laws other than those of New York, support for a federal statute mimicking the language and effect of the NY LIBOR Legislation is gaining momentum. On April 14, 2021, major financial industry groups, including the Securities Industry and Financial Markets Association, the Structured Finance Association and the

American Bankers Association submitted a joint letter to the United States House of Representatives Committee on Financial Services, calling for the passage of a federal statute achieving the same end as the NY LIBOR Legislation. Consequently, there may be more issues for corporate trust banks to consider. Both the NY LIBOR Legislation and a potential federal statute are, without question, of paramount importance to corporate trustees and may affect risk assessment and the scope of review of transactional documents. As always, the corporate trust community should remain vigilant.

Thompson Hine LLP – Irving C. Apar and Yesenia D. Batista

April 30 2021

Questions about GFOA's New Member Communities?

We've put together a number of resources to help you navigate GFOA's new Member Communities. Click the link below for helpful FAQs and how-to videos.

LEARN MORE

MSRB Par Value Report.

Par value traded in the municipal bond market decreased more than 40% in Q1 2021 compared to the same period in 2020.

See all the stats.

Why It's Time To Investigate The Wisconsin Public Finance Authority.

For some time I have been critical of this regional Wisconsin Public Finance Authority that has taken on the role of willing issuer for bonds anywhere in the United States. I don't know what its motivation was in presuming such a prominent role in the municipal bond market, but professionalism and expertise are certainly not what comes to mind. They have no dedicated professional staff and its board members experience show no particular skill in evaluating the bonds they approve. In fact, if what they review is no more than what the MSRB receives and post on the EMMA system, then they would have little or nothing substantial to evaluate.

I don't know how many of these out-of-state bond issues they have approved, but I do know that so far, some 23 issues totaling $1.9 billion have defaulted or are in distress with 19 of them occurring in 2020-2021. No other issuer, never mind state, comes even close to this number. In fact, during this time period I recorded 130 distress/defaults on $9 billion of debt. Hence, this one small regional authority accounts for 14.6% of the number of distressed or defaulted issues (or 20.5% of the dollar amount) during the last 13 months.

Most of these defaults are in the retirement and health care area, a type of bond that has historically had the worst default track record. All the more reason then for added scrutiny. A common element for the Wisconsin bonds is that there is little or no information in terms of audited financial statements or official statements. We know that audited financial disclosure has not been a requirement of the authority. Its website advertises its services and makes no pretense at providing anything more than a rubber stamp.

I understand that they took on this nationwide authorization authority at the behest of a financial institution. Just four counties and a city that decided they had a calling. Aside from the abuse we see here, there is a huge infringement on the rights of each state to police the issuance of bond debt for project within its borders. There are also caps on the volume of tax-exempt issues that represents a quota that a state has a right to allocate.

There is also a responsibility to bond buyers who show a great deal of trust in the municipal market despite the fraud and abuse we have seen over the years. It is for these and other reasons that the MSRB, SEC, Congress and state securities regulators should look into this, starting with the state of Wisconsin.

Forbes

by Richard Lehmann

Apr 29, 2021

Earth Day: Municipal Bond Climate Change Disclosure Update

Climate Change Disclosures are Growing in Importance, Writes BB&K's Mrunal Shah in PublicCEO

In recent years, bond investors have increasingly demanded information on environmental disclosure, including climate change, social and governance (ESG) disclosure. With such increased demand by bond investors, public agencies have also increasingly disclosed climate-related change and risks. However, no consistent framework exists for such disclosure. California's state leadership set out to learn more about this ever-evolving topic and tasked the California Debt & Investment Advisory Commission to conduct a study to learn more.

The Study's Findings
The study analyzed content in over 200 official statements of enterprise revenue bonds issued between 2016 and 2019 to understand how California's municipal bond issuers are disclosing the risks in climate change. The results of the Commission's study can be found in the "Climate Change Disclosure Amount California Enterprise Issuers." The study found that, despite growing expectations to report climate risk, most issuers in the study did not mention climate change in their disclosure documents. Robust disclosures were notably linked to issuance size and high-frequency issuers. Geography was also a major factor, finding coastal counties and urban counties tended to include more thorough disclosure than inland and rural areas. The Commission's report also found that, of the 39 counties in the report sample, 14 did not mention any disclosure of climate change.

Regulatory Focus
The Securities and Exchange Commission has increased its focus on ESG as it has increasingly become a priority for investors. On March 15, the SEC's Division of Corporate Finance invited public input on a number of ESG disclosure-related considerations in an effort to evaluate its current disclosure rules. While the Division of Corporate Finance does not govern municipal securities, its actions and guidelines could provide useful insight for municipal bond issuers. In a public statement

issued in conjunction with the SEC's request for public input, Acting Chair of the SEC Division of Corporate Finance Allison Herren Lee stated "[s]ince 2010, investor demand for, and company disclosure of information about, climate change risks, impacts, and opportunities has grown dramatically…Consequently, questions arise about whether climate change disclosures adequately inform investors about known material risks, uncertainties, impacts, and opportunities, and whether greater consistency could be achieved."

Why Disclosure is Important
When offering securities to the public, municipalities have an obligation to disclose information so potential purchasers can make informed investment decisions. From California's fire-ravaged towns to Texas' devastating winter storms, some state municipalities are on the forefront of dramatic global climate change impacts.

In 2020 alone, the west coast was significantly impacted by wildfires, including five of the top 10 largest wildfires in California history. It is estimated the damage caused by the 2020 wildfire season will have a direct cost of over $20 billion, not including indirect costs such as insurance hikes and loss of revenue. According to the Dallas News, damages from the Texas freeze is estimated to have damages of approximately $155 billion due to crop losses, power outages, water disruption and infrastructure loss.

Although projected effects of climate change have received increased media attention in recent years, consideration of climate change in disclosure documents is a relatively new and evolving expectation. However, depending on the type of security being issued, such risks maybe material to potential investors. Municipal issuers should evaluate their current practice related to disclosure of climate risk to investors to ensure that such risks and uncertainties are being completely and accurately disclosed. Additionally, issuers should develop best practices for monitoring the ever-changing impacts of climate change and plan for disclosure of such risks for future issuances.

Municipal issuers should also be aware that disclosure of such risks may be utilized outside of the context of issuance of securities. According to the Commission's study, a climate change disclosure – or lack thereof – became the focus of litigation in 2018 by ExxonMobil against a group of California cities and counties that had filed suit against the company for future damages from sea-level rise and coastal flooding due to greenhouse gas emissions from fossil fuel products sold by the company. ExxonMobil countered that the public agency claims were not made in good faith because these climate-related issues were not included in the cities' and counties' bond disclosures. While litigation did not move forward, it prompted public agencies to review and disclose climate change risk in their offering documents.

Best Best & Krieger LLP

April 23, 2021

MSRB Holds Quarterly Virtual Board Meeting.

Washington, DC – The municipal market's self-regulatory organization held its quarterly Board of Directors meeting virtually on April 21-22, 2021. The Municipal Securities Rulemaking Board (MSRB) continued to consider and discuss input from its public request for comment on strategic priorities and stakeholder interviews as it progresses with developing a new organizational vision and long-term strategic direction. The Board anticipates adopting a strategic plan this fiscal year that will guide the organization for several years beginning in Fiscal Year 2022.

“Planning for the future of the municipal securities market requires grappling with the pressing issues of today,” said MSRB CEO Mark Kim. “Our Board recognizes that the municipal securities market can play an important role in being part of the solution for advancing a more just and equitable society.”

The Board discussed recent initiatives of market participants and financial regulators to promote transparency around Environmental, Social and Governance (ESG) factors in the municipal market.

“Our market is beginning to establish best practices for ESG disclosure, and we are seeing ESG designations and scoring systems gain traction,” Kim said. “We are committed to leveraging our EMMA website to enhance the transparency and accessibility of ESG data and information.” The MSRB’s Electronic Municipal Market Access (EMMA®) website serves as the free central repository for municipal market disclosures and trade data.

The Board also discussed the steps it will take to align the EMMA website and other MSRB resources with the Government Accounting Standards Board (GASB) proposal to rename the Comprehensive Annual Financial Report due to the similarities in the common pronunciation of the acronym to a racially offensive term in South Africa.

Retrospective Rule Review

The Board regularly revisits existing rules to determine that they continue to achieve their intended purpose of enhancing market fairness and efficiency. The Board voted to begin a retrospective review of MSRB Rule G-10, on investor and municipal advisory client education and protection. The MSRB will publish a request for comment on potential amendments that aim to reduce unnecessary compliance burdens imposed on dealers by providing additional clarity about which customers should receive the required annual notifications.

Also at its meeting, the Board revisited a 2018 provision of MSRB Rule G-34, which was amended to address a regulatory disparity by extending the obligation to apply for CUSIP numbers in a competitive transaction on which they advise from dealer municipal advisors to all municipal advisors. The Board had previously planned to rescind the requirement for all municipal advisors, dealers and non-dealers alike. However, since the rule has been fully implemented in firms’ processes for several years and has proven to enhance market efficiency by ensuring CUSIP numbers are obtained at the earliest stage in a competitive deal, the Board determined to maintain the rule in its current form.

The Board voted to file with the Securities and Exchange Commission (SEC) housekeeping amendments to MSRB Rule A-8 to update or remove outdated descriptions of the Board’s procedures related to rulemaking.

Systems Modernization

Lastly, the Board received an update on ongoing efforts to leverage cloud technology to modernize the MSRB’s critical market transparency systems and improve the quality and utility of market data for all market participants.

“The MSRB takes its responsibility seriously to provide the public with valuable data that shines a light on municipal market trends that can have far-reaching effects on communities nationwide,” Kim said. “Our investment in the cloud is enabling us to improve the quality of data and develop powerful analytical tools to answer the market’s currently unanswerable questions.”

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Date: April 23, 2021

Contact: Leah Szarek, Chief External Relations Officer
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GASB Proposes to Rename the Comprehensive Annual Financial Report.

Norwalk, CT, April 13, 2021 — The Governmental Accounting Standards Board (GASB) today proposed to change the “comprehensive annual financial report” to the “annual comprehensive financial report.”

The proposed name change was prompted by GASB stakeholders raising concerns that the existing acronym for the report, when spoken, sounds like a profoundly offensive term. After seeking input from various stakeholder groups, the Board added a project to its current technical agenda in December 2020 to address those concerns.

The Exposure Draft (ED), *The Annual Comprehensive Financial Report*, proposes to eliminate both the financial report name and the offensive acronym from the GASB’s standards, though it is important to note that no changes have been proposed to the structure or content of the report.

Regarding the issuance of the ED, GASB Chair Joel Black said, “When you pronounce the acronym, it is a highly offensive racial slur directed toward Black South Africans. As we and our stakeholders are part of a global community, we do not wish to be offensive to anyone, so we have undertaken the project to address this.”

Stakeholders are asked to review the proposal and provide input to the Board by July 9, 2021. More information about commenting on the ED can be found in the document, which is available on the GASB website, www.gasb.org.

FINRA Proposes Amendments to Margin Requirement Rules.

The proposed amendments could significantly alter the landscape for extended settlement of securities offerings by expressly limiting the public offering exception for “whenissued” securities to equity IPOs

Key Points:

The proposed amendments:

- Define an “extended settlement transaction” as any transaction that is agreed to settle beyond T+2

and require all such transactions to be margined as though they were transacted in margin accounts
- Expressly narrow the scope of the current "primary distribution" exception for "when issued" securities to only apply to equity IPOs, and thus exclude public or "Rule 144A" offerings of debt securities, as well as follow-on or exchange offerings of equity securities
- Extend the exception whereby member firms can choose to take capital charges for any net mark to market loss on transactions in when-issued securities in "designated accounts" to the broader category of "exempt accounts" (which includes certain institutional investors), foreign broker-dealers, and DVP/RVP accounts

The Financial Industry Regulatory Authority (FINRA) has proposed amendments to its margin requirement rules, which protect member firms against customer credit risk by generally requiring firms to collect margin when they extend credit to their customers.

The proposed amendments would deem any transaction that is agreed to settle beyond T+2 an "extended settlement transaction" for which margin must be collected as if in a margin account, absent an applicable exception. The proposed amendments would also expressly limit the public offering exception for when-issued securities in cash accounts to equity IPOs. This change could significantly impact existing market practice for registered offerings of debt, as well as private offerings resold under Rule 144A. Furthermore, due to increased negative carry in debt refinancings, as well as delays in the launch of offerings that cause issuers to miss attractive market windows (as T+2 is insufficient to prepare the requisite closing documentation for many debt financings without a strong running start), the amendments could likely increase the cost of capital for issuers in the US capital markets. The authors of this Client Alert also believe the proposed amendments could cause member firms to be forced to take additional capital charges in order to allow transaction professionals (including the member firms themselves, as well as attorneys, auditors, trustees, and issuers) a sufficient amount of time to finalize the requisite closing documentation. The cost will either be borne by firms or passed through to issuers.

Background

T+2 Settlement Cycle

A settlement cycle for a securities transaction begins at the date of the contract to enter into a securities transaction (commonly referred to as the "trade date" or "T") and ends when both the "payment of funds" and the "delivery of securities" have occurred between the transacting parties. Rule 15c6-1(a) of the Securities Exchange Act of 1934 (the Exchange Act) requires the settlement cycle to take place within two days (commonly referred to as "T+2") "unless otherwise expressly agreed to by the parties at the time of the transaction."1 Accordingly, although the default requirement is that settlement take place within two business days, such period can be extended by agreement between the transacting parties.

Regulation T

Regulation T (Reg T), adopted by the Federal Reserve pursuant to Section 7 of the Exchange Act, regulates the securities credit activity of broker-dealers. As part of such regulation, Reg T specifically sets forth the periods of time in which a broker-dealer is required to (i) obtain cash payment from its customer in relation to a securities purchase in a cash account and (ii) have its customer post margin to cure a margin deficiency in a margin account. Reg T seeks to limit the exposure to market risk by broker-dealers in the event of delays beyond the normal settlement cycle by requiring either the cash payment or the posting of margin in lieu thereof to take place within one "payment period" of the date of purchase.2 "Payment period" is defined as "the number of business days in the standard securities settlement cycle in the United States, as defined in paragraph (a) of SEC Rule 15c6–1 [T+2], plus two business days."3 Reg T thus requires broker-dealers to secure from their customers payment in cash accounts or margin in margin accounts, within four business days of trade date (T+4). Reg T provides certain limited exceptions to this requirement in certain situations, including, with respect to purchases of when-issued securities and "delivery against payment" transactions in cash accounts.

With respect to when-issued securities, in cash accounts, Reg T requires full cash payment within one "payment period" of the date the security "was made available by the issuer for delivery to purchasers."4 Accordingly, in a cash account, a customer is not required to make payment within four days (T+4) after the purchase transaction is executed, but rather four days after the issuance or distribution of a when- issued security. With respect to "delivery against payment" transactions, the broker-dealer has up to 35 calendar days (T+35) to obtain payment "if the security is delayed due to mechanics of the transaction and is not related to the customer's willingness to pay."

FINRA Rule 4210

FINRA Rule 4210 builds on the requirements of Reg T to impose further requirements on FINRA member broker-dealers with respect to their credit activities, including the treatment of when-issued securities transactions. As a general matter, FINRA Rule 4210 requires when-issued transactions to be treated as if the securities were issued on the trade date in both cash and margin accounts. However, FINRA Rule 4210 provides certain limited exceptions to this requirement with respect to cash accounts. Specifically, rather than obtaining cash payment, broker-dealers can choose to take capital charges for any net mark to market loss on transactions or net positions in when issued securities in cash accounts of FINRA members or "designated accounts."5 Additionally, neither margin nor capital charge requirements apply to when-issued securities in cash accounts when the securities "are the subject of a primary distribution in connection with a bona fide offering by the issuer to the general public for cash."6 Finally, the current rule states that "the amount of margin … required by any provision of [Rule 4210] shall be obtained as promptly as possible and in any event within 15 business days from the date such deficiency occurred."7

As a practical matter, the industry has viewed the current rule as permitting extended settlements in certain situations involving when issued securities. The exception for primary distributions to the general public has been widely viewed as applying to all registered offerings, including debt offerings, and has even been extended in some cases to Rule 144A offerings.

Proposed Amendments to FINRA Rule 4210

Definition of "Extended Settlement Transaction"

In the proposed amendments, FINRA brings clarity on a fundamental level to the question of when a broker-dealer is required to obtain margin in this context by introducing a definition of "extended settlement transaction." Under the proposed new FINRA Rule 4210(a)(18), "extended settlement transaction" is defined as:

"any contract for the purchase or sale of a security (including any exempted security) that does not provide for the payment of funds by the customer (in the case of a customer purchase) or delivery of securities by the customer (in the case of a customer sale) by the second business day after the date of the contract."

In turn, the proposed rule would expressly require all extended settlement transactions to be margined as though they were in margin accounts, except for specifically excepted transactions. In explaining the application of the definition, FINRA highlights that a transaction in relation to which a firm accepted in good faith a customer's agreement to pay within T+2 but for which the customer was only able to make payment on T+3 due to an unexpected issue would not be an extended settlement transaction. FINRA states, however, that if settlement within T+3 is agreed to in advance or if the firm does not have a good- faith belief in settlement in T+2 the transaction would be an extended settlement transaction. Accordingly, the proposed rule would make clear that firms are not able to rely on the additional two-day cure period afforded by Reg T for payment in cash accounts or margin in margin accounts unless the firm accepted in good faith the customer's agreement to pay in T+2 and payment was delayed up to an additional two business days due to unforeseen circumstances.

When-Issued Securities Transactions

Restriction of Public Offering Exception to Equity IPOs

As noted above, under the current rule, neither margin nor capital charge requirements apply to when- issued securities in cash accounts when the securities "are the subject of a primary distribution in connection with a bona fide offering by the issuer to the general public for cash."8 The proposed amendments would expressly narrow the scope of this exception to only apply to equity IPOs and thus exclude when-issued transactions in debt securities and secondary follow-on or exchange offerings of equity securities. In the release, FINRA acknowledges that certain firms have interpreted this provision more broadly to additionally capture these types of offerings, but states that its original intention with the exception was to only exclude equity IPOs and that the proposed amendments clarify that original intention.9

Ironically, while FINRA's proposal would exclude equity IPOs from the default requirement, equity IPOs (and other common stock offerings) for US issuers are among the offerings least likely to use an alternative settlement cycle. The existing computer systems used for equity trading are generally unable to accommodate extended settlement of an equity IPO. When extended settlement is used in common stock offerings, it is typically due to timing constraints imposed by foreign law (including requirements for delivery of "wet ink" signatures) and the practicalities of cross-border offerings.

However, FINRA's proposal could cause a substantial change in market practice for primary distributions of debt offerings. Due to the volume of documentation to be completed between the pricing and closing of those offerings,10 market practice for the vast majority of high-yield debt is a settlement cycle of T+4 to T+6. Similarly, a significant volume of investment grade and convertible debt offerings settle between T+3 and T+5. Movement to a T+2 settlement cycle could result in delayed launches (due to a need to get more documentation into place prior to pricing), as well as increased negative carry by issuers when they issue new debt prior to completion of a redemption notice period or completion of a tender offer. Unfortunately, this change could eliminate much of the benefit provided by the Securities and Exchange Commission's (SEC's) recent relief on debt tender offers that permitted "five business day" tender offers to allow issuers and investors to better align settlement and funding dates; that synchronization requires at least a T+5 settlement cycle for an offering that prices on the day of launch. The use of a T+2 settlement cycle may also be problematic for acquisition financings, as practical realities (and regulatory approvals) necessitate additional notice periods prior to selecting a closing date (and a failed offering often results in a funded bridge loan, which cannot be documented in such a short period of time).

New Exceptions for US Treasury and Municipal Securities

FINRA acknowledges in the release that the public offering exception historically has been interpreted by firms to except new issuances of US Treasury securities and municipal securities and, based on its belief that these transactions present low risks relative to other non-equity offerings, proposes new exceptions to avoid disruptions to these markets. The new exceptions would specifically allow for settlement within T+14 for new issuances of US Treasury securities and T+42 for new issuances of municipal securities.

Allowing for Capital Charges in Lieu of Payment in Cash Accounts for Exempt Accounts, Non-Member Broker-Dealers, and Bona Fide DVP Customers

As noted above, under the current rule, firms can choose to take capital charges for any net mark-to-market loss on transactions or net positions in when-issued securities in cash accounts of FINRA members or "designated accounts" rather than obtain cash payment.11 The proposed amendment would extend this exception to "exempt accounts," an existing definition under the current rule that includes designated accounts, non-member broker-dealers (including foreign broker-dealers), and certain institutional investors that (i) have a net worth of at least US$45 million, (ii) have assets of at least US$40 million, and (iii) make available certain information through public filings or otherwise regarding ownership, business operations, and financial condition. The proposed amendment would also present this option to firms for "bona fide DVP customers," a new definition that would capture customers with whom the firm has a delivery versus payment (DVP) /receive versus payment (RVP) arrangement that satisfies the requirements of FINRA Rule 11860.

Other Changes

The proposed amendments would make certain other clarifications and changes, including by introducing certain new specific extended settlement transaction categories in relation to which the margin requirement may be delayed for certain periods of time.

Takeaways

The regulation of extended settlement transactions has long been a murky and arcane area, and clarity is welcome. However, if the proposed amendments are adopted as proposed, they could significantly change the practical settlement landscape. There are a number of situations in which extended settlements are a necessary and important structural mechanism and, while the proposed amendments create some useful bright lines, there remain many commonplace situations that practically require extended settlement. For example, many cross-border offerings are practically impossible to implement without extended settlement. Moreover, while firms do have the option to take a capital charge in lieu of collecting margin in certain situations, this option could lead to an increase in the cost of capital, which will either be borne by member firms or passed on to issuers.

While the proposed amendments seek to clarify FINRA's views on margin requirements, the policy needs for such action are worth considering further. That is: Is the credit risk mitigation that FINRA is seeking to achieve worth the inevitable increase in the cost of capital and the difficulties that shorter settlement of certain offerings will cause?

Comments on the proposed amendments must be submitted to FINRA by May 14, 2021.

Latham & Watkins LLP – Senet S. Bischoff, Gregory P. Rodgers, Stephen P. Wink and Naim Culhaci

April 13 2021

Firm Settles FINRA Charges for Placing "Throw-Away" Bids.

A firm settled FINRA charges for placing bids that were well under market value in response to bid-wanted auctions or requests for quotes ("RFQs") in municipal securities. As a result of this action, the firm was found to have failed to exercise its best judgment in determining the fair market value ("FMV") of the securities.

In a Letter of Acceptance, Waiver and Consent, FINRA found that after the firm responded to the RFQs and the below-FMV bids had been accepted, the firm then re-offered the bonds at significantly higher prices "consistent with independent market activity" (i.e., the re-offer price aligned with previously reported trades in the bonds). FINRA stated there was no market news to justify the spread between the firm's bid to the issuer and its re-offer prices. The firm was found in violation of MSRB Rules G-13 ("Quotations Relating to Municipal Securities") and G-17 ("Conduct of Municipal Securities and Municipal Advisory Activities").

Additionally, FINRA found the firm had no written supervisory procedures ("WSPs") that referenced MSRB Rule G-13, nor did the WSPs identify who was responsible for reviewing quotations in municipal securities. As a result, the firm was found in violation of MSRB Rule G-27 ("Supervision").

To settle the charges, the firm agreed to (i) a censure; (ii) a $80,000 fine ($40,000 for violations of MSRB Rules G-13 and G-17, and $40,000 for violations of MSRB Rule G-27); and (iii) an undertaking to revise its WSPs to remedy the relevant deficiencies.

Cadwalader Wickersham & Taft LLP

April 15 2021

The End of LIBOR: Transitioning to an Alternative Interest Rate - SIFMA Submission

SUMMARY

Submission for the Record by SIFMA before the U.S. House Committee on Financial Services Committee Subcommittee on Investor Protection, Entrepreneurship and Capital Markets in the hearing: "The End of LIBOR: Transitioning to an Alternative Interest Rate Calculation for Mortgages, Student Loans, Business Borrowing, and Other Financial Products"

SIFMA believes that Federal legislative action is necessary to address the set of issues that we discuss further below in order to facilitate the smooth transition from LIBOR to alternative reference rates. In particular, there is a large stock of existing contracts and instruments that, as a practical matter, cannot be amended to utilize alternative rates.

SIFMA is supportive of Federal legislation aligned with recommendations from the Alternative Reference Rates Committee ("ARRC") to address these situations where contracts cannot be easily transitioned from LIBOR due to legal or regulatory reasons. We believe such legislation would benefit all market participants including LIBOR's end users, from investors to companies to consumers, and would provide four key benefits: (1) certainty of outcomes, (2) fairness and equality of outcomes, (3) avoidance of years of paralyzing litigation, and (4) preservation of liquidity and market resilience.

Read the SIFMA Testimony.

SIFMA: Joint Trades Letter on LIBOR Contracts

SUMMARY

SIFMA and the undersigned organizations write in support of federal legislation to address "tough legacy"contracts that utilize LIBOR. There are trillions of dollars of outstanding contracts, securities, and loans that use LIBOR for their interest rates but do not have appropriate contractual language to address a permanent cessation of US dollar LIBOR, which will occur in June 2023.

Existing interest rate fallback provisions may not address the issue at all, may result in adjustable-rate contracts becoming fixed-rate contracts based on the last known LIBOR, or may defer to a party's judgement to replace LIBOR with a comparable interest rate index.

In any case, it is likely that ineffective or ambiguous fallback provisions will result in uncertainty, litigation, and harm to consumers, businesses, and investors.

Read the SIFMA letter.

Moving on from LIBOR (Update) - Squire Patton Boggs

Amid the world's turmoil, we can take comfort in the persistent march of long-foretold events. Keeping to their pre-pandemic promises (at least partially), the Federal Reserve and U.K. regulators[1] of LIBOR have reaffirmed their plans to cease publication of the one-week and two-month LIBORs by the end of 2021. Issuers, holders, and counterparties are slowly and grudgingly waking up to this reality. How are they responding?

Continue Reading

By Johnny Hutchinson and Sandy MacLennan on April 15, 2021

Squire Patton Boggs

LIBOR Legislation Bill Passed by New York State Legislature: McGuireWoods

On March 24, 2021, the New York State legislature passed a Senate Bill (the **Bill**) regarding the discontinuation of USD LIBOR, which will cease in mid-2023. New York State Governor Andrew Cuomo signed the Bill into law on April 6, 2021.

The new law applies with respect contracts governed by New York law for which U.S. dollar LIBOR (**USD LIBOR**) is used as an interest rate benchmark. Similar to the version of the legislation that the ARRC originally proposed in March 2020, the final law, among other provisions, (i) prohibits a contract party from refusing to perform its contractual obligations or declaring a breach of contract as a result of LIBOR discontinuance or the use of the legislation's recommended benchmark replacement, (ii) establishes that the use of the ARRC-recommended benchmark replacement (which will be based on the Secured Overnight Financing Rate (or SOFR) is a commercially reasonable substitute for and a commercially substantial equivalent to LIBOR, and (iii) provides a safe harbor from litigation for the use of such ARRC-recommended benchmark replacement. The proposed legislation would not override existing contract language that specifies a non-LIBOR based rate as a fallback to LIBOR (e.g., the prime rate). For this reason, market participants have observed that the law may not have a significant impact on New York law-governed bilateral and syndicated business loans, which generally provide that if USD LIBOR is not available an alternate base rate (such as the prime rate or fed funds) will be used under such contract. In addition, because the law applies only to New York law-governed contracts referencing USD LIBOR, it will not affect contracts governed by the law of other states or countries or contracts referencing LIBOR for other currencies.

The law has been welcomed by market participants, as it reduces uncertainty and economic impacts surrounding the transition by providing a means of transitioning 'tough legacy' New York law contracts that do not include effective fallbacks.

The text of the legislation was presented by the ARRC in 2020, more details of which can be found in our earlier blog post. The ARRC have endorsed Governor Cuomo's decision to sign the legislation into law, labelling it a "critical step in facilitating a smooth transition away from LIBOR". It remains to be seen whether federal legislation will be adopted alongside this New York State legislation, though the introduction of a draft discussion bill to the U.S. Congress in October 2020 suggests that such legislation could progress over the course of 2021.

Please contact any of the authors of this briefing or your regular McGuireWoods contact if you have questions about, or would like assistance with, the LIBOR transition.

By Donald A. Ensing, Barlow T. Mann, Jennifer J. Kafcas, Alvino S. van Schalkwyk & Harry Poland

April 15, 2021

McGuireWoods LLP

The End of LIBOR: Transitioning to an Alternative Interest Rate Calculation for Mortgages, Student Loans, Business Borrowing, and Other Financial Products

Mark Van Der Weide, General Counsel

Before the Subcommittee on Investor Protection, Entrepreneurship, and Capital Markets, Committee on Financial Services, U.S. House of Representatives, Washington, D.C.

Chairman Sherman, Ranking Member Huizenga, and members of the subcommittee, thank you for the opportunity to appear today. My testimony will discuss the importance of ensuring a smooth, transparent, and fair transition away from LIBOR (formerly known as the London interbank offered rate) to more durable replacement rates, as well as some of the challenges posed by this transition.

Before I delve into those issues, however, it may be helpful to review how LIBOR is used and why it will be discontinued.

LIBOR measures the average interest rate at which large banks can borrow in wholesale funding markets for different periods of time, ranging from overnight to one month, three months, and beyond. LIBOR is an unsecured rate that measures interest rates for borrowings that are made without collateral. Over the past few decades, LIBOR became a benchmark rate used to set interest rates for commercial loans, mortgages, derivatives, and many other products. In total, U.S. dollar LIBOR is used in more than $200 trillion of financial contracts worldwide.

By now the flaws of LIBOR are well documented.1 One of the fundamental problems is that LIBOR purported to be a representation of the actual funding costs of large banks in the London interbank market, but the evolution of that market over the years meant that, for many tenors, banks were estimating the likely cost of such funding rather than reporting the actual cost. This increasing element of subjectivity and discretion, coupled with the mechanisms that had been adopted to aggregate various banks' inputs into the determination of LIBOR, made the rate vulnerable to collusion and manipulation. Particularly after the global financial crisis of 2008, as banks sharply reduced their reliance on wholesale unsecured funding, there were few actual funding transactions on which to base a rate for many tenors of LIBOR.

While banks are, of course, not required to price their credit as a direct function of their cost of funding or on any amalgam of actual transaction data, the LIBOR mechanism—by purporting to be a measure of such costs even though there were not sufficient transactions to justify that perception—had become potentially misleading to many of those relying on it for credit pricing and other decisions. Over time, with a large number of contracts referencing a thinly traded rate, the incentive to manipulate LIBOR grew and actual manipulation of LIBOR abounded.

Following the exposure of these weaknesses, and the imposition of material legal penalties on a number of banks and individuals that engaged in misconduct related to the setting of LIBOR rates, the great majority of the banks that had provided submissions to be used in the setting of LIBOR (the so-called panel banks) determined that they would not continue participating in the process. This was not the result of a regulatory or legal requirement to end LIBOR. It was a private sector decision to stop providing what had always been a completely voluntary service, given the firms' assessment of the costs and benefits of doing so. While regulators are appropriately focusing on whether financial firms have prepared themselves for the date when the panel banks have said they will no longer provide LIBOR, the decision to end LIBOR itself has not been a governmental decision, but a private sector development.

Last month, LIBOR's regulator in the United Kingdom announced that the one-week and two-month U.S. dollar LIBOR term rates will cease to be published at the end of 2021, while overnight and other LIBOR term rates will cease to be published on a representative basis in mid-2023.2 This definitive announcement about the end of panel-based LIBOR underscores the importance of transitioning away from this moribund benchmark rate.

Efforts to Transition Away from LIBOR

Market participants, regulatory agencies, consumer groups, and other stakeholders have put in a great deal of work to prepare for life after LIBOR. Beginning in 2013, the domestic Financial Stability Oversight Council and the international Financial Stability Board expressed concern that the decline in unsecured short-term funding by banks could pose serious structural risks for unsecured benchmarks like LIBOR.3 To mitigate these risks and promote a smooth transition away from LIBOR, the Federal Reserve convened the Alternative Reference Rates Committee (ARRC) in November 2014. Recognizing that the private sector must drive this transition, the ARRC's voting members are private-sector firms. The Federal Reserve and the other agencies testifying today are ex-officio members of the ARRC.

The ARRC set about to identify alternative reference rates that were rooted in transactions from an active and robust underlying market. In June 2017, the ARRC identified the Secured Overnight Financing Rate (SOFR) as its recommended alternative to U.S. dollar LIBOR. SOFR is a broad measure of the cost of borrowing cash overnight, collateralized by Treasury securities. The Federal Reserve Bank of New York publishes SOFR each morning. Unlike LIBOR, SOFR is based on a market with a high volume of underlying transactions—regularly around $1 trillion daily. The ARRC developed a multi-step plan in October 2017 to facilitate the transition from LIBOR to SOFR.

The Federal Reserve and other agencies also sponsored a series of workshops with lenders and borrowers that focused on the use of credit-sensitive alternative reference rates for loans. Relatedly, the Federal Reserve, Office of the Comptroller of the Currency (OCC), and Federal Deposit Insurance Corporation (FDIC) issued a statement last year to emphasize that a bank may use any reference rate for its loans that the bank determines to be appropriate for its funding model and customer needs.4 The statement also noted, however, that a bank's loan contracts should include robust fallback language that provides for a clearly defined alternative reference rate to be used if the initial reference rate is discontinued.

Supervisory Efforts
Beginning in 2018, Federal Reserve staff began outreach to supervised institutions and examiners to raise awareness about, and encourage preparation for, the transition away from LIBOR. In 2019, we established a LIBOR Transition Working Group to coordinate monitoring of the transition and develop supervisory plans to assess banks' preparation efforts.

In November 2020, the Federal Reserve, OCC, and FDIC sent a letter to the banking organizations that we regulate, noting that there are safety and soundness risks associated with the continued use of U.S. dollar LIBOR in new transactions after 2021.5 Accordingly, we have encouraged supervised entities to stop using LIBOR in new contracts as soon as practicable and, in any event, by the end of this year. Federal Reserve Vice Chair for Supervision Randal Quarles emphasized in a recent speech that banking firms should be aware of the intense supervisory focus the Federal Reserve is placing on the LIBOR transition, and especially on plans to end issuance of new LIBOR contracts by year-end.6

Legacy Contracts
A key question is whether existing LIBOR-based contracts (legacy contracts) can seamlessly transition to alternative reference rates when LIBOR ends. The ARRC recently estimated that 35 percent of legacy contracts will not mature before mid-2023. Some of these legacy contracts have workable fallback language to address the end of LIBOR, but others do not. For example, most business loans have workable fallback language—by their terms, business loans generally fall back to an alternative floating rate, such as the prime rate. Similarly, most derivatives are governed by a master agreement published by the International Swaps and Derivatives Association (ISDA), and ISDA has published a "protocol" that allows derivative counterparties to amend their master agreements, on a multilateral basis, so that their derivative contracts fall back to a floating SOFR-based rate for counterparties that adhere to the protocol. Conversely, many floating-rate notes and securitizations have problematic fallback language—generally, these contracts convert to fixed-rate instruments at the last published value of LIBOR. Moreover, the rate terms in floating-rate notes and securitizations can typically be changed only with the unanimous consent of all noteholders, which typically would be difficult to secure.

The end of LIBOR may result in significant litigation. For example, if a legacy contract converts to a fixed rate when LIBOR ends, a party disadvantaged by that conversion might request that a court reform the contract by substituting an alternative floating rate for LIBOR.7 Parties also might request that a court reform or void a legacy contract that lacks any fallback language if the parties cannot agree bilaterally on a successor rate.8 Similarly, in instances where a legacy contract allows a person to select a replacement rate when LIBOR ends, a party disadvantaged by the replacement rate might argue that the manner in which another person—for example, a bond trustee—selected the replacement rate violates the implied covenant of good faith and fair dealing.9

Chair Powell and Vice Chair Quarles have publicly stated their support for federal legislation to mitigate risks related to legacy contracts. Federal legislation would establish a clear and uniform framework, on a nationwide basis, for replacing LIBOR in legacy contracts that do not provide for an appropriate fallback rate.10 Federal legislation should be targeted narrowly to address legacy contracts that have no fallback language, that have fallback language referring to LIBOR or to a poll of banks, or that convert to fixed-rate instruments. Federal legislation should not affect legacy contracts with fallbacks to another floating rate, nor should federal legislation dictate that market participants must use any particular benchmark rate in future contracts. Finally, to avoid conflict of laws problems, federal legislation should pre-empt any outstanding state legislation on legacy LIBOR contracts.

Thank you. I look forward to your questions on this important matter.

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1. Jerome H. Powell, Reforming U.S. Dollar LIBOR: The Path Forward (speech at the Money Marketeers of New York University, New York, NY, September 4, 2017).

2. See https://www.fca.org.uk/news/press-releases/announcements-end-libor.

3. See Financial Stability Oversight Council, 2013 Annual Report (Washington: Department of the Treasury, 2013); and Financial Stability Board, Reforming Major Interest Rate Benchmarks (Basel, Switzerland: Financial Stability Board, July 2014).

4. SR letter 20-25: Interagency Statement – Reference Rates for Loans.

5. SR letter 20-27: Interagency Statement on LIBOR Transition.

6. Randal K. Quarles, Keynote Remarks (speech via webcast at the SOFR Symposium, New York, NY, March 22, 2021). See also SR letter 21-7: Assessing Supervised Institutions' Plans to Transition Away from the Use of the LIBOR.

7. An aggrieved party might cite a variety of common law doctrines to justify judicial reformation, including mutual mistake, impracticability, and frustration of purpose. Although each of these doctrines sets a high bar for voiding or reforming contracts, it is difficult to predict how courts might rule on a contract-by-contract basis.

8. Again, parties might cite a variety of common law doctrines, including mutual mistake, impracticability, and frustration of purpose.

9. This covenant, which is implied in all contracts, generally embraces a pledge that neither party will do anything that has the effect of destroying or injuring the right of the other party to receive the fruits of the contract. See, e.g., ABN AMRO Bank, N.V. v. MBIA Inc., 17 N.Y.3d 208, 228-9 (N.Y. 2011).

10. The New York State Legislature recently enacted legislation that is intended to mitigate risks related to legacy LIBOR contracts, but that bill would apply only to contracts governed by New York law.

April 15, 2021

SIFMA: The Need for Federal Legislation in the Transition Away from LIBOR

On March 5, ICE Benchmark Administration confirmed its cessation plan for LIBOR. Most non-U.S. Dollar LIBOR tenors will cease on December 31, 2021. To provide a smoother transition for legacy instruments, U.S. Dollar denominated LIBOR, the largest and most important tenors of LIBOR, cessation will occur on June 30, 2023. LIBOR has a definitive end date, and regulators are demanding in no uncertain terms that their regulated institutions to move away from LIBOR this year.

There are undoubtedly certain issues requiring legislative action to guide the transition away from LIBOR to alternative reference rates. In particular, there is a large stock of existing contracts and instruments that as a practical matter cannot be amended to utilize alternative rates. SIFMA is supportive of Federal legislation aligned with recommendations from the Alternative Reference Rates Committee, or ARRC, to address these situations where contracts cannot be easily transitioned away from LIBOR due to legal or regulatory reasons.

We believe such legislation would benefit all market participants including LIBOR's end users, from investors to companies to consumers, and would provide four key benefits: (1) certainty of outcomes, (2) fairness and equality of outcomes, (3) avoidance of years of paralyzing litigation, and (4) preservation of liquidity and market resilience.

Continue reading.

April 13, 2021

SIFMA Podcast: The Need for Federal Legislation in the LIBOR Transition

In the latest in SIFMA's podcast series, SIFMA president and CEO Kenneth E. Bentsen, Jr. is joined by Chis Killian, SIFMA managing director, securitization and credit, to talk about the need for Federal legislation in the transition away from LIBOR.

SIFMA is supportive of Federal legislation aligned with recommendations from the Alternative Reference Rates Committee to address these situations where contracts cannot be easily transitioned from LIBOR due to legal or regulatory reasons. We believe such legislation would benefit all market participants including LIBOR's end users, from investors to companies to consumers, and would provide four key benefits: (1) certainty of outcomes, (2) fairness and equality of outcomes, (3) avoidance of years of paralyzing litigation, and (4) preservation of liquidity and market resilience.

Transcript

Edited for clarity

[Ken Bentsen] Thank you for joining us for this episode in SIFMA's podcast series. I'm Ken Bentsen, SIFMA's president and CEO. I'm joined today by my colleague, Chris Killian, SIFMA managing director, securitization and credit, for a conversation on the transition away from LIBOR and, in particular, the need for federal legislation to aid that transition.

SIFMA has been engaged on this issue for seven years, since the Alternative Reference Rate Committee, or ARRC, began working on a replacement for LIBOR in the United States. It's a priority for both the industry and the official sector. Chris, can you give us the current state of play?

[Chris Killian] To start, LIBOR is referenced in approximately $223 trillion of financial products. And it's a very shaky foundation because LIBOR is intended to measure interbank lending costs, but those transactions upon which LIBOR is supposed to be based have dwindled in numbers over the years as financial markets and bank-funding models have evolved. Much of today's LIBOR submissions is derived from estimates of transactions and not actual transactions.

So global regulators saw the problem with placing the foundation for global financial markets on this sort of construct nearly 10 years ago, and they began to examine how more-robust alternative reference rates could be identified or developed to replace LIBOR. Since then, and really ramping up in 2017, the key message from the regulatory community has been and continues to be that LIBOR isn't suitable and that market participants must transition to alternative reference rates.

The ARRC, which SIFMA is a member of, identified SOFR as the preferred alternative to LIBOR. In contrast to LIBOR, SOFR is fully transaction-based, referencing the previous day's activity in the repurchase markets, which are very liquid and very active — such that SOFR is based on approximately a trillion dollars of daily transactions that come from a wide range of market participants. And SOFR is administered and published by the New York Fed.

What's clear is that LIBOR is going away. There's no doubt about that. In December, there were finalizations [on] proposals from the administrator of LIBOR and the FCA in the U.K., which is its regulator, that most non-U.S. dollar LIBOR tenors will cease publication on December 31st of this year. The main U.S. dollar LIBOR tenors are going to cease on June 30th, 2023. And it's important to note two less used U.S. dollar LIBOR tenors will also cease at the end of this year, but the real deadline in the U.S. is June 2023.

[Chris Killian] Ken, here's a question for you: Of the $223 trillion in outstanding LIBOR transactions, the ARRC estimated that 67 percent of that would roll off by June 2023, which leaves about 74 trillion in LIBOR exposure that ends beyond June 2023. What happens to that exposure?

[Ken Bentsen] About $68 trillion of that is comprised of swaps, futures, and related transactions. And many but not all of those transactions can be amended and addressed by industry-wide protocols, such as the ISDA protocol, or by actions by clearinghouses to convert the outstanding positions.

But the remaining $6 trillion or so of exposures are comprised of various types of cash products: bonds, notes, loans, asset-backed securities, and other extensions of credit. The ARRC estimates that about $1.9 trillion of this is comprised of bonds and securitizations, which commonly do not have fallback provisions.

Many of these products were not designed at the time of issuance with a permanent cessation of LIBOR in mind, and in many cases these products are difficult or effectively impossible to amend due to regulatory constraints or practical issues, such as identifying all of the holders of a widely distributed security.

There are tens of thousands of floating-rate securitizations and corporate-bond transactions, and some of those contracts don’t have fallbacks. More commonly, the fallback provisions would result in a floating-rate bond becoming a fixed-rate bond or other contracts’ fallback to the judgment of an issuer, administrator, or other party.

In other words, from a practical standpoint, the existing fallbacks aren’t effective. The outcome of a permanent cessation of LIBOR may frequently not be in line with the expectations of the issuers, investors or customers, and may lead to vast amounts of litigation that ties up courts for years and causes major disruptions in financial markets and with investor portfolios.

The ARRC has taken steps to address this in New York state, where many financial contracts, certainly not all, are governed by New York state law. Chris, do you want to talk about what was done there?

[Chris Killian] The legacy problem was clear to the ARRC, and the ARRC created a working group to look at options and develop recommendations for how to deal with these legacy transactions that we like to call “tough legacy transactions.”

In March of 2021, the ARRC published a proposal for a statutory mechanism to address these ineffective tough legacy transaction fallback provisions, and what the legislation would do is it would create a statutory safe harbor from litigation and replace LIBOR-based fallbacks with those that are recommended by the ARRC, the Federal Reserve, or the New York Fed. And these would be based on SOFR.

The goals of the approach are manifold. One is to provide certainty of outcomes to contract participants. Another is to make sure that those outcomes are equal and fair across all of the market participants. And finally, ultimately this is being done to promote the liquidity and stability of financial markets.

Given that many financial contracts are governed by New York state law, the ARRC initially proposed this legislation in the state of New York. SIFMA supported it — supported the publication of the language and advocated for its passage in New York. And just a couple weeks ago, the New York Assembly and Senate passed legislation that’s in line with the ARRC’s recommendation on a nearly unanimous vote, and the governor signed the bill. So, Ken, while the New York state legislation is a positive outcome and something we’re very happy to see, we believe there’s more to be done at the federal level. Can you talk about the reasons for why that is?

[Ken Bentsen] While, as you said, the New York legislation is quite useful in regard to New York-governed instruments or contracts, it’s not a full solution for many of the instruments or contracts that are not governed by New York law or addressing such federal issues as the Trust Indenture Act, which is a key factor in this, as well.

Only federal legislation can apply a standard uniformly across all the states, and certainly only federal legislation can affect the Trust Indenture Act. A uniform federal law can promote the benefits provided by New York state for contract certainty, fairness, and equality in outcomes and avoid some litigation in market liquidity across the nation.

While certainly it’s conceivable that 49 other states, plus other territories and jurisdictions like the District of Columbia, could attempt to enact similar legislation to New York, it’s not really practical and would take a tremendous amount of time, definitely exceeding the period of time when LIBOR will cease to exist. So really, federal law is appropriate. And I might add: Given that the transition away from LIBOR is a federal public policy initiative and priority, it just underscores the need for federal legislation in and of itself.

In addition to this, I talked about the Trust Indenture Act being a federal statute. And the baseline of a trust indenture under the Trust Indenture Act requires unanimous consent to amend the document. In this case, the interest rate on the product. I might add – unless in the original contract, at that original point, that had been changed.

But in most cases, most of these contracts rely on the baseline unanimous consent. And that's not really practical because even if you could find all of the holders and get them to opine or take a position, you're not guaranteed that you would get 100 percent.

So federal legislation would provide narrow targeted relief that would allow contracts to transition to more-robust reference rates without having to deal with the really impossible hurdle of meeting unanimous consent requirements. And federal legislation could also ensure that there are not adverse tax or other consequences to issuers, holders, or consumers. In sum, federal legislation would offer a consistent outcome for all stakeholders and parties, and they would provide certainty about the outcome of the transition away from LIBOR.

And of course, lastly, federal legislation would help to avoid litigation gridlock, whether it's trustees seeking guidance from a court where it's not clear or various parties litigating over whatever fallback mechanism would be chosen without that certainty. And that's important not just to avoid unnecessary litigation but also to ensure market stability and liquidity.

Chris, obviously, a lot of work has been done over, really, the past seven years, since the formation of the ARRC. And then fast-forward 2017, with the establishment of SOFR, and now addressing these legacy contracts. What do you see next in terms of this? What's the status of potential federal legislation?

[Chris Killian] There was a hearing today, April 15th, in the subcommittee of the House Financial Services Committee, where legislation from Representative Brad Sherman, who's from California, was published and discussed. And the witnesses at the hearing were from federal regulators, like the Fed and the OCC and the Treasury.

The hearing, I think, was positive, and regulators expressed agreement with the need for federal legislation. And that legislation, hopefully, will expediently move through the congressional process because, despite the fact that the main U.S. dollar LIBOR tenors will be around until 2023, it takes a fair amount of time to implement changes.

In our mind, that legislation is something that needs to happen this year, as soon as it can. And that gives everybody ample time to change documents, update systems, be prepared to deal with different reference rates and all of those things that people need to do operationally and technically.

[Ken Bentsen] Great. Thank you, Chris. So, more to come. And I want to thank you for participating today, and also thank our listeners for tuning in to hear our views on this issue involving federal legislation and the transition away from LIBOR. To learn more about this issue and SIFMA and our various work to promote effective and resilient capital markets, please visit us at www.sifma.org. And thank you, again, for joining us.

April 19, 2021

Ken Bentsen is president and CEO of SIFMA and CEO of the Global Financial Markets Association.

Chris Killian is SIFMA managing director, securitization and credit

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MSRB Email Reminders for Recurring Financial Disclosures.

Read the MSRB publication.

S&P Credit FAQ: How S&P Global Ratings Thinks About LIBOR Risks In U.S. Public Finance

On March 5, 2021, the U.K. Financial Conduct Authority (FCA) announced the cessation of one-week and two-month U.S. dollar London Interbank Offered Rate (LIBOR) publication by ICE Benchmark Association (IBA) effective Jan. 1, 2022, followed by the cessation of overnight and 12-month LIBOR publication effective July 1, 2023. Although these announcements were expected, the 2023 date provides a longer time for issuers to prepare to transition their legacy contracts than was once anticipated.

Below, we answer some frequently asked questions regarding this announcement and the impact to U.S. public finance market participants

Frequently Asked Questions

How could this change affect a credit rating?

S&P Global Ratings' analysts continue to assess the financial exposure U.S. public finance (USPF) issuers could face due to financing and hedging transactions tied to LIBOR as well as management's preparedness to mitigate risks through proactive transitionary measures.

S&P Global Ratings' issuers need to remain mindful of the approaching deadline when considering and managing LIBOR-based debt instruments and derivatives by assessing potential exposure to LIBOR across all obligations. Additionally, we believe sound credit quality hinges on management demonstrating a strategy for transitioning to an alternative benchmark, including assessing the financial exposures of replacing it and limiting exposure to basis risk throughout the transition.

Although many market participants have yet to work with their counterparties to identify a successor benchmark or quantify the financial magnitude of transitioning to an alternative, we believe there is enough guidance from authorities to initiate the transition.

Nevertheless, S&P Global Ratings believes that the low notional amount of LIBOR exposure relative to overall debt portfolios should limit the extent of financial pressures and credit implications for USPF issuers. Given the recent announcement and permitted extension of LIBOR publication, S&P Global Ratings believes the transition of LIBOR has become less of an immediate threat as USPF issuers now have longer to prepare.

Does this announcement mean LIBOR is definitely going away?

We think it is likely the IBA and FCA will stop publishing LIBOR and that issuers should be

ready to transition as the recent announcement may affect trigger clauses in certain documents.

While the IBA has the ability to continue to post one-month, three-month, and six-month LIBOR for a period beyond June 30, 2023, the announcement by the FCA on March 5, while not unexpected, does potentially trigger LIBOR events found in many documents tied to issuer debt and derivative obligations and, consequently, issuers should be aware of the associated fallback language and how a replacement benchmark will be implemented with the cessation of LIBOR.

Despite the extension of LIBOR cessation through June 30, 2023, and potentially beyond for some tenors, U.S. authorities are still encouraging banks and borrowers to transition away from LIBOR by the end of 2021. As a result, the Federal Reserve, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency are no longer allowing new contracts to use LIBOR beyond December 2021 and, that being the case, we expect to experience an increase in alternative benchmark securities throughout the sector.

What ramifications will these trigger events have on issuers?

The trigger event indicates that a benchmark transition is underway, and issuers should identify the scope of impact and potential costs associated with transitioning to a new benchmark.

We believe that LIBOR trigger events that will affect the majority of USPF issuers will be predominately found in derivative agreements and are considered an index cessation event. The International Swaps and Derivatives Association (ISDA) published IBOR Fallbacks Protocol and Supplement, effective Jan. 25, 2021, where parties can adopt the protocol to amend outstanding agreements where upon the cessation of LIBOR, the replacement benchmark will be the Secured Overnight Financing Rate (SOFR) plus a credit adjustment spread.

In the U.S., the Alternative Reference Rate Committee (ARRC) was established to guide the transition away from LIBOR to SOFR. The ARRC has provided fallback language recommendations for floating rate notes as well as loan documents which provides issuers guidance to adopt new LIBOR based securities as well as amend existing obligations. On March 24, 2021, New York State's Senate and Assembly approved legislation that assists in the transition of legacy LIBOR contracts governed by New York State law that does not have fallback language. If signed into law, the legislation will provide fallback language similar to the ARRC and the replacement rate will be SOFR-based. Since most contracts reference New York State law, we believe this legislation could mitigate potential transition risks relating to fallback language.

The change in benchmark carries the potential for an increased cost of capital as well as reissuance costs that could negatively affect an issuer's budgetary performance, flexibility, and liquidity; consequently, management should be aware of the implication and act accordingly.

What will the new benchmark be and how has the U.S. market responded?

SOFR, a transaction-based interest rate which is based on overnight loans collateralized by U.S. Treasuries, will be the new benchmark rate supported by the ARRC and the U.S. market has been slow to shift to SOFR.

SOFR is traded with an average daily volume of more than $1 trillion in overnight treasury repo transactions, whereas LIBOR pales by comparison with a transaction volume of about $500 million. While the Federal Reserve Bank of New York began publishing SOFR overnight rates in April 2018, markets have been slow to adopt SOFR as a replacement rate despite seeing SOFR-linked debt issuances, derivatives, futures, and options all being exercised. Compared to the U.K's equivalent replacement Secured Overnight Index Average (SONIA) that has traded derivative notional totaling $3.4 trillion YTD compared to SOFR's $475.1 billion, we believe this indicates the U.S. market's burgeoning acceptance of this transition from LIBOR to SOFR. For more on the comparison between LIBOR and SOFR benchmark rates, see "SOFR Emerging as Alternative to LIBOR in U.S. Debt Markets," published Dec. 4, 2020, on Ratings Direct.

USPF exposure tends to be limited because of moderate use of variable-rate debt in the past decade thanks to an exceptionally low-interest-rate environment, which in turn limited the use of related swaps and hedges with LIBOR benchmarks

7 Apr, 2021

NY LIBOR Transition Legislation: Can We Now Stop Talking About LIBOR Fallbacks and Amendments?

On March 24, 2021, New York State's Senate and Assembly approved LIBOR transition legislation. New York Governor Andrew Cuomo's consent awaits and is expected as the governor indicated his support earlier this year.

The law will have limited impact on syndicated loan markets; the long-running discussion of LIBOR fallbacks and LIBOR transition amendments will continue. This is a positive step, however, for other debt markets where inclusion of LIBOR fallback language is not common.

The law closely tracks the text of legislation proposed by the Alternative Reference Rates Committee (ARRC), the committee established by the Federal Reserve Board and the New York Federal Reserve Bank to manage the transition from LIBOR. The law includes the following key provisions:

- It covers only contracts governed by New York State law. There are efforts to pass similar legislation at a federal level and in other states.
- It covers only LIBOR contracts that either (i) contain no methodology or procedure for determining the interest rate once LIBOR is not available (a fallback provision) or (ii) have a fallback provision using a different LIBOR-based rate as the fallback.
  Most sophisticated syndicated and bilateral loan agreements contain a fallback provision, even those agreements entered into prior to regular market use of the model ARRC fallback language. The ARRC "hardwired" or "amendment" fallback language provides for SOFR or a negotiated rate, respectively, to be used in the case of LIBOR termination. Pre-ARRC fallback language typically falls back to a prime interest rate.
  A significant number of other types of debt contracts, however, have no fallback language. This new law aims to provide a procedure for determining a fallback for this group of contracts. A recent Federal Reserve Bank "Progress Report" on the state of LIBOR transition estimates that $2 trillion of "tough legacy" LIBOR contracts exist without any fallback provisions. Many of these contracts exist in debt markets where amendments to debt contracts are difficult to obtain. These include certain types of securitizations, floating rate notes, mortgages, municipal bonds, and derivatives.
- It provides that the fallback for applicable contracts will be a SOFR-based interest rate similar to the approach of the ARRC hardwired fallback model language, and declares SOFR as a "commercially reasonable substitute for and a commercially substantial equivalent to LIBOR."

- It prohibits parties to applicable contracts from refusing to perform their obligations under the contracts as a result of application of the law, and provides a litigation safe harbor as a result of application of the law.
- It nullifies contractual fallback methodology relying on polls, surveys, and inquiries of dealers and lenders, more often found in certain derivatives and loan agreements. The law is not without potential controversy. Some commentators, including the New York City Bar Association (which supports the law), have noted that, in the case of contracts subject to the Federal Trust Indenture Act, application of the law may violate the Act. Other concerns with the law include possible federal and New York State constitutional claims to its legality.

Morrison & Foerster LLP – Geoffrey R. Peck

March 29 2021

FINRA Requests Comment on Proposed Amendments to the Margin Rule Regarding When Issued and Other Extended Settlement Transactions.

Comment Period Expires: May 14, 2021

Summary

FINRA seeks comment on proposed amendments to Rule 4210 (Margin Requirements) that would clarify and incorporate into the rule current interpretations regarding when issued and other extended settlement transactions, and provide relief to facilitate the application of the rule to these transactions.

The proposed rule text marked to show changes from the current rule text is available in Attachment A.

Two additional attachments are included to assist in the review of the proposed amendments. Attachment B consists of examples illustrating the operation of the rule under the proposed amendments. Attachment C is a flow chart outlining an analysis of the application of the proposed rule to these transactions. Attachments B and C are included for illustrative purposes only.

Continue reading.

GFOA New and Revised Best Practices and Advisories.

On March 5, GFOA's Executive Board passed several sweeping best practices and advisories regarding Environmental, Social and Governance (ESG) disclosures by municipal issuers as well as member alerts regarding LIBOR cessation and In-Kind Asset Transfers to Defined Benefit Pension Plans.

Please see below for details and links to the new and revised best practices and advisories:

GFOA Best Practice on ESG Disclosure

Governmental issuers are getting ahead of the curve by moving forward with voluntary best practices calling for governments to include information about climate risk and what it is doing to prepare for climate change and environmental events in their bond offering documents. This best practice is instructive on disclosure data already at hand and provides a template to move forward on environmental disclosures to all stakeholders. Specifically, this best practice ***recommends that governments evaluate the development and disclosure of information regarding the primary environmental risks applicable to municipal issuers and their bonds in their preliminary and final official statements used in connection with bond sales and in other voluntary disclosure. Governments should also disclose plans developed, strategies deployed, actions taken, and infrastructure built to address the environmental risks, which will vary depending on the geographical location of the issuer.***

VIEW BEST PRACTICE

GFOA Advisory on LIBOR Transition

Additionally, the GFOA Executive Board issued an advisory regarding the cessation of LIBOR. This is in addition to GFOA's suite of materials created with GFOA's Industry Workgroup on LIBOR including the Hunt for LIBOR and the ISDA Top Ten. For these resources and more, go to the LIBOR landing page. ***GFOA recommends that governments start planning for the phase out of LIBOR despite the ICE announcement that certain LIBOR tenors may continue to be published past the December 31, 2021, Cessation Date. Steps include identifying LIBOR exposure in contracts; consulting with municipal/swap advisors and bond counsel; determining whether, and obtaining, governing body approval to amend any contracts with LIBOR references; and determining whether changes in those contracts may trigger any disclosure and/or accounting reporting requirements. GFOA encourages governments not to enter into new contracts that reference LIBOR especially if the contract extends past the expected LIBOR Cessation Date.***

VIEW ADVISORY

GFOA Advisory on In-Kind Asset Transfer to Defined Benefit Pension Plans

Aggregating perspectives of GFOA members representing both general governments as well as administrators of defined benefit pension plans, this advisory ***does not recommend transferring ownership of government-owned infrastructure to a defined benefit plan for many reasons including:***

- The intangibility of the benefit to pensioners
- The significant liquidity risk of such a transaction and
- Valuation costs and irrevocability of such a transaction

VIEW ADVISORY

GFOA Best Practice on Issuing Taxable Debt

GFOA Executive Board renewed and enhanced the best practice on issuing taxable debt. ***GFOA recommends that state and local governments consider whether issuing taxable debt is the best financing option for their proposed project, and develop a thorough understanding of the differences between the tax-exempt and taxable markets before proceeding with a planned sale. Each issuer should conduct an analysis of how these differences will affect the overall financial plan and ability to manage its debt program, and consult appropriate counsel, and advisors.***

VIEW BEST PRACTICE

GFOA Best Practice on Managing Build America and Other Direct Subsidy Bonds

GFOA Executive Board renewed and enhanced the best practice on managing direct subsidy bonds. ***GFOA recommends that governments that issued BABs or other direct subsidy bonds, be acutely aware of their ongoing responsibilities associated with these bonds and be cognizant of Internal Revenue Service (IRS) actions related thereto. Additionally, if Congress reinstates direct subsidy bond programs, the GFOA advises governments to exercise caution and have a full understanding of the differences between tax-exempt bonds and direct subsidy taxable bonds.***

VIEW BEST PRACTICE

GFOA Best Practice on Sale of Bonds

GFOA Executive Board renewed and enhanced the best practice on selecting and managing the method of sale. ***When state and local laws do not prescribe the method of sale of debt, the Government Finance Officers Association (GFOA) recommends that issuers select a method of sale based on a thorough analysis of the relevant rating, security, structure and other factors pertaining to the proposed bond issue. If the issuer has in-house expertise (dedicated debt management staff whose responsibilities include daily management of a debt portfolio), this analysis and selection could be made by the issuer's staff. However, in the more common situation where an issuer does not have sufficient in-house expertise, this analysis and selection should be undertaken with the advice of a municipal advisor. Note: Municipal Securities Rulemaking Board (MSRB) Rule G-23 states that a firm may not serve as a municipal advisor and an underwriter on the same transaction.***

VIEW BEST PRACTICE

MBFA Submits Testimony to Ways and Means on Municipal Bond Hearing.

Today, the Municipal Bonds for America Council (MBFA) submitted testimony following the House Ways and Means Subcommittee on Select Revenue Measures March 11th hearing titled, "Tax Tools to Help Local Governments."

The MBFA testimony can be viewed here.

While the hearing covered a multitude of other tax issues, the majority of the discussion focused on municipal bonds in the context of infrastructure financing, highlighting many municipal market and MBFA priorities.

The MBFA testimony focuses on the Councils main legislative priorities:

- Restoration of tax-exempt advance refundings
- Expansion of PABs including ESG
- Raising the BQ debt limit; and
- Reinstatement of direct-pay bonds exempt from sequestration.

This week, the MBFA Steering Committee is hosting the legislative staff of Senator Roger Wicker (R-

MS), the sponsor of the LOCAL Infrastructure Act that would fully reinstate tax-exempt advance refundings, to discuss next steps in the Senate and possible reintroduction of the Senators American Infrastructure Bond legislation of the 116th Congress.

The MBFA will continue to provide details as they become available.

Bond Dealers of America

March 24, 2021

SEC 2021 Examination Priorities – Focus on Municipal Securities and Municipal Advisors - Ballard Spahr

The U.S. Securities and Exchange Commission's Division of Examination (Division) announced its 2021 examination priorities (the Report) on March 3, 2021. The Division's examination priorities reflect areas that present "heightened risks to investors or the integrity of U.S. Capital Markets."

This briefing discusses the following areas of the Division's 2021 focus:

- Respecting the importance of compliance departments
- Municipal advisors
- Environment, Social, and Governance (ESG) and how registrants are preparing for the expected discontinuation of the London Inter-Bank Offered Rate (LIBOR)

Looking back over 2020, the Division reported its satisfaction that firms delivered financial services "as they should have" in spite of the COVID-19 pandemic but noted their heightened and continuing concern about cybersecurity with the publication in 2020 of two cybersecurity risk alerts and a special report. The 2021 Report also discussed the completion of initial examinations of firms' implementation of Regulation Best Interest and the new Form CRS and provided guidance on successful implementation approaches.

Emphasis on the Critical Role Played by Compliance Departments

The Report included a strongly worded message about the critical importance of internal compliance programs at regulated entities, especially since an increasing number of staff of registered firms are working remotely. Based on "thousands of examinations of many different types of firms," the Report noted certain "hallmarks" of effective compliance programs including:

- a compliance department's active engagement in most facets of firm operations;
- early involvement by compliance in important business development, such as product innovation and new services;
  knowledgeable and empowered Chief Compliance Officers with full responsibility, authority, and resources to develop and enforce policies and procedures of the firm; and
- a commitment from C-level and similar executives to set a tone from the top that compliance is integral to the success of the firm and a continuous commitment to ensure adequate resources and tangible support for compliance at all levels of the firm.

Municipal Securities and Other Fixed Income Securities

In connection with a statement about the importance of timely and accurate municipal issuer disclosure as a result of the significant effects of the pandemic on the finances and operations of many municipal issuers, the Division stated it will examine the activities of broker-dealers and underwriters to assess whether they are meeting their respective obligations in relation to municipal issuer disclosure. This portends an examination of underwriter due diligence practices and SEC Rule 15c2-12 compliance in connection with municipal issuer offering documents. For a discussion of the SEC's views on municipal disclosure practices in the light of the pandemic, see our Mid-Year 2020 Newsletter here. In addition, the Division will focus on an examination of broker-dealer trading activity in the areas of best execution, fairness of pricing, mark-ups and mark-downs, commissions, and confirmation disclosure requirements.

Municipal Advisor Examination Topics

Throughout 2021, the Division plans to examine the following areas:

- Whether municipal advisors "adjusted their practices" in the light of the impact of COVID-19 on the finances and operations of municipal issuers. In the Report, the Division draws a clear connection between "the importance of timely and accurate municipal disclosures" which is "critical to investors" and the duties of municipal advisors. This emphasis may portend a closer examination of the scope of services provided by municipal advisors to issuers in the context of disclosure. The Report also stated that the Division intends to examine whether municipal advisors documented the scope of their client engagements as required under MSRB Rule G-42.
- Whether municipal advisors relied on the Temporary Conditional Exemption from the Broker Registration Requirements of Section 15(a) of the Exchange Act of 1934 for Certain Activities of Registered Municipal Advisors (June 16, 2020).

  Whether municipal advisors have met their fiduciary duty obligations to municipal entity clients in regard to their disclosure of and management of conflicts of interest.
- Whether municipal advisors satisfied registration, qualification, CLE and supervisory requirements.

LIBOR Preparedness, Municipal Advisors: The Division stated its intent to engage with municipal advisors to assess their understanding of their own exposure to LIBOR, their preparations for the expected discontinuation of LIBOR and the transition to an alternative reference rate in connection with their financial matters related to LIBOR, and most relevant, those of their clients.

This follows the MSRB's publication *LIBOR Transition Information* available here and the SEC's Office of Municipal Securities Staff *Statement on LIBOR Transition in the Municipal Securities Market* available here. In both statements, municipal advisors were advised that under MSRB Rule G-42, if a municipal advisor makes a recommendation of a municipal securities transaction or product involving LIBOR (or is asked to review a recommendation of a third party), it must have a reasonable basis to believe the transaction or product is suitable for that client. In addition, with respect to a recommendation, the municipal advisor must inform the client of the risk, benefits, structure, and other characteristics as well as the suitability basis for any recommendation.

LIBOR Preparedness, Underwriters of Municipal Securities: The MSRB LIBOR publication described above reminded underwriters of their duty to make particularized disclosures for underwritings deemed complex municipal securities financings, in which LIBOR related financings are included. The Report portends the enhanced examination of municipal underwriters and their G-17 disclosure obligations respecting instruments using LIBOR.

Market Regulatory Infrastructure

Acting SEC Chair Allison Herren Lee stated that the Division will continue its oversight of the

Financial Industry Regulatory Authority (FINRA) by "focusing on examinations on FINRA's operations and regulatory programs and the quality of FINRA's examinations of broker-dealers and municipal advisors." The Division will also examine the Municipal Securities Rulemaking Board (MSRB) to evaluate the effectiveness of its policies, procedures, and controls.

Our Municipal Securities Regulation and Enforcement Group and Public Finance Group continue to monitor any developments of the Division's exam priorities and findings as they relate to the municipal securities market.

By Kim Magrini, Rebecca Lawrence, Andy Miles

March 24, 2021

NFMA Releases White Paper on COVID Disclosure.

The NFMA has released a draft White Paper on Guidance & Insights Regarding Emergency Event Disclosure Affecting State & Local Governments: COVID-19 Focus for public comment through April 30, 2021.

To view the paper, click here.

National Federation of Municipal Analysts

SIFMA Statement on Passage of New York State LIBOR Legislation.

New York, NY, March 25, 2021 – SIFMA today issued the following statement from president and CEO Kenneth E. Bentsen, Jr. on the passage of LIBOR legislation by the New York State Legislature:

"We are pleased the New York State Legislature passed the model law for New York to help transition 'tough legacy' contracts that are difficult or practically impossible to amend. SIFMA, as a member of the Alternative Rates Reference Committee (ARRC), helped develop and championed this legislation to facilitate a smooth transition from LIBOR to an alternative reference rate, which is a top priority for the financial services industry. SIFMA supports market, legislative and regulatory efforts to ensure a smooth transition while avoiding market disruption and legal uncertainty, and to that end we encourage Congress to pass a federal law similar to the one passed in New York to address these issues on a national level."

GASB Publishes Annual Crain Grant Program Request for Research Proposals.

Request for Research Proposals.

03/22/21

MSRB Seeks Comment on Regulation of Solicitor Municipal Advisors.

The MSRB requested comment on proposed MSRB Rule G-46 ("Duties of Solicitor Municipal Advisors"), which would codify previously issued interpretive guidance concerning the requirements applicable to solicitor municipal advisors under MSRB Rule G-17 ("Conduct of Municipal Securities and Municipal Advisory Activities").

Proposed MSRB Rule G-46 would, among other things:

- require solicitor municipal advisors to record their relationships in writing;
- require that representations made by solicitor municipal advisors to solicited entities be accurate and not misleading;
- require additional compensation and conflict of interest disclosures; and
- establish standards concerning the timing and manner of the required disclosures.

The proposed rule would also conform certain requirements applicable to such firms to those that apply to (i) non-solicitor municipal advisors under MSRB Rule G-42 ("Duties of Non-Solicitor Municipal Advisors") and (ii) underwriters under MSRB Rule G-17, as they relate to the conduct of municipal securities and the activities of municipal advisors.

Comments on the proposed rule must be submitted by June 17, 2021.

Cadwalader Wickersham & Taft LLP

March 18 2021

FINRA Seeks Comment on Margining of Extended Settlement Transactions.

FINRA requested comment on proposed amendments intended to clarify the application of the FINRA Rule 4210 ("Margin Requirements") to "when issued" and other extended settlement transactions.

Among other things, the proposed amendments would:

- provide a definition for "extended settlement transaction" (generally T+2);

- subject to significant exceptions, require all extended settlement transactions and net positions resulting from extended settlement transactions to be margined as if they were in a margin account;
- exempt from the margining requirements (i) covered agency transactions, (ii) certain when-issued security transactions, (iii) certain refunding transactions and (iv) settlements extended as a result of the mechanics of a transaction with a bona fide delivery vs. payment ("DVP") customer;
- clarify that the scope of the public offering exception for when-issued transactions is limited to equity IPOs;
- provide new exceptions for when-issued transactions in U.S. Treasury (14 calendar days) and municipal securities (42 calendar days); and
- codify interpretations as to concentration and other limits on a firm taking capital charges taken in lieu of collecting margin.

Comments on the proposed amendments must be submitted by May 14, 2021.

Commentary

There is currently a fairly wide divergence as to the understanding of the regulations applicable to extended settlement transactions, not only as between member firms and FINRA, but even as between the member firms. This long-awaited FINRA proposal (which, if adopted, would be the most extensive amendments to Rule 4210 in over a decade) is a positive step forward in that it provides a means for a public discussion as to the appropriate requirements.

Although the issue has been a notable topic for years among market participants and FINRA, all broker-dealers should closely review their practices in this area. Among other things, firms should consider their settlement processes as to new issues, both public and private, so as to determine whether these practices would conform to the FINRA proposal, and whether they should put in a comment.

Cadwalader Wickersham & Taft LLP – Nihal S. Patel

March 15 2021

[Are you Ready for the End of LIBOR? The Fed Issues Guidance on Assessing LIBOR Transition Progress - McGuireWoods]

On March 9, 2021, the Federal Reserve in its [Supervision and Regulation Letter] (the **Letter**) provided guidance to Federal Reserve examiners and supervised institutions to assist in assessing progress in preparing for the LIBOR transition.

Specifically, examiners are directed to review the supervised institutions' "planning for, and progress in, moving away from LIBOR." Supervised institutions should note that examiners are encouraged to consider taking supervisory action if an institution is not ready to cease issuances of new LIBOR-based contracts by the end of 2021.

In the Letter, the Fed recognizes that the transition plans will differ depending on the institution's LIBOR exposure and have provided separate guidance for those with less than $100 billion in total consolidated assets (**Small Firms**) and institutions with more than $100 billion in total consolidated assets (**Large Firms**). The guidance for both [Small Firms] and [Large Firms] sets out considerations for examiners in six key areas:

- **Transition planning:** Institutions should have plans in place to transition from LIBOR and the detail and scope of those plans should be commensurate with its LIBOR exposures. Large Firms should ensure that their LIBOR transition plans are more detailed and include a governance structure that clearly defines roles and responsibilities needed to execute the plan.
- **Financial exposure measurement and risk assessment:** Institutions should accurately measure their LIBOR exposures and report those exposures to senior management. Large Firms should ensure that reporting is done frequently, and that the institution can identify the proportion of its LIBOR exposure that runs off before the relevant LIBOR tenor ceases (for more information, please see our earlier blog post). Large foreign firms should measure LIBOR exposures booked and/or managed within the U.S., and be able to quantify exposures within their U.S. operations in comparison to the exposures of the foreign parent entity.
- **Operational preparedness and controls:** Institutions should identify internal and vendor-provided systems and models that use or require LIBOR and, wherever possible, make adjustments to ensure smooth operation of those systems and models upon the cessation of LIBOR. A contingency plan should be established in the event that a service provider is unable to deliver a solution in a timely manner.
- **Legal contract preparedness:** All LIBOR-referencing contracts should be identified, and new LIBOR-referencing contracts should have robust fallback language that includes a clearly defined alternative reference rate. Institutions should determine the impact of LIBOR's cessation on their contracts and take steps to modify those contracts prior to LIBOR's cessation. For institutions that are large users of derivatives, adherence to ISDA's IBOR Fallback Supplement and Protocol should be considered.
- **Communication:** Institutions should communicate with all counterparties, clients, consumers and internal stakeholders about the LIBOR transition, and ensure compliance with all applicable laws and regulations, and with the prohibition on engaging in unfair or deceptive practices. Large Firms should implement training for employees on the LIBOR transition, including how staff should communicate the implications of the transition externally.
- **Oversight:** Institutions should provide their LIBOR transition plans to management, and provide regular status updates to senior management. Foreign institutions with U.S. total assets exceeding $100 billion should provide status updates to the U.S. Chief Risk Officer and U.S. Risk Committee.

Based on this, supervised institutions should expect more scrutiny on their LIBOR transition plans in the upcoming weeks and months. Supervised institutions should ensure that they allocate sufficient resources and attention to their plans and be careful to ensure compliance with this guidance.

Please contact any of the authors of this briefing or your regular McGuireWoods contact if you have questions about, or would like assistance with, the LIBOR transition.

By Donald A. Ensing, Susan Rodriguez, Jennifer J. Kafcas, Alvino S. van Schalkwyk & Harry Poland on March 17, 2021

McGuireWoods LLP

Ridding Trust Indentures of Pesky Bearer Bond Language: Butler Snow

The euphemistically-named Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA"), that became law on September 3, 1982, required that tax-exempt obligations be in registered form (as well as denying certain tax benefits to non-tax-exempt obligations that are not in registered form). Prior to the enactment of TEFRA, virtually all municipal bonds were bonds payable to bearer, with payment coupons attached, and the bonds were printed by a handful of specialty printers, most notably Northern Banknote in Chicago. From the enactment of TEFRA until 1999, when The Depository Trust Company ("DTC") and National Securities Clearing Corporation combined and DTC began clearing municipal securities, tax-exempt bonds were typically printed by the same bond printers with a blank following "Registered Owner" into which would be typed the name of the owner of the bond. Beginning in 1999, tax-exempt bonds began being issued in book-entry form with the registered owner being Cede & Co., the nominee of DTC. Initially, bonds, which were now typically typewritten, had to be delivered physically to DTC prior to closing the bond issue. Within a few years, it became customary for bonds to delivered to the indenture trustee to be held in custody under the DTC Fast Automated Securities Transfer ("FAST") program.

Despite approaching 40 years since bearer bonds were eliminated and over 20 years since printed bonds were customary, 2021 trust indentures still often contain bearer-bond and printed bond concepts. A confession by the author – he is still attempting to weed out these concepts and definitions.

Temporary Bonds.

One still sees the following provision on occasion. Temporary bonds were infrequently issued in the days of printed bonds, but have unlikely been used since the early 2000s.

Pending preparation of definitive Bonds, or by agreement with the purchasers of all the Bonds, the Issuer may issue, and, upon its written direction, the Paying Agent shall authenticate, in lieu of definitive Bonds one or more temporary printed or typewritten Bonds in Authorized Denominations of substantially the tenor recited above.

Presentation of Bonds.

Book-entry bonds are not presented for payment – all payments of principal, premium, and interest are wired to DTC. Occasionally in private activity bond financings, subordinated bonds are issued as physical bonds rather than book-entry bonds and these provisions would be appropriate. In most instances, the requirements for presentment should be eliminated.

The principal of, and premium, if any, on the Bonds shall be payable upon presentation and surrender thereof at the principal office of the Trustee, or of its successor in trust.

Each notice of redemption shall specify the date fixed for redemption, the principal amount of Bonds or portions thereof ($5,000 or any integral multiple of $5,000 in excess thereof) to be redeemed, the redemption price, the place or places of payment, that payment will be made upon presentation and surrender of the Bonds to be redeemed, that interest accrued to the date fixed for redemption will be paid as specified in said notice, and that on and after said date interest thereon will cease to accrue.

Use of the term Bondholder.

Bondholder is a bearer bond concept – once bonds were held by the owners of the bonds, but for nearly four decades that has not been the case. It is still common to see various provisions in indentures require consent or direction of Majority Bondholders, often defined as follows,

"Majority Bondholders" means, at the time of determination, the Owners of a majority in principal amount of Bonds then Outstanding.

"Bondholders" or "Bondowners" or "Owners" means the Persons in whose names any of the Bonds

are registered on the books kept and maintained by the Paying Agent as bond registrar.

DTC is the Owner under these definitions and DTC is simply a nominee for its participants which hold bonds on behalf of the beneficial owners, the "true" owners of the bonds. Better defined terms are "Registered Owner" for DTC as the person in whose name the bonds are registered on the books kept by the bond registrar and "Beneficial Owner" for the true owners of the bonds who would give consent or direction.

Butler Snow LLP

March 16, 2021

Financial Accounting Foundation Appoints Robert W. Hamilton to the Governmental Accounting Standards Advisory Council.

Norwalk, CT—March 17, 2021 — The Board of Trustees of the Financial Accounting Foundation (FAF) has announced the appointment of Robert W. Hamilton to the Governmental Accounting Standards Advisory Council (GASAC). He is the statewide accounting and reporting manager for the state of Oregon.

Mr. Hamilton was nominated by the National Association of Auditors, Comptrollers and Treasurers (NASACT) and will assume the role vacated by the appointment of Alan Skelton to the position of director of research and technical activities of the Governmental Accounting Standards Board (GASB). He will serve a two-year term that began on February 23, 2021 and concludes December 31, 2022. He is eligible for reappointment for two additional two-year terms.

The GASAC is responsible for advising the GASB on technical issues, project priorities, and other matters that affect standards setting for accounting and financial reporting by state and local governments. Members of the GASAC represent a cross-section of the GASB's state and local government stakeholders, including users, preparers, and auditors of financial information. GASAC members are selected on the basis of their professional expertise and the depth and breadth of experience they bring to the GASAC.

"We are pleased to welcome Robert as a member of the GASAC," noted FAF Board of Trustees Chair Kathleen Casey. "His experience with the implementation of GAAP, in addition to his committed participation in the GASB task force advising the updating of the existing concepts on note disclosures, makes him a valuable addition to the Advisory Council," Ms. Casey added.

Mr. Hamilton has served the state of Oregon since 2012, advancing from senior accounting analyst to his current role. He is responsible for issuing the state's audited annual financial report, maintaining the state's accounting manual, overseeing the statewide accounts receivable management team, providing statewide direction on appropriate accounting practices, and leading statewide implementation of GAAP changes, among other duties.

He holds a bachelor of arts in accounting from the University of Oregon and is a certified public accountant. Mr. Hamilton is actively involved with the National Association of State Comptrollers (NASC), including as a member of its Executive Committee and NASACT.

FINRA Requests Comment on Rule 4210 – Follows BDA Member Recommendations.

Today, following extensive work with the BDA and its members, FINRA announced that they seek to comment on proposed amendments to Rule 4210 (Margin Requirements) that would clarify and incorporate into the rule current interpretations regarding when issued and other extended settlement transactions, and provide relief to facilitate the application of the rule to these transactions.

The BDA will host a call in the coming weeks to work on draft comments with membership. Comments are due May 14, 2021

The notice can be viewed here.

All BDA advocacy on Rule 4210 can be viewed here.

On extended settlement trades, FINRA intends to adopt these provisions:

- Extended settlement transaction will be defined as any time a trade is not funded by a customer within the standard T+2 settlement cycle. The rule will make clear that extended settlement is an extension of credit.
- The rule will permit a capital charge in lieu of customer-posted margin for trades with extended settlement cycles of up to 35 days with "DVP customers," a term which will be defined in the rule, for trades with settlements.

On when-issued transactions, FINRA intends to adopt these provisions:

- When-issued trades will be subject to the margin rule.
- The rule will permit capital charges in lieu of customer margin for all when-issued trades with "exempt accounts." That will be in addition to interdealer and designated trades which are exempted in the current rule.
- Exempt accounts will be defined as minimums of $45 million in financial assets, $40 million in net assets, and providing sufficient financial information to conduct a credit review.
- There will be an exception to margin requirements for trades in new-issue Treasury securities that settle within T+14 and new-issue municipal securities that settle within T+42.
- The rule will permit a capital charge in lieu of margin for DVP customers on when-issued new issues in general if the trades are settled soon after securities are issued.

Bond Dealers of America

March 15, 2021

SIFMA Amicus Brief: Walters, et al. v. J.P. Morgan Chase & Co., et al.

SUMMARY

Court:
U.S. Supreme Court

U.S. District Court
(E.D. Michigan)

Amicus Issue:
Whether municipal bond underwriters are potentially liable for any harms caused by the public works projects they help finance, and whether state law claims against such underwriters are preempted by the federal securities laws.

Counsel of Record:
Sullivan & Cromwell LLP

Download the Brief.

SEC Division of Examinations Announces 2021 Examination Priorities.

On March 3, the U.S. Securities and Exchange Commission's (SEC) Division of Examinations (Division), formerly known as the Office of Compliance Inspections and Examinations, announced its examination priorities for fiscal year 2021. The Division publishes the report annually to identify areas where it believes potential risks to investors and U.S. capital markets may exist. This year's report focused particularly on climate-related risks, conflicts of interests for brokers and investment advisers, and attendant risks related to fintech.

Below find a summary of the Division's 2021 examination priorities.

Retail Investors, Including Seniors and Those Saving for Retirement

The Division will continue to prioritize investments and services marketed to retail investors, including seniors and those saving for retirement. Specifically, the Division will focus on compliance concerns related to mutual funds and exchange-traded products, municipal securities and other fixed income instruments, and microcap securities. The Division will also review the use of primary tools for investor protection, such as Regulation Best Interest, Form CRS, and the Interpretation Regarding Standard Conduct for Investment Advisers, to ensure firms and investment advisors appropriately mitigate conflicts of interests and fulfill their fiduciary duties.

Information Security and Operational Resiliency

The 2021 report also emphasized the heightened risk of cyberattacks and the need for firms to proactively identify and address these risks. The Division will review whether firms have taken adequate measures to (i) safeguard customer accounts, (ii) verify investors' identities, (iii) oversee vendors, (iv) address malicious email activities, (v) respond to incidents, and (vi) manage operational risk related to employees working from home.

The Division will also continue to review firms' business continuity and disaster recovery plans, but it will incorporate a greater focus on climate-related risks for fiscal year 2021. Specifically, the Division will evaluate whether such plans adequately account for the growing physical and other relevant risks associated with climate change.

Fintech and Innovation, Including Digital Assets

With innovations in fintech and capital formation continuing at a rapid pace, the Division will focus its examinations on whether registrants operate consistently with their representations and handle customer orders in accordance with their instructions. The Division will also focus on reviewing registrants compliance around trade recommendations made on mobile applications. With respect to digital assets, the Division will continue to assess the following: (1) whether investments are in the best interests of investors; (2) portfolio management and trading practices; (3) safety of client funds and assets; (4) pricing and valuation; (5) effectiveness of compliance programs and controls; and (6) supervision of representatives' outside business activities.

For more information on the Division's stance on digital assets, see our client advisory, *Division of Examinations Issues Risk Alert on Digital Asset Securities.*

Additional Areas of Focus

The Division reaffirmed its prioritization of ensuring compliance with the AML requirements of the Bank Secrecy Act. Additionally, the Division will examine registrants to evaluate their understanding of exposure to the London Inter-Bank Offered Rate (LIBOR), preparations for the anticipated discontinuation of LIBOR, the transition to an alternative reference rate, and any adverse effects on investors.

Other areas of prioritization identified in the report include areas involving registered investment advisers (RIAs) and certain investment companies. With respect to RIAs, examinations will continue to evaluate core compliance programs ensuring proper execution of typical items. The Division specified that examinations would focus on RIAs that either have never been examined or have not been examined for several years, as well as RIAs that are dually registered as broker-dealers. Regarding registered funds, including mutual funds and ETFs, the Division will generally focus on fund compliance programs and financial conditions, particularly where funds have instituted advisory fee waivers. Further, the Division will continue to focus on advisers to private funds, particularly those with a higher concentration of structured products to assess whether such funds are at a higher risk for holding nonperforming loans and having loans with higher default risk than that disclosed to investors.

With respect to broker-dealers and municipal advisors, the Division will continue to prioritize, among other things, compliance with the Consumer Protection Rule, Net Capital Rule, best execution obligations, Rule 606 regarding order routing, and market-maker compliance with Regulation SHO. The Division also expressed concern regarding the effects of the COVID-19 pandemic and how municipal advisors have adjusted their practices.

Regarding market infrastructure, the Division will focus its examinations on clearing agencies, national securities exchanges, regulation systems compliance and integrity, transfer agents, and the Financial Industry Regulatory Authority (FINRA) and the Municipal Securities Rulemaking Board (MSRB), among other things.

For a full copy of the Division's 2021 Examination Priorities Report, click here.

Troutman Pepper – Gabrielle A. Gaudet, Genna Garver and James W. Stevens

March 9 2021

SEC Division of Examinations Announces 2021 Exam Priorities: DLA Piper

On March 3, the Division of Examinations (Division) of the Securities and Exchange Commission (SEC) announced its 2021 Examination Priorities. Published annually for the last nine years, the priorities are designed to provide securities industry participants with insight into the Division's risk-based approach to examinations and the areas it currently believes present potential risks to investors and the US capital markets. The 2021 release highlights nine areas:

- Retail investors, including seniors and retirement savers
- Information security and operational resiliency
- Financial technology and innovation, including digital assets
- Anti-money laundering (AML)
- London Inter-Bank Offered Rate (LIBOR) transition
- Registered investments advisers (RIAs) compliance programs and investment companies
- Broker-dealer financial responsibility and trading practices and municipal advisors
- Market infrastructure (clearing agencies, exchanges, and transfer agents) and
- Regulating the regulators: examinations of the Financial Industry Regulatory Authority (FINRA) and Municipal Securities Rulemaking Board (MSRB).

The priorities list is prefaced with a message from the Division's leadership team and an introduction offering further insight to the Division's work and strategic direction. Set forth below is our summary and key takeaways.

Continue reading.

DLA Piper – Mary Dunbar, Katrina A. Hausfeld, Deborah R. Meshulam and Michael Boardman

March 9 2021

BDA 2021 Advocacy Update is Now Available.

BDA's 2021 Advocacy update is now available. To view online, click here or here to view and print the pdf.

Bond Dealers of America

March 10, 2021

Another Abuse Of The EMMA Municipal Reporting System.

It has become a common practice of late to hold bondholder meetings online or by phone in order to update them on adverse events. We see this as an improvement over the untimely notices written in legalize which so often emanate from bank trust departments. I do, however, see distinct shortcomings in how this practice fails to meet the MSRB goal of trying to level the playing field through full disclosure not just for current bondholder, but also for buyers in due course and analysts or fund investors.

Online conference calls where borrower representatives provide updates and answer questions is not unlike the quarterly earnings calls by listed corporations. It allows bondholders to benefit, even from the answers to questions they themselves could not come up with. The shortcoming of this system is that access to such calls is usually subject to a 30 day replay time period after which the information is erased. Some trustees go a step further and require you to identify yourself before the call in order to get the call login information to make sure only bondholder are present.

This means a bondholder may decide to sell his bonds based on information he obtained from a call which is no longer available to the buyer of the bonds. In effect, after 30 days the “public information” definition of the call once again becomes “insider information.” This problem doesn’t exist with corporate stocks and bonds which trade daily because there are analysts who make a living on reporting out such information, the quicker the better.

With municipal bonds, when actionable information becomes available, we often see a clear pattern of selling even before the calls, especially by holders of large positions. We don’t consider this legal in the corporate market. Why shouldn’t it also be illegal in the municipal one?

My suggestion is that the MSRB should require that bondholder notices via telephone or internet calls must be made available to anyone using the EMMA information system for a minimum time period of, say, one year. While timely reporting of information through the EMMA system has many shortcomings, lets not have one of the improvements to the system come with new ways to abuse the market.

Forbes

by Richard Lehmann

Mar 10, 2021

Disclosure Rules Led to Drop in Bond Trading Markups.

The average transaction fee paid by retail investors to buy or sell corporate bonds fell 5% after regulators forced brokers to disclose these fees, according to new research co-authored by Berkeley Haas Asst. Prof. Omri Even-Tov.

The fee disclosure, which brokerage firms fought for about two decades, finally took effect for some corporate and municipal bond trades in 2018. This paper is the first academic research to examine its impact on trading costs for corporate bonds, and the findings highlight the need for regulators to provide better disclosures to retail investors, Even-Tov said.

“If their fees were fair before this, we shouldn’t have seen any effect, but we do find a reduction,” he said. “They were charging higher fees than they should have been.”

Hidden markups

When companies sell bonds to investors, they are borrowing money. After they have been issued, these bonds are bought and sold “over the counter,” between broker-dealers who trade them with their clients. When a broker charges a client more than the prevailing market price, it’s known as a markup. The difference represents the broker’s profit and the client’s trading cost—akin to a commission.

Until recently, investors had no easy way to know how much they were paying their brokers because the markup was not disclosed; it was embedded in the bond's price. For example, an investor might have seen that they paid $102.50 for the bond, but not that the firm had purchased it for only $100.

Knowledgeable investors could estimate the markup by looking up the bond's trading history in a database known as Trace—short for Transaction Reporting and Compliance Engine. They could then negotiate with their broker for a lower markup.

"However, estimating markups imposes information processing costs on investors, potentially creating information asymmetry between unsophisticated investors and bond-market professionals," wrote the authors, who include Christine Cuny of New York University's Stern School of Business and Edward Watts from the Yale School of Management.

New disclosure rule
In 2016, the Financial Industry Regulatory Authority, Wall Street's self-regulator, adopted a rule that required broker-dealers to disclose their markups when they buy corporate bonds and sell them to retail (non-institutional) investors the same day. Brokerage firms take little risk of losing money on same-day trades. The disclosure applied to such trades starting in May 2018.

These markups appear in the confirmation investors receive after they've made the trade. That's too late to negotiate a lower commission, but it could lead customers who previously didn't know how big these markups are "to reevaluate their brokerage relationship." Even-Tov and his co-authors wanted to know whether this had led brokers to reduce markups on trades subject to the disclosure.

To test this hypothesis, they used Trace to examine retail-size trades—which they defined as trades of $100,000 or less—during the six months before and six months after the rule took effect. They calculated the markup as the total cost that investors would incur to buy and sell a bond.

On average, they found the markup on same-day retail trades declined by about 5% compared to trades not subject to the disclosure, or from about $431 to $409 on a $50,000 trade, Even-Tov said.

The reduction was larger than average for the smallest trades. "These trades are likely executed by unsophisticated investors who have a limited supply of information processing capacity," the authors wrote. They also found that the reduction in markups was more pronounced for less-liquid bonds, such as high-yield, long-duration and smaller issues.

Lower costs for consumers

Consumer groups had argued that this long-overdue rule change would give retail investors more information to make better decisions and foster increased price competition. The securities industry had contended that the implementation costs would be significant and passed on to investors. The authors said the 5% savings they observed was after any costs passed to customers.

Markups are large "because frictions in the over-the-counter bond market enable market professionals to take advantage of uninformed investors," the authors wrote.

"Our findings show that disclosure requirements function as a regulatory tool, and constrain financial professionals' opportunistic behavior," Even-Tov said.

2-Mar-2021 5:45 PM EST, by University of California, Berkeley Haas School of Business

SEC Announces Enforcement Task Force Focused on Climate and ESG Issues: Ballard Spahr

Today, the SEC sent a very clear signal about one of its chief enforcement priorities by announcing the creation of a Climate and ESG Task Force within the Division of Enforcement. ESG stands for Environmental, Social, and Governance.

Since Allison Herren Lee was named the Acting Chair of the SEC on January 21, 2021, the SEC has repeatedly signaled that Climate and ESG issues and disclosures will be an SEC priority. For instance, on February 1, 2021, the SEC announced that Acting Chair Lee would have, for the first time, a senior policy advisor solely dedicated to these issues. On February 24, 2021, Acting Chair Lee directed the Division of Corporation Finance to scrutinize disclosures for adherence to the SEC's 2010 guidance on climate change-related disclosures. And just yesterday, the SEC's Division of Examinations announced that in the context of inspections, "emerging risks, including those relating to climate and ESG," will be a priority.

Today's announcement, however, is the most significant sign to date about the seriousness with which the SEC is studying Climate and ESG issues.

By creating a task force within the Division of Enforcement, the SEC is broadcasting that its focus will not solely be on providing climate and ESG guidance to publicly traded companies and SEC registrants, but that it will "regulate through enforcement" by bringing enforcement actions related to these issues. In the past, the Division of Enforcement created a Retail Strategy Task Force (2018), Financial Reporting and Audit Task Force (2013), and the Microcap Fraud Task Force (2013), to name a few. In each instance, the creation of the task force meant a swell of SEC enforcement actions in that area.

The Climate and ESG Task Force will be led by Acting Deputy Director of Enforcement Kelly Gibson—a former Ballard Spahr attorney in Philadelphia—who will oversee a 22-person team drawn from the Division of Enforcement. Ms. Gibson, who was until recently the Regional Director of the Philadelphia Regional Office of the SEC, is no stranger to enforcement actions involving climate and ESG issues.

SEC enforcement actions in this space will likely involve fraud charges under Section 10(b) of the Securities Exchange Act of 1934 (the Exchange Act) and Rule 10b-5 thereunder, Section 17(a) of the Securities Act of 1933, and books and record violations in violation of Section 13 of the Exchange Act.

The SEC's focus on ESG comes as no surprise. Investors, consumers, employees, lenders, and the general public have increasingly focused their attention on the non-financial aspects of an entity's business. This is true for public companies, financial institutions, real estate related entities, investment advisors, broker dealers, municipal securities issuers, and even private companies.

Ballard Spahr has established a cross-disciplinary team to assist clients with all ESG-related issues that may will likely arise. For example:

- We can assist in the development of metrics regarding sustainability, and diversity and inclusion of the workforce;
- We can assist in developing corporate climate strategies to meet ESG goals, positions on racism, immigration, and other social equity and justice issues; and
- Our ESG Working Group addresses corporate governance issues, including board diversity, shareholder proposals, and the direction and flow of political contributions.

Most importantly, in light of the SEC announcement, we have a team of lawyers with the procedural and substantive expertise to counsel our clients with respect to the many disclosure issues that may arise when an entity makes voluntary or compulsory ESG disclosures. Our securities and finance lawyers, aided by our securities enforcement litigators, advise on the best practices regarding disclosure of ESG issues and preparing to meet and address the concerns of governmental regulators.

Our environmental, labor and employment, finance, and real estate lawyers regularly collaborate with our securities lawyers to provide clients with the depth of knowledge and experience necessary to ensure each disclosure is fully compliant with the securities laws, meets the expectations of investors and lenders, and is clearly understandable to all constituencies that may be affected – officers and directors, employees, consumers, investors, lenders, the general public, and the relevant regulators.

Finally, in the event of an inquiry or investigation by a government agency or other investigative body, the ESG's team of long-experienced securities enforcement litigators, again working with the subject matter experts within the ESG Working Group, has the demonstrated ability to bring such inquiries to a positive outcome.

ESG has become a key measure of transparency and performance in all sectors of the economy. Our Working Group not only helps its clients navigate the ESG waters but enables its clients to improve, highlight, and appropriately disclose their ESG issues.

by the Environmental, Social, and Governance Group

March 4, 2021

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MSRB Publishes 2020 Fact Book of Municipal Securities Data.

Washington, DC – The Municipal Securities Rulemaking Board (MSRB) today published its annual Fact Book, the definitive compilation of the most recent five years of statistics on municipal market trading, interest rate resets and disclosures. The data in the 2020 Fact Book can be further analyzed to identify market trends.

The MSRB collects real-time municipal securities trade data, as well as primary market and secondary market disclosures. In addition to making the data and disclosures available for free on its Electronic Municipal Market Access (EMMA®) website and compiling quarterly and annual statistics, the MSRB conducts independent research and analysis to support understanding of market trends. Recent MSRB market analyses tease out noticeable trends in buying patterns over the past decade and document the historic volatility and recovery of the municipal market in 2020.

"The data in our annual Fact Book arm municipal market participants, policymakers, regulators, academics and others with information to understand long-term and emerging trends in our market," said MSRB Director of Research Marcelo Vieira. "For example, the MSRB's most recent research paper explored trading activity trends over the past decade. Declining numbers of small trades coupled with an increase in large trades possibly point to the growing use of separately managed accounts (SMAs), mutual funds and exchange traded funds (ETFs)."

Highlights in the report include a decrease in trades of $100,000 or less, typically associated with individual investors, which were down 3.9% in 2020 compared to 2019, while institutional trades—trades of over $1 million—increased 5.3%. There was a notable spike in the average daily number of trades and par amount traded during March and April 2020, the result of the market volatility associated with the COVID-19 pandemic.

The MSRB also found a significant increase in transactions and par amount traded of taxable municipal securities in 2020 compared to 2019. Trades of taxable securities were up 9.8% to 676,248 trades and accounted for nearly 8.0% of all municipal securities trades in 2020. Par amount of taxable securities traded increased 52.9% to $441.9 billion, accounting for 14.1% of total par amount traded.

"The increase in taxable trades and par amount traded accompanied a spike in taxable issuance in 2020," continued Vieira. "As noted in our review of the municipal bond market in 2020, taxable issuance in 2020 was more than double that in 2019, driven in part by issuers taking advantage of the low interest rate environment to refund outstanding tax-exempt debt with taxable debt."

Continuing disclosures submitted to the MSRB increased to 156,847 in 2020, up 4.2% from the 150,585 submissions in 2019. Event-based disclosures, which increased 15.2% to 59,521 in 2020, were the main drivers of the increase in total disclosures.

The 2020 Fact Book includes monthly, quarterly and yearly aggregate market information from 2016 to 2020, and covers different types of municipal issues, trades and interest rate resets.

Download the 2020 Fact Book.

Date: March 3, 2021

Contact: Leah Szarek, Chief External Relations Officer
202-838-1500
lszarek@msrb.org

GASB Requests Input on Proposal to Improve Guidance on Compensated Absences, Amend Certain Disclosures.

Norwalk, CT, March 3, 2021 — The Governmental Accounting Standards Board (GASB) today issued for public feedback a proposed Statement designed to enhance the recognition and measurement guidance for compensated absences and refine related disclosure requirements.

The proposed Statement would supersede the guidance issued by the GASB in Statement No. 16, *Accounting for Compensated Absences*, which was issued in 1992. The proposal is in keeping with the Board's commitment to periodically reexamine its standards to ensure they remain effective.

State and local governments often provide paid leave benefits to their employees, such as vacation leave and sick leave. Some benefits have evolved such as with the use of a paid time off (PTO) model that may have characteristics of both vacation and sick leave. The Exposure Draft, *Compensated Absences*, proposes to align recognition and measurement guidance for all types of compensated absences under a unified model.

The Exposure Draft details the circumstances under which governments would be required to recognize a liability for compensated absences and proposes guidance for measuring that liability. The general approach for measurement would be accumulated leave multiplied by an employee's pay rate as of the financial reporting date.

The proposed model would result in governments recognizing a liability that more appropriately reflects when they incur an obligation for compensated absences. The Board believes the model also would lead to greater consistency in application and improved comparability across governments.

The proposal would amend certain disclosures that are required at present. For example, the proposed Statement would provide an alternative to the existing requirement to disclose the gross increases and decreases in a compensated absences liability, such that governments would have an option to disclose only the net change in the liability.

Stakeholders are asked to review the proposal and provide input to the Board by June 4, 2021. More information about commenting on the Exposure Draft can be found in the document, which is available on the GASB website, www.gasb.org.

BDA Comments on Electronic Trading.

The BDA today submitted comments to the SEC on their "*Concept Release on Electronic Corporate Bond and Municipal Securities Market*." We focused our comments just on Section VIII of the release related to electronic trading in corporate and municipal bonds. The concept release was motivated by a recommendation from the SEC's Fixed Income Market Structure Advisory Committee.

BDA tells the SEC "We agree with the FIMSAC's suggestion that electronic platforms dedicated to bringing together buyers and sellers of debt securities for the purpose of effecting transactions should generally be regulated the same regardless of how they are structured internally. Regulation should be based on the functions and services trading platforms provide in the market." Our letter addresses issues such as investor protection in electronic trades, treatment of individual firms' customer trading systems, and how electronic trading volume is reported to regulators."

View the BDA's comment letter here.

The SEC's concept release is the first step in a long-term project to revise Rule ATS's treatment of corporate and municipal trading. Thank you to all who contributed to this project. We will continue to press BDA's members' views with the SEC and the discussion evolves. Please call if you have any questions.

Bond Dealers of America

March 1, 2021

[SEC Warned Against Regulation of Electronic Muni Platforms.]

Broker-dealers and operators of electronic trading platforms are warning the Securities and Exchange Commission that expanding alternative trading system regulation to request for quote functions would harm the municipal market.

In comment letters filed to the SEC on Monday regarding a concept release to update the current alternative trading system regime to create uniformity, broker-dealers cautioned the SEC against using stringent regulatory requirements on all electronic platforms without first conducting a study on the impact of additional regulations.

"Electronic trading of corporate and municipal bonds is still developing and creating significant regulatory burdens on electronic platforms could harm the customer interactions with their broker-dealers and ultimately reduce the number of different platforms available when most retail investors generally want their orders exposed to multiple platforms to obtain the best price," the Securities Industry and Financial Markets Association said.

The SEC's request for comment closely follows 2018 recommendations from the SEC's Fixed Income Market Structure Advisory Committee. FIMSAC said at that time that some platforms were regulated as ATS', or regulated as broker-dealers, and others that operate on the same or similar models are not regulated.

Regulatory differences were driven by Regulation ATS, an SEC rule that established a regulatory framework for ATS' in 1998. To comply, an ATS must register as a broker-dealer and file an initial operation report with the SEC. In 2018, the SEC voted on amendments to Regulation ATS to improve transparency, such as requiring certain ATSs to file detailed public disclosures.

Further regulation could negatively impact broker-dealers ability to provide best execution to retail investors who hold over 72% of the market, SIFMA said.

SIFMA also said that platforms that act just as platforms that provide RFQs but where transactions get executed independently should remain outside the scope of Regulation ATS.

"Significant changes to Regulation ATS and/or the definition of exchange are not warranted and could have unintended negative consequences on the growth and development of electronic trading in these markets," SIFMA said.

Instead of creating new regulations for municipal ATS' the SEC could instead act through interpretive guidance, SIFMA said.

The current equity-focused ATS framework won?t work for fixed-income, electronic trading platform MarketAxess (MKTX) warned. Platforms that aren't regulated at all should be regulated and minimum standards should be created in a newly formed ATS rule that works for fixed income, MarketAxess (MKTX) said.

Rules related to ATS' should not be applied to requests for quotes, MarketAxess (MKTX) added. MarketAxess (MKTX) itself allows participants to post requests for quotes and execute deals on its platform. Securities Exchange Act Rule 15c3-5 requires a broker-dealer providing market access on an exchange or ATS to have a variety of financial and regulatory risk management controls.

MarketAxess (MKTX) told the regulator that electronic trading has grown rapidly and that any future regulation should not upset that momentum.

SEC rules such as SEA Rule 15c3-5 should not be applied to an RFQ and if RFQs were to be included as an ATS, the SEC should be wary of that and other rules that rely on Regulation ATS, MarketAxess (MKTX) said.

Electronic trading platform Tradeweb Markets Inc. (TW) said while it supports the SEC's efforts to tailor regulation to fixed income trading platforms, it will be complicated. Tradeweb offers a RFQ platform that was, but that is no longer registered as an ATS.

The group said it is important that platforms have similar trading protocols but that the SEC should not take a "one size fits all" approach.

SEA Rule 15c3-5 should not be applied to RFQs, Tradeweb said.

"… fixed-income trading platforms do not uniformly provide for arrangements between broker-dealers and customers for automated and anonymous trading platforms," Tradeweb argued.

The Bond Dealers of America said current regulation is inconsistent and could motivate regulatory arbitrage if new electronic trading entrants choose a structure that minimizes regulatory duties. Regulatory arbitrage is the practice of exploiting loopholes in rules by taking advantage of inconsistent standards.

Investor protections aren?t currently applied when two customers trade with each other.

"BDA supports applying key investor protection rules to trades executed on electronic platforms regardless of the parties to the trade," said Michael Decker, BDA senior vice president for public policy. "In a transaction where a dealer's counterparty is a non-dealer and their identity is known to the dealer, the dealer should bear customer protection responsibility."

If two non-dealers are trading, the trading platform should shoulder that responsibility, Decker said. That doesn't happen often, though, Decker said.

"The trading platform should have the responsibility for ensuring that the trade was conducted at a fair price so that the trade complies with Municipal Securities Rulemaking Board fair pricing rules or that the trade met suitability or best interest guidelines," Decker said. "All of the kinds of regulations that apply to a dealer when a dealer is conducting a trade on behalf of a customer should apply to the trading platform when there is no dealer involved."

Decker said the request for comment was just the start of a long rulemaking process.

The MSRB also weighed in, noting that ATS' have become a significant component of liquidity in the market – MSRB trade data for 2020 also shows that ATSs were involved 21% of all trades and 55% of all inter-dealer trades.

“Consistent with the FIMSAC recommendation, the MSRB looks forward to working collaboratively with the SEC and the Financial Industry Regulatory Authority to review the regulatory framework for oversight of the fixed income electronic trading platforms,” said Ed Sisk, MSRB chair.

FINRA also commented Monday, saying it was difficult to harmonize rules to fixed income trading platforms without updates to Regulation ATS.

“In addition, given the Commission’s broker-dealer interpretive role, and its supervisory role over the fixed income markets, FINRA believes the SEC should update trading platform classifications in the unified manner recommended by the FIMSAC,” FINRA said.

By Sarah Wynn

BY SOURCEMEDIA | MUNICIPAL | 03/02/21 11:56 AM EST

SEC Office of Municipal Securities Issue Staff Statement on LIBOR Transition: Mayer Brown

On January 8, 2021, the staff of the US Securities and Exchange Commission’s (“SEC”) Office of Municipal Securities (“OMS Staff”) issued a statement focusing on the impact of the discontinuation of LIBOR on the municipal securities markets. The statement highlights considerations for issuers of municipal securities and other “obligated persons” and municipal advisors to address the fact that the expected discontinuation of LIBOR “could have a significant impact on the municipal securities market and may present a material risk” for market participants.

The statement discusses considerations for remediating contracts with exposure to LIBOR, ongoing disclosure requirements, and the duties of municipal advisors in light of the December 31, 2021 discontinuation of LIBOR.

Remediation of existing and new contracts

OMS Staff urged municipal market participants to take action with respect to existing and new contracts that may have exposure to LIBOR, which may include municipal bonds, notes, bank loans, derivatives, leases, installment sales agreements, other credit agreements and financial instruments, commercial contracts (e.g., contracts with vendors, suppliers, service providers, other contractors, employees, and others), and investments held by municipal obligors.

Existing contracts may contain reference to LIBOR and require remediation. OMS Staff has requested that market participants identify existing contracts that extend past 2021 to determine exposure to LIBOR, noting that the consequences of any unanticipated changes in the financial terms of an instrument can be particularly impactful in circumstances where the instrument has an extended maturity or termination date, or where another financial arrangement has previously been entered into as a hedge against, or otherwise in anticipation of, an existing LIBOR-based instrument. OMS Staff noted that firms should specifically consider: (1) potential constraints of state law upon replacing LIBOR, (2) the impact of LIBOR discontinuation on a firm’s hedging strategies, (3) potential tax consequences of replacing LIBOR, and (4) operational capabilities to amend outstanding instruments.

Further, OMS Staff noted that municipal obligors should consider whether contracts entered into in the future should reference an alternative rate to LIBOR or include “fallback language” that triggers a replacement rate. The statement calls attention to three major initiatives by industry groups to facilitate the transition away from LIBOR:

- The Alternative Reference Rates Committee ("ARRC") has published recommended fallback language for new issuances of a variety of debt instruments, some of which may be used in the municipal securities market.
- The International Swaps and Derivatives Association ("ISDA") has led development of fallback language for derivatives contracts, including updates to ISDA standard definitions for new contracts, the 2020 IBOR Fallbacks Protocol for legacy contracts, and a template form of bilateral agreement to facilitate the transition away from LIBOR.
- ICE Benchmark Administration ("IBA") announced a consultation on its intention to cease the publication of one-week and two-month USD LIBOR (as well as all other key LIBOR currencies) on December 31, 2021, and the overnight, one-month, three-month, six-month and 12-month USD LIBOR tenors on June 30, 2023, in order to allow most legacy LIBOR contracts to mature prior to LIBOR's discontinuation. This consultation garnered general support from U.S. banking regulators, former SEC Chairman Jay Clayton, the ARRC, and the United Kingdom's Financial Conduct Authority. The consultation closed in late January 2021 and an announcement from IBA of the results of the consultation is expected any day but regulators have made clear that the target cessation date for use of LIBOR in new contract originations remains December 31, 2021.

Disclosures related to the LIBOR transition

OMS Staff noted that municipal obligors should consider the need to make appropriate disclosures regarding the material risks related to the expected discontinuation of LIBOR, and mitigating actions taken in response.

In the primary market, the official statement for a new issue affected by LIBOR should include appropriate disclosures regarding the material risks related to the expected discontinuation of LIBOR, mitigating actions taken or expected to be taken in response, and any fallback language governing the interest rate provisions after the discontinuation of LIBOR.

OMS Staff also recognized the importance of secondary market disclosures, either through disclosures required under continuing disclosure undertakings or by voluntary disclosure, about the progress toward risk identification and mitigation, and the anticipated impact on the municipal obligor, if material. OMS Staff encouraged municipal obligors to provide investors with forward-looking information regarding the potential future impact of the LIBOR transition on their outstanding municipal securities, relevant derivatives positions, hedging strategies, investments and other contracts, and their overall financial and operating conditions.

How can municipal advisors prepare for LIBOR discontinuation?

The statement highlighted pertinent parts of the SEC's Division of Examinations' (formerly, the Office of Compliance Inspections and Examinations) Risk Alert on LIBOR transition considerations for municipal advisors.1 In particular, OMS Staff noted that municipal advisors should take into account and address:

- The exposure of the firm and its customers, clients, and investors to LIBOR-linked contracts that extend past the current expected discontinuation date, including any fallback language incorporated into these contracts;
- The firm's operational readiness, including any enhancements or modifications to systems, controls, processes, and risk or valuation models associated with the transition to a new reference rate or benchmark;

- The firm's disclosures, representations, and/or reporting to investors regarding its efforts to address LIBOR discontinuation and the adoption of alternative reference rates;
- Any potential conflicts of interest associated with the LIBOR discontinuation and the adoption of alternative reference rates; and
- Clients' efforts to replace LIBOR with an appropriate alternative reference rate.

OMS Staff also specifically reminded municipal advisors of their duties under the Municipal Securities Rulemaking Board ("MSRB") Rule G-42, which creates a suitability requirement for recommendations by a municipal advisor, and Section 15B(c)(1) of the Exchange Act, which imposes a fiduciary duty on municipal advisors when advising municipal entity clients.

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Market participants continue to be encouraged by applicable regulatory authorities to cease new originations of LIBOR contracts prior to December 31, 2021. Firms should be prepared to handle not only their own LIBOR transition, but also to deal with the wide range of LIBOR exposure that may arise from other sources, such as relationships with clients, counterparties, or vendors.

Mayer Brown – Marlon Paz and Kyle P. Swan

February 22 2021

MSRB Extends Date for Compliance with Primary Offering Disclosure Form: Cadwalader

The MSRB extended the date for compliance with amendments to Form G-32 pursuant to MSRB Rule G-32 ("Disclosures In Connection With Primary Offerings"). Under Form G-32, the MSRB collects data elements for the Electronic Municipal Market Access (or "EMMA") system.

The extension from March 31, 2021 to August 2, 2021 is intended to provide brokers, dealers and municipal securities dealers more time to operationalize compliance with the amended form. As previously covered, the SEC expanded Form G-32 to capture data that an underwriter is obligated to input into the New Issue Information Dissemination Service ("NIIDS") for NIIDS-eligible offerings.

Cadwalader Wickersham & Taft LLP

February 19 2021

SEC Data Disclosures – Temporary Conditional Exemptive Order for Municipal Advisor Activities

Read the Temporary Conditional Exemptive Order.

Office of Municipal Securities Staff Statement on LIBOR Transition in the

Municipal Securities Market[1]

1. Managing the Transition from LIBOR in the Municipal Securities Market

The expected discontinuation of LIBOR[2] could have a significant impact on the municipal securities market and may present a material risk for many issuers of municipal securities and other obligated persons[3] (collectively, "municipal obligors"). Municipal obligors should consider the potential actions available to mitigate these risks, including the repercussions of not taking the steps necessary to effect an orderly and timely transition, in anticipation of LIBOR's discontinuation.[4] Risks that could arise in connection with the LIBOR transition are also relevant to other municipal securities market participants, including those who advise municipal obligors. As such, when advising their municipal obligor clients on issuances of municipal securities and municipal financial products that reference LIBOR (or that may otherwise be materially affected by the transition from LIBOR), municipal advisors should be aware of and, to the extent relevant, should take into consideration the issues arising from the LIBOR transition.[5]

This statement focuses on issues specifically relevant to the municipal securities market. For additional information and context, municipal market participants should also review the Commission staff's statements with regard to the broader securities market.[6]

a. Existing Contracts

OMS staff urges municipal obligors to identify existing contracts that extend past 2021 to determine their exposure to LIBOR. Potentially affected contracts include, but are not limited to, municipal bonds, notes, bank loans, derivatives, leases, installment sales agreements, other credit agreements and financial instruments, commercial contracts (e.g., contracts with vendors, suppliers, service providers, other contractors, employees and others), and investments held by municipal obligors. To avoid unanticipated risks, municipal obligors should consider taking appropriate steps in connection with any existing LIBOR-based contracts to resolve potential issues arising from LIBOR's discontinuance as soon as practicable.[7]

OMS staff believes that consequences of any unanticipated changes in the financial terms of an instrument can be particularly impactful in circumstances where the instrument has an extended maturity or termination date, or where another financial arrangement has previously been entered into as a hedge against, or otherwise in anticipation of, an existing LIBOR-based instrument. OMS staff acknowledges there are rarely quick fixes to these types of issues and encourages market participants to focus on them now to avoid financial, operational, and market disruptions after 2021.

OMS staff believes that the following questions also may be relevant for municipal obligors:

1. **State Laws.** Do state laws constrain municipal obligors' ability to replace LIBOR with an alternative reference rate (e.g., do any debt or investment authorization statutes limit interest rate structures or permissible reference rates, thereby constraining the ability of municipal obligors to effectively implement a transition)?
2. **Hedging Strategies.** For long-dated derivative contracts referencing LIBOR used to hedge floating-rate investments or obligations (which may extend for periods beyond those more typically seen in other segments of the financial markets), what effect will the discontinuation of LIBOR have on the effectiveness of the party's hedging strategy?[8]
3. **Tax Consequences.** Would a potential change in financial terms of an instrument resulting from a transition from LIBOR risk material tax consequences for the municipal obligor or investors in its debt obligations? What actions may be needed to avoid negative tax consequences?[9]
4. **Amending Outstanding Debt Instruments.** Are municipal obligors familiar with the process by

which their outstanding debt obligations referencing LIBOR can be amended, and are such amendments reasonably feasible within the timeframe anticipated for the LIBOR transition? What would be the repercussions to municipal obligors if such amendment(s) occur?

b. New Contracts

Municipal obligors also should consider whether contracts entered into in the future should reference an alternative rate to LIBOR (e.g., SOFR) or, if a municipal obligor determines to enter into new contracts referencing LIBOR notwithstanding the risks identified herein, whether such contracts include effective fallback language. Municipal obligors should understand the potential impacts if such fallback provisions are triggered under their contracts, such as any potential change in interest rate levels or behavior under different market conditions resulting from the new rate structure as compared to the original LIBOR-based structure.

i. ARRC Fallback Language

The Alternative Reference Rates Committee ("ARRC") has published recommended fallback language for new issuances of a variety of debt instruments, some of which may be used in the municipal securities market.[10] Such fallback language seeks to provide interest rate provisions that will function upon discontinuation of LIBOR and promote consistency in defining key terms such as benchmark transition events, benchmark replacement, and benchmark replacement adjustments.[11]

ii. ISDA Fallback Language

ISDA has been leading an industry effort to implement fallback language for derivatives contracts. Specifically, on October 23, 2020, ISDA released the (i) "IBOR Fallbacks Supplement" and (ii) "IBOR Fallback Protocol."

The "IBOR Fallbacks Supplement" amends ISDA's standard definitions for interest rate derivatives to incorporate robust fallbacks for derivatives linked to certain IBORs, effective on January 25, 2021 (after this date, all new cleared and non-cleared derivatives that reference these definitions will include the new fallbacks).[12] The "IBOR Fallbacks Protocol" is a template agreement that allows market participants to incorporate the revised definitions and fallbacks of the "IBOR Fallback Supplement" into their legacy non-cleared derivatives trades with other willing counterparties. Counterparties may enter the "IBOR Fallbacks Protocol" immediately, and similar to the "IBOR Fallbacks Supplement," it becomes effective on January 25, 2021.[13]

iii. IBA Announcement and Regulatory Response

On November 30, 2020, IBA announced that it planned to consult on its intention to cease the publication of one-week and two-month LIBOR on December 31, 2021, and the overnight, one-month, three-month, six-month and 12-month LIBOR tenors on June 30, 2023.[14]

That same day, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (together, the "agencies") jointly responded to IBA's announcement.[15] First, the agencies encouraged banks to stop writing contracts referencing LIBOR as soon as possible (and in any event by the end of 2021, subject to certain limited exceptions), stating that entering into new contracts that use LIBOR as a reference rate after December 31, 2021 and failing to prepare for disruptions to LIBOR (including operating without robust fallback language that includes a clearly defined alternative reference rate) could cause significant issues if not addressed.[16] Second, the agencies noted that extending the publication of certain LIBOR tenors until June 30, 2023 would allow most legacy LIBOR contracts to mature before LIBOR experiences disruptions.[17] Former Commission Chairman Jay Clayton, the ARRC, and the United Kingdom's Financial Conduct Authority supported these announcements through their own statements.[18]

Municipal obligors and market participants acting as counterparties to, or advising, municipal obligors should closely review the IBA announcement and the subsequent regulatory response. In particular, municipal obligors should carefully analyze all new contracts entered into with banks or any other counterparties to determine whether they should continue to reference LIBOR, paying particular attention to those contracts into which municipal obligors would enter after December 31, 2021.[19] If they do continue to reference LIBOR in new contracts, municipal obligors should determine whether the contracts include robust fallback language to mitigate against risks identified herein and by the agencies.

2. Disclosure Related to LIBOR Transition

Former Commission Chairman Clayton and OMS Director Rebecca Olsen recently observed that, "[w]hile there are significant differences between our corporate capital markets and our municipal securities markets, the importance of high quality disclosure, particularly in times of uncertainty, is consistent."[20] The Commission has previously stated that, particularly in connection with "… complex and sophisticated derivative and other municipal products … investors need a clear understanding of the terms and the particular risks arising from the nature of the products."[21] Consistent with this observation, OMS staff believes that municipal obligors should consider the need to make appropriate disclosures regarding the material risks related to the expected discontinuation of LIBOR, and mitigating actions taken in response.

a. Primary Market

In the primary market, the official statement for a new issue affected by LIBOR (whether it is the rate borne by the securities or applies to derivatives or other financial arrangements that secure, hedge or otherwise have a material impact on the new issue) should include appropriate disclosures regarding the material risks related to the expected discontinuation of LIBOR, mitigating actions taken or expected to be taken in response, and any fallback language governing the interest rate provisions after the discontinuation of LIBOR.

b. Secondary Market

In the secondary market, it is important to keep investors informed, either through disclosures required under continuing disclosure undertakings or by voluntary disclosure, about the progress toward risk identification and mitigation, and the anticipated impact on the municipal obligor, if material. OMS staff encourages municipal obligors to provide investors with forward-looking information regarding the potential future impact of the LIBOR transition on their outstanding municipal securities, relevant derivatives positions, hedging strategies, investments and other contracts, and their overall financial and operating conditions.

Notably, OMS staff believes that the discussion in the Municipal Market COVID-19 Statement under the heading "Important Considerations that Generally Weigh in Favor of Providing Updated Investor-Oriented Disclosures that Discuss the Current and Anticipated Effects of COVID-19" with respect to liability concerns also would generally apply to voluntary disclosures relating to the potential implications of the LIBOR transition.[22]

OMS staff also notes that the Governmental Accounting Standards Board ("GASB") issued Statement No. 93 revising certain GASB standards relating to references to LIBOR and certain hedge accounting issues implicated by replacing LIBOR with an alternative reference rate.[23] GASB encourages early application for municipal obligors for those portions that have not yet become effective.[24] If financial statements are included in the official statement or in continuing disclosures, the municipal obligor should be cognizant of, and seek to adhere to, applicable accounting standards with regard to the LIBOR transition.

3. Municipal Advisors' Preparation for the LIBOR Transition

Municipal advisors should consider the impact of the LIBOR transition regarding both their own operations as well as their clients.

a. LIBOR Risk Alert

A recent "Risk Alert" from the Commission's Division of Examinations[25] identified aspects of the LIBOR transition that may be relevant for municipal advisors and other regulated entities to consider when preparing to be examined by Commission staff,[26] including:

1. The exposure of the firm and its customers, clients and investors to LIBOR-linked contracts that extend past the current expected discontinuation date, including any fallback language incorporated into these contracts;
2. The firm's operational readiness, including any enhancements or modifications to systems, controls, processes, and risk or valuation models associated with the transition to a new reference rate or benchmark;
3. The firm's disclosures, representations, and/or reporting to investors regarding its efforts to address LIBOR discontinuation and the adoption of alternative reference rates;
4. Identifying and addressing any potential conflicts of interest associated with the LIBOR discontinuation and the adoption of alternative reference rates; and
5. Clients' efforts to replace LIBOR with an appropriate alternative reference rate.[27]

b. Municipal Advisor Duties

Municipal advisors providing advice to municipal obligors regarding municipal securities or municipal financial products with LIBOR exposure should be aware of and, to the extent relevant, should consider the issues arising from the LIBOR transition in formulating their advice. Beyond such action, OMS staff reiterates the duties imposed upon municipal advisors by: (i) MSRB Rule G-42; and (ii) Exchange Act Section 15B(c)(1).

i. MSRB Rule G-42
The MSRB issued a statement related to the duties of municipal advisors and LIBOR. The MSRB noted that, under MSRB Rule G-42, if a municipal advisor makes a recommendation of a municipal securities transaction (or a municipal financial product) involving LIBOR to a municipal entity or obligated person client, it must have a "reasonable basis to believe that the recommended municipal securities transaction or municipal financial product is suitable for the client, based on the information obtained through the reasonable diligence of the municipal advisor."[28]

ii. Exchange Act Section 15B(c)(1)
Municipal advisors are reminded that Exchange Act Section 15B(c)(1)[29] imposes a fiduciary duty on municipal advisors when advising their municipal entity clients.

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[1] This statement represents the views of staff of the U.S. Securities and Exchange Commission ("Commission")'s Office of Municipal Securities ("OMS"). It is not a rule, regulation, or statement by the Commission. The Commission has neither approved nor disapproved its content. This statement does not alter or amend applicable law and has no legal force or effect. This statement creates no

new or additional obligations for any person.

[2] Formerly an acronym for “London Interbank Offered Rate,” LIBOR is common parlance for its current official name, “ICE LIBOR.” See “ICE LIBOR,” ICE Benchmark Administration (“IBA”), available at https://www.theice.com/iba/libor. IBA is an independent subsidiary of Intercontinental Exchange, Inc., and is responsible for the end-to-end administration of the LIBOR benchmark.

[3] Obligated person is defined in 15 U.S.C. § 78o-4(e)(10) and 17 C.F.R. § 240.15c2-12(f)(10).

[4] See “Overview: The Future of LIBOR,” available at https://www.theice.com/iba/libor (providing a discussion of the LIBOR discontinuation scheduled to occur in 2021 and proposed possible limited exceptions thereto).

[5] While this statement focuses on municipal obligors and municipal advisors, other municipal securities market participants (including, but not limited to, investors, broker-dealers, investment advisers, commodity trading advisors, and their legal counsel) should understand the legal, financial, and operational implications of the LIBOR transition and the associated risks in connection with their activities in the municipal securities market.

[6] See “Staff Statement on LIBOR Transition” (July 12, 2019), available at https://www.sec.gov/news/public-statement/libor-transition.

[7] For example, depending on their individual facts and circumstances, parties to existing LIBOR-based contracts could resolve their LIBOR references by negotiating a new reference rate, or agreeing upon new fallback language, as described herein in connection with new contracts.

[8] As discussed below, the International Swaps and Derivatives Association (“ISDA”) proposed fallback language in connection with the LIBOR transition that, if counterparties consent, could be applied to existing contracts. ISDA is a global association of market participants, key components of the derivatives market infrastructure, as well as law firms, accounting firms, and other services providers. ISDA works to promote sound risk management practices and policies in the derivative space (such as developing the ISDA Master Agreement, the standard document regularly used to govern over-the-counter derivatives transactions). See “About ISDA,” available at https://www.isda.org/about-isda.

[9] In October 2019, the Internal Revenue Service (“IRS”) published proposed regulations providing guidance on the tax consequences of the LIBOR transition. Although not yet finalized, OMS staff understands that the proposed regulations are intended to allow municipal issuers to replace LIBOR with an alternate reference rate without causing a reissuance, provided that the issuer complies with certain conditions. See Guidance on the Transition From Interbank Offered Rates (“IBORs”) to Other Reference Rates, 84 FR 54068 (Oct. 9, 2019). Pending finalization of these proposed regulations, the IRS has provided interim guidance that the adoption of certain fallback language recommended by the ARRC and ISDA (described herein) for contracts with terms referencing IBORs will not impact the tax status of municipal securities. See “IRS Rev. Proc. 2020-44,” (Oct. 9, 2020), available at https://www.irs.gov/pub/irs-drop/rp-20-44.pdf.

[10] These include, among others, floating rate notes (see “ARRC Recommendations Regarding More Robust Fallback Language for New Issuance of LIBOR Floating Rate Notes,” (Apr. 25, 2019), available at https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2019/FRN_Fallback_Language.pdf), securitizations (see “ARRC Recommendations Regarding More Robust Fallback Language For New Issuances Of Libor Securitizations,” (May 31, 2019), available at https://www.newyorkfed.org/

medialibrary/Microsites/arrc/files/2019/Securitization_Fallback_Language.pdf), and syndicated loans (see “ARRC Recommendations Regarding More Robust Fallback Language For New Originations Of Libor Syndicated Loans” (Apr. 25, 2019), available at https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2019/ Syndicated_Loan_Fallback_Language.pdf).

[11] See “ARRC Releases Recommended Fallback Language for Floating Rate Notes and Syndicated Loans” (Apr. 25, 2019), available at https://www.newyorkfed.org/ medialibrary/Microsites/arrc/files/2019/ARRC-Apr-25-2019-announcement.pdf.

[12] See “ISDA 2020 IBOR Fallbacks Supplement” (Oct. 23, 2020), available at http://assets.isda.org/media/3062e7b4/23aa1658-pdf.

[13] See “ISDA 2020 IBOR Fallbacks Protocol” (Oct. 23, 2020), available at http://assets.isda.org/media/3062e7b4/08268161-pdf. Notably, the ARRC published its support of the “IBOR Fallbacks Protocol,” encouraging market participants to adhere to it before its January 25, 2021 effective date. See also “ARRC Supports Forthcoming ISDA IBOR Fallbacks Protocol and Encourages Adherence” (Oct. 22, 2020), available at https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2020/ARRC_Press_Release_ISDA_Protocol.pdf.

[14] See “ICE Benchmark Administration to Consult on Its Intention to Cease the Publication of One Week and Two Month USD LIBOR Settings at End-December 2021, and the Remaining USD LIBOR Settings at End-June 2023” (Nov. 30, 2020), available at https://ir.theice.com/press/news-details/2020/ICE-Benchmark-Administration-to-Consult-on-Its-Intention-to-Cease-the--ublication-of-One-Week-and-Two-Month-USD-LIBOR-Settings-at-End-Decemb-r-2021-and-the-Remaining-USD-LIBOR-Settings-at-End-June-2023/default.aspx. IBA expects to conclude its consultation for feedback by the end of January 2021. Id.

[15] See “Statement on LIBOR Transition” (Nov. 30, 2020), available at https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20201130a1.pdf.

[16] Id. (“Given consumer protection, litigation, and reputation risks, the agencies believe entering into new contracts that use USD LIBOR as a reference rate after December 31, 2021, would create safety and soundness risks and will examine bank practices accordingly”). Various provisions of federal law require banks to operate in a safe and sound manner. See, e.g., 12 U.S.C. 321–338a, 1467a(g), 1818(b), 1844(b), and 3101 et seq.

[17] Supra note 15.

[18] See “Statement on Developments Related to the LIBOR Transition” (Nov. 30, 2020), available at https://www.sec.gov/news/public-statement/clayton-libor-2020-11-30; “ARRC Applauds Major Milestone in Transition from U.S. Dollar LIBOR” (Nov. 30, 2020), available at https://www.newyorkfed.org/medialibrary/Microsites/ arrc/files/2020/ARRC_Press_Release_Applauds_Milestone_Transition_US_Dollar_LIBOR.pdf; “FCA Response to IBA’s Proposed Consultation on Intention to Cease US$ LIBOR” (Nov. 30, 2020), available at https://www.fca.org.uk/news/statements/fca-response-iba-proposed-consulta-ion-intention-cease-us-dollar-libor.

[19] While IBA is considering proposals that could extend LIBOR (subject to certain limited exceptions) beyond 2021, there is at this time no certainty that such extension will occur and therefore OMS staff’s discussion of the LIBOR transition herein reflects the current IBA deadlines.

[20] See Jay Clayton, Chairman, Commission, and Rebecca Olsen, OMS Director, "The Importance of Disclosure for our Municipal Markets" (May 4, 2020), available at https://www.sec.gov/news/public-statement/statement-clayton-olsen-2020-05-04 ("Chairman Clayton and OMS Director Olsen Statement").

[21] See "Statement of the Commission Regarding Disclosure Obligations of Municipal Securities Issuers and Others," 59 FR at 12752 (Mar. 17, 1994). The Commission further stated therein that "… investors need to be informed about the nature and effects of each significant term of the debt … [and] should be aware of their exposure to interest rate volatility, under all possible scenarios."

[22] See Chairman Clayton and OMS Director Olsen Statement. While the safe harbors for forward looking statements that are available to certain corporate issuers are not available to issuers of municipal securities, OMS staff notes that a municipal issuer's approach to forward-looking disclosures should be informed by the judicially developed "bespeaks caution" doctrine. For a description of the "bespeaks-caution" doctrine developed by the federal courts of appeals, see generally Robert A. Fippinger, The Securities Law of Public Finance, §8:3.4[B] (3d. ed. 2019).

[23] GASB Statement No. 93, Replacement of Interbank Offered Rates (Mar. 2020). Not all municipal obligors are subject to GASB standards. For those municipal obligors that are subject to standards set by the Financial Accounting Standards Board ("FASB"), see FASB Accounting Standards Update ("ASU") 2020-04, Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting (Mar. 2020). Municipal obligors that are subject to accounting standards other than GASB or FASB should consider the extent to which they should follow the guidance set forth in GASB Statement No. 93 or FASB ASU 2020-04, as appropriate.

[24] Most changes became effective after June 15, 2020. However, GASB Statement No. 93 provides for a later effective date for the removal of LIBOR as an appropriate benchmark interest rate, with such removal to become effective for reporting periods ending after December 31, 2021. GASB has postponed effectiveness of portions of GASB Statement No. 93 relating to lease modifications until June 15, 2021 due to the COVID-19 pandemic. See GASB Statement No. 95, Postponement of the Effective Dates of Certain Authoritative Guidance (May 2020).

[25] Division of Examinations (then known as the Office of Compliance Inspections and Examinations) Risk Alert, Examination Initiative: LIBOR Transition Preparedness (June 18, 2020), available at https://www.sec.gov/files/Risk%20Alert%20-%20OCIE%20LIBOR%20Initiative_1.pdf ("LIBOR Risk Alert").

[26] While the LIBOR Risk Alert is directed toward regulated entities, other municipal securities market participants (including, but not limited to, municipal obligors) may wish to consider the issues raised in the LIBOR Risk Alert.

[27] See LIBOR Risk Alert.

[28] See "LIBOR Transition Information," available at http://www.msrb.org/Regulated-Entities/Resources/LIBOR-Information.

[29] 15 U.S.C. § 78o-4(c)(1) (2019).

NFMA Newsletter.

The NFMA's Municipal Analyst Bulletin, Vol. 31, No. 1, has been published.

Click here to download the February 2021 edition.

2021 GASB Accounting Support Fee to Fund the GASB's Annual Budget: Katten Muchin Rosenman

Pursuant to a Securities and Exchange Commission order, the Financial Industry Regulatory Authority (FINRA) established an accounting support fee to fund the annual budget of the Governmental Accounting Standards Board (GASB). Each quarter, FINRA collects a quarter of the annual GASB accounting support fee from its member firms. Each member firm's assessment is based on its portion of the total par value of municipal securities transactions reported to the Municipal Securities Rulemaking Board by all FINRA members in the previous calendar quarter.

FINRA Regulatory Notice 21-06

Katten Muchin Rosenman LLP – Susan Light and Gregory A. Uffner

February 26 2021

Financial Accounting Foundation Appoints Lise Valentine as Vice Chair of the Governmental Accounting Standards Advisory Council.

Norwalk, CT—February 23, 2021 — The Board of Trustees of the Financial Accounting Foundation (FAF) has announced the appointment of Lise Valentine, the deputy inspector general for audit and program review for the city of Chicago, as vice chair of the Governmental Accounting Standards Advisory Council (GASAC). Ms. Valentine currently represents the Association of Local Government Auditors (ALGA) on the GASAC.

Ms. Valentine assumes the role of vice chair on February 24, 2021, and will serve in that capacity until her existing GASAC term concludes on December 31, 2022. She is also eligible for one additional two-year term. Ms. Valentine replaces Alan Skelton, who was appointed the director of research and technical activities for the Governmental Accounting Standards Board (GASB) effective April 1, 2021.

The GASAC is responsible for advising the GASB on technical issues, project priorities, and other matters that affect standards setting for accounting and financial reporting by state and local governments. Members of the GASAC represent a cross-section of the GASB's state and local government stakeholders, including users, preparers, and auditors of financial information. GASAC members are selected on the basis of their professional expertise and the depth and breadth of experience they bring to the GASAC.

"We thank Lise for her commitment to the GASAC as the liaison to the ALGA and look forward to working with her in the role of vice chair," said FAF Board of Trustees Chair Kathleen Casey. "Lise has always been an active member who regularly provides insightful input to the Board from both her perspective as a city auditor and her prior experience at a citizen research organization," Ms. Casey added.

In her current position with the city of Chicago, which she has held since December 2011, Ms. Valentine conducts independent, objective analysis and evaluations of city programs and operations, issues public reports, and makes recommendations to strengthen and improve the delivery of city services.

Prior to working with the city, Ms. Valentine was a vice president and director of research at The Civic Federation where she conducted original research on state and local government finance topics and developed the organization's annual research agenda.

Ms. Valentine earned a Ph.D. in communication studies from the University of Iowa, a master's degree in accounting from DePaul University, and a bachelor of arts degree in humanistic studies from McGill University. She is a certified inspector general auditor, certified internal auditor, and certified public accountant. Ms. Valentine is also an active member in the ALGA.

About the Financial Accounting Foundation

Established in 1972, the Financial Accounting Foundation (FAF) is the independent, private-sector, not-for-profit organization based in Norwalk, Connecticut responsible for the oversight, administration, financing, and appointment of the Financial Accounting Standards Board (FASB) and the Governmental Accounting Standards Board (GASB). The FASB and GASB establish and improve financial accounting and reporting standards—known as Generally Accepted Accounting Principles, or GAAP—for public and private companies, not-for-profit organizations, and state and local governments in the United States. For more information, visit www.accountingfoundation.org.

About the Governmental Accounting Standards Board

Established in 1984, the GASB is the independent, private-sector organization based in Norwalk, Connecticut, that establishes accounting and financial reporting standards for U.S. state and local governments that follow Generally Accepted Accounting Principles (GAAP). These standards are recognized as authoritative by state and local governments, state Boards of Accountancy, and the American Institute of CPAs (AICPA). The GASB develops and issues accounting standards through a transparent and inclusive process intended to promote financial reporting that provides useful information to taxpayers, public officials, investors, and others who use financial reports. The Financial Accounting Foundation (FAF) supports and oversees the GASB. For more information, visit www.gasb.org.

Financial Accounting Foundation Reappoints Jeffrey J. Previdi as Vice Chair of the Governmental Accounting Standards Board.

Norwalk, CT—February 23, 2021 — The Board of Trustees of the Financial Accounting Foundation (FAF) today announced the reappointment of Jeffrey J. Previdi as vice chair of the Governmental Accounting Standards Board (GASB). The FAF oversees the GASB and its sister organization, the Financial Accounting Standards Board (FASB).

As vice chair, Mr. Previdi will continue to focus on enhancing stakeholder engagement with a primary focus on financial statement users. His reappointment is effective July 1, 2021, and will extend for a five-year term, ending June 30, 2026.

A former credit analyst with Standard & Poor's Ratings Services, now known as S&P Global Ratings, Mr. Previdi brings more than two decades of experience, in a variety of roles, to his tenure on the

GASB. Most recently, he served as managing director and project leader in the agency's risk program. In that role, he led a global team of individuals who analyzed and implemented rules stemming from the Dodd-Frank Wall Street Reform and Consumer Protection Act.

Mr. Previdi started his career at S&P as a tax-exempt housing bond analyst. He was later promoted to head the team that covers municipal structured finance ratings, eventually assuming co-leadership of the group responsible for all tax-backed ratings in the United States. Mr. Previdi also served on the U.S. Public Finance Criteria Committee for many years.

"We are very pleased that Jeff has agreed to serve an additional term as the GASB vice chair. His depth of knowledge of the dynamics of the municipal bond market will allow the Board to continue to build and strengthen ties with analysts, investors, and the broader financial statement user community," said FAF Board of Trustees Chair Kathleen Casey.

Mr. Previdi holds a bachelor's degree in economics from Connecticut College and a master of public policy degree from the College of William & Mary. He is a member of the National Federation of Municipal Analysts.

"Over the last five years, Jeff has played an important role on the GASB," said GASB Chair Joel Black. "His perspectives and continued effort and focus on not only increasing but enhancing engagement with financial statement users will provide the Board with the type of input needed to reach better-informed decisions on all standard-setting issues."

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The LIBOR Phase-Out: What Borrowers Should Know Now

The London Interbank Offered Rate ("LIBOR") is a benchmark interest rate index used in setting the interest rate for many variable-rate loans and other financial obligations. LIBOR is currently set to be phased out in stages, with the first stage scheduled to begin at the end of this year. This phase-out poses a number of risks to borrowers with outstanding LIBOR-based financial obligations. In this blog, we discuss the steps that borrowers should take now in order to mitigate those risks and to ensure a smooth transition to an alternative benchmark rate.

On November 30, 2020, the International Exchange (ICE) Benchmark Administration (the "IBA"), the administrator of LIBOR, announced its intention to cease publishing one-week and two-month LIBOR on December 31, 2021 and the remaining tenors (overnight, one-month, three-month, six-month and 12-month) on June 30, 2023. The IBA expects to finalize this plan soon. In response, the Board of Governors of the Federal Reserve System, the Office of the Controller of the Currency and the Federal Deposit Insurance Corporation (collectively, the "Agencies") have jointly recommended that banks cease entering into new contracts using LIBOR as a reference rate as soon as practicable and in any event by December 31, 2021. In addition, the Agencies advise that new contracts entered into prior to December 31, 2021 should either use a reference rate other than LIBOR or include effective fallback language with a clearly-defined alternative reference rate effective upon the discontinuation of LIBOR. With these dates and recommendations in mind, borrowers with LIBOR-based financial obligations should consider taking the following steps to address the potential risks posed by the LIBOR transition.

Borrowers should immediately begin the process of identifying their outstanding LIBOR-based financial obligations with maturity dates that extend beyond 2021, including the particular LIBOR tenor (overnight, one-week, one-month, two-month, three-month, six-month or 12-month) that is used. Such obligations may include, but are not limited to, municipal bonds, notes, bank loans and lines of credit, derivatives, leases, installment sales agreements, reimbursement agreements governing letters of credit, standby bond purchase agreements governing the purchase of bonds upon an optional or mandatory tender, other credit facilities and certain investments.

Once the outstanding LIBOR-based financial obligations have been identified, borrowers should review the underlying agreements to determine whether they include effective fallback language. For example, agreements entered into prior to 2017 may contain fallback language designed for only a temporary, rather than permanent, discontinuance of LIBOR as a reference rate. It is therefore unlikely that such language would effectively address the LIBOR transition.

If the agreements include effective fallback language, then borrowers should work with their counsel and financial advisors to consider any fundamental differences between LIBOR and the alternative reference rate that would replace LIBOR, such as: (i) potential changes in interest rate levels, profitability or costs; (ii) responses to changing market conditions; (iii) state lending law constraints; and (iv) the possible impact on financial ratios, reporting and other covenants, or accounting practices. If it is determined that the alternative reference rate could introduce unanticipated risks to, or reduce the anticipated economic return of, the financial obligation, the borrower may wish to approach the counterparty to explore a possible renegotiation of the terms.

If the agreements lack fallback language, or the fallback language is inadequate or otherwise exposes the borrower to the unintended or disadvantageous risks described above, the borrower should consider the steps necessary to amend the agreements within the timeframe anticipated for the LIBOR transition. Such amendments may extend beyond simply swapping out LIBOR for an alternative reference rate. For example, the amendments could include: (i) appropriate adjustments to the spread above the reference rate to account for anticipated differences between the alternative reference rate and LIBOR and/or (ii) a one time, lump-sum payment in lieu of a spread adjustment. In that respect, borrowers should consult with their counsel and financial advisors throughout any amendment process in order to fully evaluate the legal and economic impact of such amendments.

The LIBOR transition also poses unique tax risks to borrowers that are 501(c)(3) corporations.

Under certain circumstances, 501(c)(3) corporations may borrow the proceeds of tax-exempt municipal bonds issued by a quasi-public corporation. If the bonds bear interest at a LIBOR-based rate, then the LIBOR transition and resulting amendments to the financing agreements may subject the borrower to reissuance risk and the possible termination of a qualified hedge. On October 9, 2019, the Internal Revenue Service ("IRS") published proposed regulations (which may be relied upon prior to the release of the final regulations) that would allow 501(c)(3) corporations to amend their outstanding tax-exempt financial obligations in order to replace LIBOR with an alternate reference rate without triggering such tax issues; provided, that the amendments satisfy certain conditions. Pending release of the final regulations, the IRS also issued Revenue Procedure 2020-44 ("Rev. Proc. 2020-44") on October 9, 2020. Under Rev. Proc. 2020-44, the IRS has endorsed certain amendments to financial obligations that incorporate fallback language recommended by the Alternative Reference Rates Committee and the International Swaps and Derivatives Association (ISDA). We will continue to monitor further announcements from the IRS regarding the LIBOR transition, including additional tax consequences or new safe harbors, and provide updates in future blogs.

Additionally, borrowers that are 501(c)(3) corporations should confirm their disclosure obligations with respect to the LIBOR transition. Pursuant to the Securities and Exchange Commission's Rule 15c2-12, an underwriter may not sell municipal bonds without determining that the issuer or the "obligated person" (i.e., the 501(c)(3) corporation that borrows the proceeds of the bonds) has entered into a written continuing disclosure agreement to disclose certain matters to the bondholders on an ongoing basis. Pursuant to continuing disclosure agreements entered into after February 27, 2019, such borrowers are required to file a notice with the MSRB's EMMA system of: (i) the incurrence of material financial obligations or (ii) material amendments to outstanding financial obligations, if such amendments are determined to affect existing bondholders. The borrower would be required to file the notice within ten business days of the effective date of the financial obligation or amendment. Amending the agreements underlying the borrower's financial obligations to add or change the fallback language could trigger this filing requirement.

As a preliminary matter, such borrowers should review their continuing disclosure policies and procedures, particularly the standard for assessing materiality of a financial obligation or related amendment. Then, the borrower should work with its counsel and financial advisor to confirm the specific process for: (i) evaluating LIBOR-related amendments to its financing agreements against this standard and (ii) ensuring the filing of any required notices within the necessary timeframe. For outstanding financial obligations that already contain effective fallback language, such that no amendment to the underlying agreements is necessary, borrowers may consider whether a voluntary disclosure regarding the change in the benchmark rate is appropriate.

By instituting a robust LIBOR transition protocol as soon as possible, borrowers will be well positioned to identify risks and troubleshoot undesirable outcomes in a timely manner.

Adler Pollock & Sheehan P.C.

February 16, 2021

[OCC Publishes LIBOR-Transition Self-Assessment Tool.]

On February 10, 2021, the Office of the Comptroller of the Currency (the "OCC") issued a bulletin ([OCC Bulletin 2021-7]) that provides a self-assessment tool for national banks, federal savings associations, and federal branches and agencies of foreign banking organizations ("banks") to evaluate their preparedness for the expected cessation of the London Interbank Offered Rate ("LIBOR").

What's the Background?
LIBOR is a reference rate used most commonly in transactions involving loans and derivatives engaged in by financial institutions and other sophisticated market participants. It is being phased out globally and replaced by risk-free rates, including the Secured Overnight Financing Rate. It is expected that banks will cease entering into new contracts that use LIBOR as a reference rate by December 31, 2021. For additional background on the LIBOR transition, please visit our LIBOR Transition Resource Center.

The global effort to transition away from LIBOR has been an operational and legal hurdle for the industry, requiring varying levels of attention depending on the size and scope of activity engaged in by market participants. As the OCC notes in its bulletin, "[t]here is risk of market disruptions, litigation, and destabilized balance sheets if acceptable replacement rate(s) do not attract sufficient market-wide acceptance or if contracts cannot seamlessly transition to new rate(s)."

What Is the OCC's Self-Assessment Tool?
The OCC's self-assessment tool is designed to assist bank management personnel in evaluating an institution's progress with the LIBOR transition. The assessment tool, which is annexed to this memorandum, is in the form of a checklist focusing on four areas:

- Exposure Assessment and Planning,
- Replacement Rates,
- Fallback Language, and
- Progress and Oversight.

Not all sections or questions will apply to all banks. According to the OCC, responses will depend on the size and scope of their activities. Perhaps not surprisingly, the OCC also acknowledges that large or complex banks and those with material LIBOR exposures are expected to have a "robust, well-developed transition process in place," whereas smaller or non-complex banks and those with limited LIBOR exposures may be engaging in "less extensive and less formal transition efforts."

The OCC advises that, in 2021, LIBOR-related assessments and plans should be "at least near completion with appropriate management oversight and reporting in place," and that "[m]ost banks should be working toward resolving replacement rate issues while communicating with affected customers and third parties."

Which Institutions Are Covered?
The self-assessment tool is directed to bank management personnel at national banks, federal savings associations, and the federal branches and agencies of foreign banking organizations.

What Are the Next Steps?
There is no indication in the bulletin that responses to the self-assessment tool are required to be reported to the OCC or that a self-assessment is required to be conducted at all. However, as a practical matter, institutions should view the tool as offering an analytical framework for assessing their LIBOR transition preparedness. Responses to the questions contained in the tool will be helpful in eventually responding to any more formal requests for information, including from examiners.

Print or download the OCC's LIBOR Self-Assessment Tool.

MSRB Reminds Dealers of Upcoming Compliance Date for Underwriting Disclosure Obligations.

The MSRB reminded municipal securities dealers of an upcoming March 31, 2021 compliance date concerning the fair dealing obligations of underwriters to issuers.

As previously covered, amendments to the interpretive notice on MSRB Rule G-17 ("Conduct of Municipal Securities and Municipal Advisory Activities") are intended to reduce disclosure burdens on underwriters, as well as the burden on issuers to acknowledge and review disclosures of risks that are (i) unlikely to materialize, (ii) not unique to a particular transaction or underwriter where a syndicate is formed or (iii) otherwise duplicative.

February 18 2021

Cadwalader Wickersham & Taft LLP

GASB Fact Sheet: Financial Reporting Model Improvements

Executive Summary | Full Fact Sheet

2/19/21

How FINRA Should Adapt its Rules to the Work-From-Home Reality.

Potential changes to Financial Industry Regulatory Authority rules would likely reflect on the municipal space as the regulator contemplates lessons learned during the pandemic and dealers seek greater work-from-home flexibility.

In comment letters filed Tuesday, dealer groups said FINRA should work with the Securities and Exchange Commission and Municipal Securities Rulemaking Board to make potential rule changes more cohesive. Though FINRA doesn't write rules for municipal securities, changes to its rules would likely reflect on MSRB rules.

"A lot of the points we make in the context of remote work, work at home and other lessons learned from the pandemic apply equally to the municipal bond business as they do to corporate bonds," said Michael Decker, senior vice president of policy and research at Bond Dealers of America.

Remote work has been so successful, BDA wrote in its letter to FINRA, that some firms are considering implementing work-from-home on a permanent basis. Some of BDA's member firms reported that as office leases come up for renewal, they have considered shrinking the size of offices or eliminating them.

"It is our understanding that other regulators like the Securities and Exchange Commission and the Municipal Securities Rulemaking Board are also examining their regulations that apply to remote work and other issues brought about by the pandemic," BDA wrote. "It is important that FINRA and the other agencies collaborate closely and conduct parallel rulemaking as appropriate."

The regulatory process could take some time. Changes to MSRB rules could be a part of the MSRB's ongoing retrospective rule review, Decker said. Earlier this month, the MSRB decided to retire decades-old guidance as part of that review.

Issues tend to arise when MSRB and FINRA rules don't match, Decker said, leading to dealers incorrectly applying rules.

BDA asked for changes to FINRA's Rule 3110 on supervision, which is similar to the MSRB Rule G-27 on supervision. BDA wants FINRA to amend its rule so that employees conducting trading, sales, or banking activity from home are not mandated to have annual inspections of employees' homes.

Branch offices are inspected every three years and offices of supervisory jurisdiction (OSJ) — where order execution, endorsing customer orders, among others takes place — annually.

"From the rule, it appears that a trader working at home with authority to make trade execution decisions is an OSJ," BDA said. "However, we do not believe it is FINRA's intention to require inspections of employees' homes even if they are working from home."

BDA's letter also asked FINRA to consider a risk-based approach when deciding whether in-person examinations are necessary.

The Securities Industry and Financial Markets Association said an almost fully remote work environment has brought a "quantum leap" towards adopting fully remote capabilities, work habits, procedures, and controls.

SIFMA wants FINRA to revise its definitions of OSJ and branch offices in its Rule 3110. The pandemic has demonstrated that almost all tasks can be done by employees working remotely without on-site supervision, so those terms should be updated, SIFMA said. Using its current rule, firms would have to register a number of one-person branches at remote locations and private homes, SIFMA added, and in the meantime, FINRA should issue additional guidance.

The MSRB would likely amend its Rule G-27 if FINRA made such changes, said Leslie Norwood, SIFMA's managing director, associate general counsel, and head of municipals.

SIFMA also wants changes to FINRA rules so that a location would not be registered as an OSJ or a branch office if there is no customer-facing activity or handling of customers' funds or securities, so long as there is a reasonably-designed system of supervision in place.

If a location can't meet certain requirements such as having few customer complaints or complying with federal securities laws and FINRA rules on books and record keeping, and also meets the definition of a branch office or OSJ, then that location should be registered, SIFMA said. FINRA should also allow dealers to work from home without being subjected to on-site examinations as long as they have adequate supervision, SIFMA said.

"The COVID-19 pandemic has proven that it is possible to shift operations to decentralized, remote locations on short notice," SIFMA said.

"However, we recognize the broad range of broker-dealers which FINRA supervises, some of which may neither have the capabilities to conduct activities in a fully electronic manner, nor the financial resources to upgrade to such a paradigm."

Therefore the "new paradigm should be presented as a complementary framework," SIFMA added.

FINRA allows its member firms to do remote inspections through 2021, and FINRA should allow firms to continue that indefinitely, SIFMA said. FINRA should also take a risk-based approach when it comes to supervision. FINRA Rule 3110 is largely based on where certain activities are conducted, said Kevin Zambrowicz, SIFMA managing director & associate general counsel.

"If certain activities, such as supervising another office, occur at a location then a range of regulatory requirements are triggered," Zambrowicz said. "SIFMA believes that changes in technology and firm-client interactions should result in changes to FINRA Rule 3110 so that firms focus more on the level of risk than where an activity is conducted."

Bond Dealers of America

February 18, 2021

by Sarah Wynn

[FINRA Issues 2021 Report on its Examination and Risk Monitoring Program.]

Released on February 1, the Financial Industry Regulatory Authority (FINRA) [2021 Report on its Examination and Risk Monitoring Program] (Report) provides a roadmap for member firms to use to prepare for examinations and to review and assess compliance and supervisory procedures related to business practices, compliance, and operations. The Report replaces two of FINRA's prior annual publications: (1) the Report on Examination Findings and Observations, which provided an analysis of prior examination results, and (2) the Risk Monitoring and Examination Program Priorities Letter, which highlighted areas FINRA planned to review in the coming year.

This year's Report covers four major areas: (i) firm operations, (ii) communications and sales, (iii) market integrity, and (iv) financial management.

For each regulatory obligation discussed, the Report (1) identifies the applicable rule and key related considerations for member firm compliance programs, (2) summarizes noteworthy findings from recent examinations and outlines effective practices that FINRA observed during its oversight, and (3) provides additional resources that may be helpful to member firms.

Firms should review the Report in connection with their compliance and supervisory procedures and consider enhancements as appropriate. Firms should be prepared to explain their compliance and supervisory policies in these areas in their upcoming FINRA examinations and provide documentation of relevant reviews. The following discussion focuses on FINRA's most notable exam findings and recommended practices.

Firm operations

The first section of the Report covers operations issues related to anti-money-laundering (AML), cybersecurity and technology governance, outside business activities, books and records, regulatory event reporting, and fixed income markup disclosure.

FINRA identifies that many firms employed inadequate AML transaction monitoring and failed to account for AML risks relating to cash management accounts, which led to issues in monitoring, investigating, and reporting suspicious activities related to money movement. Investments in issuers based in restricted markets, microcap and penny stocks, and special-purpose acquisition companies

(SPACs) were identified as emerging AML or financial crime risks. FINRA suggests that firms, as an initial matter, should bolster their customer identification programs by confirming customers' identification using multiple methods. In addition, firms should increase their focus on testing AML procedures and provide appropriate training to their AML personnel. FINRA also observed that some introducing firms improperly relied on their clearing firms for transaction monitoring and suspicious activity reporting; FINRA suggests that introducing firms should ensure they have a complete understanding regarding which responsibilities have been allocated to their clearing firms and should establish policies and procedures to comply with the obligations that remain with the introducing firm.

Cybersecurity has been a perennial emphasis for FINRA, and even more so in this remote work environment. In recent exams, FINRA observed inadequate access controls that led to unauthorized access to critical systems and confidential data. In addition, FINRA observed issues related to insufficient oversight for technology changes and insufficient policies to review the cybersecurity controls of existing technology vendors. FINRA suggests that firms put additional resources into collaborating across technology, risk, compliance, fraud, and internal investigations/conduct departments to assess key risk areas, monitor access and entitlements, and investigate potential violations of firm rules or policies with regard to data access by firm personnel or outside vendors.

One notable observation from the Report related to outside business activities (OBAs) and private securities transactions (PSTs) is that many firms incorrectly assume that all digital assets are not securities and therefore firms do not evaluate or supervise such activities for associated persons who engage in OBAs relating to digital assets that do qualify as securities. FINRA suggests that firms create checklists with a list of considerations to confirm whether digital asset activities would be considered OBAs or PSTs, including reviewing private placement memoranda or other materials and analyzing the underlying products and investment vehicle structures. FINRA further encourages firms to conduct thorough reviews of publicly available data in supervising OBAs, noting that some financial advisers have obtained Paycheck Protection Program loans for undisclosed outside business activities and that this information could be identified through public records.

FINRA also observes that many firms have not performed due diligence to verify their vendors' ability to comply with books and records requirements. FINRA suggests that firms review their vendor contracts and test the capabilities of each of their vendors. Further, on the topic of regulatory events reporting, FINRA notes that the associated persons of many firms have failed to report complaints or other events to their firms' compliance departments. To address these issues, firms should use email surveillance techniques and review publicly available information to identify relevant issues.

The Report also addresses recent amendments to FINRA Rule 2232 and the Municipal Securities Rulemaking Board's Rule G-15, which have required firms to provide additional transaction-related information to retail customers for certain trades in corporate, agency, and municipal debt securities (other than municipal fund securities). FINRA has observed various types of incorrect disclosures and other practices inconsistent with these recently amended rules. Firms should review their confirmation systems and collaborate with their clearing firms to formulate processes that result in proper and accurate disclosures.

Communications and sales

The Report addresses Regulation BI (Reg BI) and Form CRS, communications with the public, private placements, and variable annuities.

In its recent exams, FINRA has found many instances of firms making misrepresentations related to cash management accounts and digital assets. FINRA advises firms to implement comprehensive procedures for its communications, including with respect to certain products such as digital assets. Regarding private placements, FINRA has found that many firms have participated in offerings without performing the necessary due diligence, and FINRA suggests that firms create private placement checklists and perform independent research on the material aspects of each private placement offering including procedures to determine compliance with FINRA Rules 5122 and 5123, which could trigger filings with FINRA. In addition, FINRA notes that firms should evaluate whether participating in certain offerings, such as Regulation A offerings or SPACs, may require the firm to file a continuing membership application with FINRA and obtain its preapproval. FINRA will also focus on app-based platforms with interactive or "gamelike" features that are intended to influence customers and the appropriateness of the activity that they are approving clients to undertake through those platforms.

Regarding variable annuities, FINRA has observed that firms have not adequately addressed issues where customers that accept buyouts may be losing valuable benefits or instances where customers receive recommendations that are inconsistent with their investment objectives. FINRA suggests that firms perform holistic reviews of their supervision over buyouts and recommendations and offer additional training to all registered representative regarding these issues.

Further, while the Report briefly discusses Reg BI, FINRA states that it is in the early stages of reviewing for compliance with these new obligations and that the Report does not include exam findings or effective practices relating to Reg BI and Form CRS. However, FINRA states that it intends to expand its testing of Reg BI and Form CRS in 2021 to give it a more comprehensive view of firms' implementation of those rules.

Market integrity

The market integrity section of the Report covers the Consolidated Audit Trail (CAT), best execution, large-trader reporting, market access, and the vendor display rule.

FINRA has observed firms inadequately tracking and reviewing execution quality versus competing market execution quality, performance of certain order types, and certain metrics such as speed of execution and price improvement. As a related issue, FINRA has observed firms providing inadequate Rule 606 disclosures. FINRA emphasizes that firms should conduct regular and rigorous reviews of execution quality on a quarterly basis or more often if required by the firm's business model. In particular, FINRA has focused on "zero commission" trading and any impact on order-routing practices. Firms should also update their procedures to account for market and technology changes.

Concerning large trader, the report states that firms have simply failed to create procedures to address the relevant requirements, including timely filing of Form 13H. FINRA reminds firms to review their procedures to ensure that the relevant requirements are addressed and to complete daily large-trader calculations to monitor for large-trader status.

Market access is often a focus of FINRA exams. Recently, FINRA has found many firms using insufficient controls and limits in addition to overreliance on third-party vendor tools to effect the required financial controls. To account for these issues, FINRA suggests that firms use rigorous testing of their controls and holistic supervision to monitor for potential manipulative trading patterns, among other things.

Regarding vendor display, FINRA observes that firms have provided inaccurate information or failed to provide the required elements under Rule 603 and suggests that firms focus on performing comprehensive review of their data display systems and validation of information against publicly available sources. Further, regarding the recently adopted CAT rules, the Report states that FINRA is in the early stages of reviewing for compliance with certain CAT rules and therefore does not yet have findings to report.

Financial management

The financial management section of the Report covers net capital, liquidity management, credit risk management, and segregation of assets and customer protection.

The Report details various issues related to net capital, such as incorrect classification of assets (including receivables), liabilities, and revenue, in addition to incorrect capital charges for certain items and inaccurate recording of revenue and expenses. FINRA suggests that firms develop more robust training programs and perform periodic assessments of their net capital treatment with respect to various items, including assets such as CD products, specifically whether account agreements for CDs contain stipulations restricting withdrawals before maturity. FINRA notes that for firms with expense sharing agreements, firms should carefully review their allocation methodology and documentation to support their allocations.

FINRA notes that firms should ensure that if they are acting as chaperones under SEC Rule 15a-6(b)(3), they are appropriately taking required fail net capital charges and that they maintain appropriate blotters reflecting fails.

FINRA notes that firms should review their policies and procedures to ensure that they are reflecting moment-to-moment and open contractual commitment charges on firm commitment underwritings and that firms understand their role in an offering as “best efforts” or firm commitment.

FINRA has observed firms inadequately adjusting their liquidity controls, which has led to difficulties in accounting for their business. FINRA reminds firms that they should continue to update their liquidity risk management practices to account for factors such as quality of funding sources, potential mismatches in duration between liquidity sources and uses, and potential losses of counterparties. FINRA notes that firms should review their policies and procedures to ensure compliance with SEC Rule 17a-3(a)(23) to make and keep records documenting that they maintain adequate credit, market, and liquidity risk management controls.

Many firms have implemented deficient processes related to credit risk management by performing no credit risk management reviews or by not monitoring exposure to affiliated counterparties. FINRA recommends that firms develop comprehensive controls to capture, measure, and manage relevant factors related to their credit risk.

Finally, the Report addresses failures with respect to remediating segregation deficits (in possession or control of customers’ fully paid securities or excess margin securities), including understanding the cause of the deficit and appropriate resolution and ensuring control locations are appropriately coded as “good” or non-good . FINRA notes that some firms have inadequate policies and procedures with respect to determining whether the firm is acting as custodian with respect to digital securities. FINRA also notes that some firms that operate under an exemption from the customer protection rule do not transmit (in a timely manner) customer checks that they receive to their clearing firms. Moreover, FINRA has observed that some firms have inaccurate reserve formula calculations due to errors in coding arising from limited personnel training and staff turnover as well as from inadequate communication within the firm and gaps in reconciliation calculations. As such, FINRA states that firms should ensure that the proper departments within each firm are coordinating appropriately and that the relevant personnel receive appropriate training.

Conclusion

The Report covers a wide array of topics and discusses themes that were commonly found in past versions of FINRA's Risk Monitoring and Examination Program Priorities Letter and its Report on Examination Findings and Observations. In addition, the Report speaks to some newer areas of focus, including Reg BI, CAT, and the marketing and monitoring of digital asset activity. As detailed here, firms should review their practices and procedures in each of the areas and be prepared to address these areas in future examinations.

Sidley Austin LLP – James Brigagliano, W. Hardy Callcott, Kevin J. Campion, David M. Katz, John I. Sakhleh, Corin R. Swift, Michael D. Wolk and Steffen Hemmerich

February 8 2021

SIFMA Issues New MSRB Rule G-17 Model Risk Disclosure Documents for Additional Products.

New York, NY, February 2, 2021 – SIFMA today announced it has made new additions to its set of G-17 Model Risk Disclosure Documents to help municipal securities underwriters comply with the recently amended requirements for disclosure to municipal issuers set forth by the revised interpretive guidance to Municipal Securities Rulemaking Board (MSRB) Rule G-17.

The new model disclosure documents cover the following products:

1. Capital Appreciation Bonds (CABs)
2. Commercial Paper (CP)
3. Convertible Advance Refunding (Cinderella) Bonds
4. Variable-Rate Remarketed Obligations (VROs)
5. Exchange Offers

"SIFMA created our G-17 model underwriter documents in 2012 to assist underwriters in their compliance with the Rule. In May 2020 we revised our G-17 model underwriter disclosure documents to reflect the changes the MSRB made to the guidance, and in early 2021 we offered newly updated versions of our model risk disclosures as well," said Bernard Canepa, SIFMA vice president and assistant general counsel. "As part of these efforts, our members requested that we create additional model risk disclosures for other products, to assist them in complying with MSRB Rule G-17's requirement to disclose risks associated with complex municipal securities financings. We are glad to support the underwriting community in managing their legal costs and reducing their regulatory risks by issuing these documents today."

The MSRB established a compliance date of March 31, 2021 (extended as a result of the COVID-19 pandemic) for its amended and restated guidance regarding the fair dealing obligations underwriters owe to issuers of municipal securities under MSRB Rule G-17, which covers the conduct of both municipal securities and municipal advisory activities.

SIFMA recommends that underwriters update their internal processes and continue to educate their public finance departments and issuer clients about the coming changes.

MSRB Analyzes Effects of COVID-19 on Municipal Bond Market.

In a new report on the effects of the COVID-19 pandemic on the municipal bond market, the MSRB found market resilience in the face of unprecedented volatility.

The MSRB found:

- unprecedented municipal mutual fund outflows in March 2020, but net inflows of $39 billion by the end of the year;
- a return to lower rates following significant market dislocation in March 2020;
- a record new issuance of $483 billion in 2020; and
- that COVID-19-related disclosures, of which the MSRB received 38,000 between February and December 2020, accounted for 21% of all disclosure submissions to its Electronic Municipal Market Access website.

Cadwalader Wickersham & Taft LLP

January 29 2021

BDA Washington Weekly – Munis Considered in Stimulus Debate

As the Biden Administration works to close its second full week in office, both of which have included a flurry of executive actions and little legislative progress, a deal on additional stimulus seems imminent, but questions remain on its size and scope.

President Biden touted bipartisanship in his 2020 presidential run, and he still appears to want to remain on that path. However, House and Senate Democratic Leadership have become restless and are charting a course to use the partisan tactic of budget reconciliation, ensuring the massive spending package can pass on a simple majority vote which passed the Senate early this morning after 15 hours of debate and a tie-breaking vote by VP Harris.

Earlier this week a group of GOP Senators met with President Biden and VP Harris to discuss their initial offering and present a trimmed back $600 million dollar plan. Of note, the GOP does not contain any aid for state and local governments, while the Biden plan offers more than $350 billion in unencumbered aid.

Yesterday, Senator Roger Wicker (R-MS) introduced amendments to the stimulus package that would restore tax-exempt advance refundings and create a new direct-pay bond program exempt from sequestration. Senate Republicans offered well over 700 amendments and only a portion was considered. While these provisions were not amongst those voted on, it is a step in the right direction for continued consideration of this Congress.

More on this below.

Continue reading.

Bond Dealers of America

February 5, 2021

Green Bond Disclosure: NFMA Call for Volunteers

The NFMA is seeking volunteers for participation in a committee to develop a "Best Practices for Green Bond Disclosure" paper.

- The Green Bond Disclosure committee will help facilitate and develop a much-needed Best Practices regime for issuer disclosure on Green Bonds.
- The paper will focus specifically on guidelines for new-issue disclosures to be included in offering documents.
- There are no well-established Green Bond Disclosure guidelines currently available to the market.
- This committee will have the assistance of the State of California's Green Bond Market Development Committee, which is interested in supporting NFMA in this effort and is willing to dedicate resources including staff at the UC Berkeley Goldman School – Center for Environmental Public Policy.

To volunteer, please contact Lisa Good at lgood@nfma.org.

SEC Seeks Public Input on Possible Money Market Fund Reforms.

WASHINGTON, Feb 4 (Reuters) – The U.S. Securities and Exchange Commission is kicking off a renewed effort to overhaul rules around money market funds, soliciting public input on how to reform the sector.

The consultation, announced Thursday, suggests the SEC wants to kickstart languishing efforts to address the sector, which has twice needed government intervention in recent years to stabilize after investor runs.

Specifically, the agency is seeking comment on a report issued by a Treasury-led working group in December, which called for significant policy changes to address weaknesses in the market. The report laid out a number of reform options, including setting stricter rules around fund redemptions, or higher capital buffers for such funds, but did not advocate any particular approach.

The SEC is casting a wide net with its solicitation, seeking comment on any suggestions from the Treasury report, or any additional suggestions on how to reform the market.

The most recent government intervention came in March, when short-term funding seized up with a massive pandemic-driven sell-off in U.S. markets, including Treasuries. Among institutional and retail prime money market funds, which allow daily redemptions while holding less-liquid short-term assets, outflows as a percentage of fund assets exceeded that of the September 2008 crisis.

The crunch prompted the Federal Reserve to buy $1.6 trillion in Treasuries and other bonds to stabilize the markets. It continues to buy around $80 billion monthly. Top officials have warned that liquidity could collapse again if that support is withdrawn.

(Reporting by Pete Schroeder; Editing by Dan Grebler)

February 4, 2021

SIFMA: LIBOR Consultation on Timeline of Cessation of Published LIBOR Fixings

SUMMARY

SIFMA, AFME, and ASIFMA are pleased to respond to this important consultation on the timeline for the cessation of published LIBOR fixings. Our members have been actively engaged in the LIBOR transition process. We appreciate that IBA is asking for market input on these critically important steps in the transition.

Read the SIFMA submission.

BDA Announces Newly Formed MBFA Council.

Today, the Bond Dealers of America launched the new Municipal Bonds for America (MBFA) Council.

The press release can be viewed here

Today's story in the BondBuyer story can be viewed here

Municipal Bonds for America is a Council of the municipal market leadership working together and in concert with issuers and State and local groups to promote and advance the municipal bond market in the context of infrastructure.

MBFA is led by an Advisory Board of recognized municipal market leadership, past and present, with deep knowledge and experience in the industry and in Washington, DC:

Sheila Amoroso, former Director, Municipal Bond Department, Franklin Templeton Fixed Income Group

Frank Chin, former Head of Public Finance, Citi; Co-founder of American Public Infrastructure LLC

Ron Fielding, former Head of Municipal Bond Fund Group, OppenheimerFunds

Kevin Giddis, former President, Fixed Income Capital Markets, Raymond James

Chris Hamel, former Head of Municipal Finance, RBC Capital Markets

Lynnette Kelly, former CEO, Municipal Securities Rulemaking Board

Hector Negroni, former Head of Municipal Bond Trading, Goldman Sachs; Founder and CEO, Foundation Credit

MBFA is committed to advancing proposals that improve the municipal securities market while protecting the interests of taxpayers, investors, and state and local governments.

For more information on the Municipal Bonds for America Council please visit our website at www.munibondsforamerica.org or contact Brett Bolton at brettbolton@munibondsforamerica.org.

Bond Dealers of America

January 27, 2021

Federal Reserve Seeks a Permanent Muni Expert.

The Federal Reserve is looking to add a municipal market specialist to its ranks following a tumultuous year for munis in which the Fed saw a need to quickly create programs to help state and local governments.

In a job posting, the Federal Reserve Bank of New York said it is looking for a permanent municipal markets specialist. That person should have at least seven years of relevant professional experience, some including in municipal finance, expertise in the municipal markets, and the ability to identify market themes relevant to the Fed's objectives.

The position would be within the FRBNY's Markets Group, the largest group at FRBNY responsible for monitoring and analyzing all global capital markets on behalf of the Fed.

"You will work in an environment with a diverse group of experienced professionals to foster and support the safety, soundness, and vitality of our economic and financial systems," the job posting said. "It is a challenge that demands the skills of a financial service professional and the intelligence an academic?all combined with a passion for public service."

The job would be in New York and would ideally be someone who can monitor and analyze municipal markets and can interact extensively with market participants, the Fed said. The ideal candidate will also have expertise from either the broker dealer or buy side on specifically market sales and trading rather than credit or banking.

"It's very positive if the Fed is trying to enhance in-house expertise on municipal bonds and municipal finance," said Chuck Samuels, counsel to the National Association of Health & Educational Facilities Finance Authorities. "It has not had to have that expertise in the past and it clearly did not as it rolled out these various programs. That is why they borrowed people from elsewhere."

In March, the Fed hired Kent Hiteshew, a veteran muni banker and former Treasury official and the Municipal Securities Rulemaking Board's John Bagley – both on a temporary basis.

In March, the Fed created the Municipal Liquidity Facility to buy $500 billion of short-term notes and created the Money Market Mutual Fund Liquidity Facility to buy short-term debt with maturities of 12 months or less.

"Given the programs that we saw last year that may continue in some form in the future, it makes a lot of sense to build up that expertise," Samuels said.

"Surely they want to be in a position to participate and plan for the future and having greater in-house expertise allows them to do that," Samuels added.

The Fed's non-profit expertise is also scarce. They don't have that in-house expertise either when it comes to non-profits, Samuels said.

It is unclear whether the Fed will take steps to create a new muni program since the MLF expired at the end of 2020. The MMLF expires on March 31, 2021. The Fed can?t reestablish the MLF and use it again in 2021, but can still create new or similar programs.

By Sarah Wynn

BY SOURCEMEDIA | ECONOMIC | 01/26/21 02:19 PM EST

Network Sends Exempt Bond Wish List to Yellen.

Public finance organizations promptly urged the new leadership of the Treasury Department to pursue tax policies favorable to tax-exempt bonds.

In a January 28 letter to Treasury Secretary Janet Yellen, who assumed office two days earlier, groups belonging to the Public Finance Network said their members "rely significantly on the federal partnership represented by the tax-exemption for municipal securities and the effective use of that tax exemption for their own communities."

The network asked Yellen to consider several recommendations — first on the list is preserving the tax exemption for municipal bonds.

Eliminating, reducing, or capping the exemption would mean higher costs for critical projects financed by state and local issuers, forcing state and local governments to make difficult and pro-recessionary choices, the network said. It added that taxpayers ultimately would bear the increased costs.

Treasury should also support restoration of the tax exemption for advance refunding bonds, the Public Finance Network said. The exemption was eliminated by the Tax Cuts and Jobs Act.

"Restoration of this tax exemption would require an act of Congress, but would be one of the most effective actions to provide state and local governments with more financial flexibility to weather downturns and increase infrastructure investment," the letter said.

Another priority for the Public Finance Network is making it easier for smaller issuers to access capital.

The network spoke favorably of the Municipal Bond Market Support Act of 2019, which sought to make more small issuers eligible to issue bank qualified debt and "provide an additional purchaser in our markets to further diversify sources of credit to state and local governments."

Treasury's Office of Tax Policy should also have a dedicated municipal bond expert, a position that's been unfilled since 2019, according to the network.

"This expertise in the tax rules for qualified municipal securities and the manner in which the municipal bond markets operate had long been effective in drafting and implementing tax policy in the tax-exempt domain," the letter said. "Filling this role would allow Treasury to better meet the diverse needs of municipal issuers."

In recent weeks, other municipal finance groups have also asked the new administration to adopt policies favorable to exempt financing.

The Bond Dealers of America made several recommendations to the incoming Biden administration, including maintaining the tax exemption for municipal bonds, restoring advance refunding bonds, and expanding private activity bonds.

TAX ANALYSTS

by FRED STOKELD

POSTED ON FEB. 1, 2021

Libor Doesn't Have to Mean Libor.

My basic theory of Libor, the London interbank offered rate, is that it is a function call. You want to have a contract that specifies a floating interest rate, one that changes (say) every quarter based on prevailing interest rates. One way to do that is specify in the contract that, each quarter, you will observe some market data and call some banks for quotes and do some calculations and produce a number, the number being the interest rate. The contract could spell out the entire methodology to take some facts about the world and convert them into an interest rate.

But the way Libor works in contracts is mostly not like that. The way Libor works in contracts is mostly by saying "the interest rate will be whatever Libor says it is." (Plus a fixed spread.) Exactly how that is expressed varies, but it is generally expressed by reference to some source, either the official administrator of Libor (formerly the British Bankers' Association, now Intercontinental Exchange Benchmark Administration) or a Bloomberg or Reuters page that displays the official Libor.[1]

And then ICE is in charge of figuring out what Libor is, and Bloomberg and Reuters are in charge of getting that information and displaying it, and your contract can just take it as a given. To write the contract, you don't have to know the exact mechanics of how ICE calculates Libor by polling banks about the interest rate at which they can do unsecured short-term borrowing. If ICE adds banks to the panel that it polls, or deletes banks, or changes the wording of the question it asks them, or tells them to use more transaction data in answering the question, or changes its method of topping and tailing and averaging the answers—all of that just flows through to your contract automatically. You call the Libor function, it returns a value, you use the value, and you don't really care how the function operates internally. The people who maintain the function can tinker with it, and you won't even notice.

We are in the middle of a long and boring effort to get Libor out of contracts. Contracts—floating-rate loans, interest-rate derivatives, etc.—are no longer supposed to use the Libor function. The main reason for this change is that it turns out that the way that Libor was calculated, during and shortly after the 2008 financial crisis, was pretty bad: The BBA polled banks about their cost of short-term unsecured borrowing, and the banks lied about it, so Libor was, in an important sense, "wrong."[2] A secondary reason for the change is that the eurodollar markets used to calculate Libor are not as active and important as they once were, so even a more honest calculation of Libor—the kind that ICE does now—may not reflect "true" interest rates the way Libor used to. And so regulators want banks and derivatives traders to stop using Libor and start using some other, more market-based interest-rate reference. In the U.S. this is mainly SOFR, the Secured Overnight Financing Rate, which is calculated by the New York Fed based on actual transaction data.

There are various problems with this transition, but the simplest and dumbest one is that there are a lot of contracts that say “the interest rate will be Libor” (plus a spread), and you have to go find all of them and get the contracting parties to agree to cross that out and write in “the interest rate will be SOFR” (plus a spread) or whatever. That is hard administratively—you have to find the contracts, you have to get the two parties to pay attention, etc.—but there is also an economic problem. Libor and SOFR are different; they measure different things; Libor is unsecured and SOFR is secured; SOFR is overnight and Libor comes in longer tenors. If your loan pays interest of six-month Libor plus 150 basis points, will it now pay the six-month SOFR futures rate plus 175 basis points, or six months of daily SOFR compounded in arrears plus 168 basis points, or what? The borrower will say “let’s change to SOFR but not increase the spread,” the lender will say “let’s change to SOFR and increase the spread a lot,” there will be some economics to be worked out, and there’s no guarantee that everyone will agree. And so banks are going out and trying to renegotiate trillions of dollars of contracts to replace Libor with something more sensible, but they kind of have to do that one client at a time.

The simple dumb solution would be to answer these questions, once and for all, by changing the internal mechanics of Libor. ICE could just wake up one day and say, “We will keep reporting Libor, but instead of being based on a panel of banks, it will be SOFR plus 20 basis points, that’s just what Libor means now.”[3] And then if your contract says “our interest rate will be Libor,” you will go to the Bloomberg or Reuters page that reports Libor, and it will keep reporting Libor, and the function will produce an answer just like before. But now the guts of the function will be based on SOFR—the good rate, the one regulators like, the one with a future—rather than the old and discredited method of calling up banks for their unsecured lending rates.

In practice it would be a bit tough for ICE to do this, and people who use Libor and don’t like how ICE answers the economic questions would get mad and sue it. On the other hand … New York could do it?

> New York Governor Andrew Cuomo has proposed legislation that would help prevent hundreds of billions of dollars of financial contracts from descending into chaos when the London interbank offered rate expires.
>
> Provisions to help troublesome Libor-linked contracts switch to replacement rates are contained in Cuomo’s state budget plan, which was published on Tuesday. Bankers, investors and regulators see such proposals as crucial to ensuring that a large swath of the global financial system isn’t disrupted. …
>
> As home to the world’s biggest financial center, much of the debt falls under New York law. …
>
> The U.K. hasn’t faced the same complications around sterling Libor, partly because of its different exit strategy. Proposals to keep publishing a “synthetic” Libor number that doesn’t require trading data from panel banks would help legacy contracts that can’t transition to avoid a cliff-edge scenario at the end of 2021, when the U.K. benchmark will likely retire.
>
> In New York, the bill would allow contracts to instead use the replacement rate recommended by the Fed Board, New York Fed, or the ARRC.

Lots of financial contracts are governed by New York law, so the New York legislature can, within some limits, change what those contracts mean. Cuomo’s budget includes an article on “Libor

Discontinuance," which says (section 18-401, page 237) that "On the Libor replacement date, the recommended benchmark replacement shall, by operation of law, be the benchmark replacement for any contract, security or instrument that uses Libor as a benchmark," unless there is a different fallback provision in the contract. If you trace through the defined terms, what that means is basically that when Libor stops publishing, any contracts that use Libor will automatically instead use a different function. The different function will be whatever is recommended by the Fed,[4] which is administering the Libor transition, and will presumably be (1) SOFR, (2) termed out in some way (using futures curves or compounding to compute a longer-term rate from overnight SOFR), (3) plus a spread (to reflect the difference between secured and unsecured rates). The law doesn't choose what the function will be; it leaves it up to the Fed.

This is actually pretty similar to the U.K.'s "synthetic Libor," though the U.K. approach is a bit more direct:

> The term began circulating in the leveraged loan and floating rate bond markets after the UK government announced in late June 2020 that it intends to amend the UK regulations of benchmark interest rates to give the Financial Conduct Authority ("FCA") enhanced powers, including the power to select a new calculation methodology to any benchmark. This includes the power to direct the administrator of LIBOR to change the methodology of LIBOR if the FCA determines that the current LIBOR methodology (i.e., polling of panel banks) is no longer representative of the market and if it would be both more appropriate and feasible to change to an alternative methodology. This new methodology would result in a new interest rate being published as the "screen rate" instead of LIBOR. In other words, the Intercontinental Exchange intends to publish a new rate on the same screen and in the same location on the screen where it had previously published LIBOR.
>
> However, it is important to understand that, as envisioned by the FCA, this new rate would not replicate LIBOR through some synthetic calculation. Rather, in the accompanying FAQs the FCA explains that the new methodology would follow the market consensus that emerges on how to calculate fair alternatives to LIBOR. For most currencies, this will be a risk-free rate chosen by the applicable LIBOR currency area, adjusted for the relevant term of the contract, and with a fixed credit spread adjustment added. In other words, for the USD LIBOR market, "synthetic LIBOR" would likely be SOFR plus a modifier.

The U.K. approach would *directly change what shows up on the Libor scree*n. Contracts wouldn't have to change at all; they'd continue to call the Libor function, but by U.K. law that function would now work differently. The New York approach would just automatically change all the contracts written under New York law. The contract—the piece of paper documenting the trade—would still say "the interest rate is Libor," but lawyers would know that, as a matter of law, you have to read those words to mean "the interest rate is SOFR plus a spread."

Nobody thinks any of this is a *good* solution. Here is a speech from last March by Edwin Schooling Latter of the U.K. FCA, warning people that synthetic Libor is a terrible idea, because "parties who rely on regulatory action enabled by this legislation, will be giving up their control over the economics of their contracts." Much of the proposed New York legislation is about exempting contracts from the law if the contract parties pick some other fallback, some other way to get around Libor. Obviously it is better for each contract to be carefully renegotiated to reflect the economic intent of the parties, rather than some dumb one-size-fits-all approach imposed by Albany.

But that is easy to say, and hard to do. What is the economic intent of the parties? Often they have different intents: Borrowers want to pay a lower rate, lenders want to get a higher rate, etc. Often they have no particularly clear view on what sort of interest rate they want and how it should be calculated. *That was why they used Libor*, why they called some externally administered function and let someone else give them a number for their interest rate. That number was widely accepted, it was the “normal” number, and that’s what they wanted; they just wanted whatever the interest rate was. For those people, sure, whatever, let New York law tell them to use what the New York Fed thinks the interest rate is. They want someone else to tell them a number. Why not do that?

Bloomberg Opinion

by Matt Levine

Jan 21, 2021

[NABL Releases an Update to the Crafting Disclosure Polices Paper.]

The National Association of Bond Lawyers (NABL) has released Section 5.3 to Appendix B of *Crafting Disclosure Policies*, a paper released by NABL in 2015. The purpose of Section 5.3 is to provide NABL members with tools to advise issuers and obligated persons of municipal securities in developing written disclosure policies and procedures in response to the 2019 amendments that added two new listed events to Rule 15c-12 (the Rule). Section 5.3 is intended to be read in connection with Appendix B of Crafting Disclosure Policies.

You can view Crafting Disclosure Policies here.

You can view Section 5.3 here.

FAF Trustees Announce New Members and Reappointments of the GGASAC.

Norwalk, CT—January 21, 2021 — The Board of Trustees of the Financial Accounting Foundation (FAF) announced today the appointment of Kristine Brock, Chris Brown, Davis Collins, Samuel Owl, Beth Pearce, Daron Tarlton, Elizabeth Thomas, Stephen Stuart, and Phil Vidal to the Governmental Accounting Standards Advisory Council (GASAC). All appointees’ terms began January 1, 2021.

In addition to the nine newly named members, the FAF reappointed eight GASAC members and extended the term of Chair Robert Scott by an additional year.

The GASAC advises the Governmental Accounting Standards Board (GASB) on strategic and technical issues, project priorities, and other matters that affect standard setting. The GASAC provides the GASB with diverse perspectives from individuals with varied governmental, professional, and occupational backgrounds.

“I am pleased to welcome our new GASAC members and know they will play an important role in the GASB process,” said Kathleen L. Casey, chair of the FAF Board of Trustees. “I would also like to thank the departing members for their time, expertise, and contributions to improving financial reporting for all our stakeholders.”

The new GASAC members will serve a two-year term and are eligible to be reappointed for up to two additional consecutive terms. They are:

- Kristine Brock, City of Franklin, TN, nominated by International City/County Management Association (ICMA)
- Chris Brown, Comptroller, City of Houston, TX, nominated by National League of Cities (NLC)
- Davis Collins, T. Rowe Price, nominated by Investment Company Institute (ICI)
- Samuel Owl, CLA, nominated by Native American Finance Officers Association (NAFOA)
- Beth Pearce, Treasurer, State of Vermont, nominated by National Association of State Treasurers (NAST)
- Stephen Stuart, Bureau of Governmental Research, nominated by Governmental Research Association (GRA)
- Daron Tarlton, Dixon Hughes Goodman, nominated by Healthcare Financial Management Association (HFMA)
- Elizabeth Thomas, Butler Snow, nominated by National Association of Bond Lawyers (NABL)
- Phil Vidal, U.S. Census Bureau, nominated by U.S. Census Bureau.

New two-year terms of the reappointed members begin January 1, 2021. The reappointed members are:

- Duncan Baird, nominated by National Association of State Budget Officers (NASBO)
- Robert Balducci, nominated by U.S. Conference of Mayors (USCM)
- Kristen Fontana, nominated by Securities Industry and Financial Markets Association (SIFMA)
- Matt Harvey, nominated from insurance industry investors
- Joe Morrissette, nominated by National Governors' Association (NGA)
- Lise Valentine, nominated by Association of Local Government Auditors (ALGA)
- Lisa Washburn, nominated by National Federation of Municipal Analysts (NFMA)
- Michael Weinstein, nominated from municipal bond insurance industry.

Nine members departed from GASAC on December 31, 2020: Eric Bringardner, Wayne Gerhold, Brian Green, Demetria Hanna, Shirley Hughes, John Kinnaird, Fiona Ma, Nadine Paisano, and Phyllis Resnick.

For a complete list of current Council members, visit the GASAC webpage.

NFMA 2021 Officers and Board Announced.

The NFMA is pleased to announce that Anne Ross, Principal Consultant, Muni Credit & Compliance Advisors, LLC, has been elected NFMA Chair for 2021. She succeeds Nicole Byrd, Senior Investment Professional at Nationwide Mutual Insurance, who served as 2020 NFMA Chair. Rachel Barkley, Senior Vice President at Loop Capital Markets, has been elected Vice Chair, and will also chair the Industry Practices Committee. Mark Capell, Managing Vice President and senior underwriter at BAM, will continue his role of Secretary and Education Chair. Elected Treasurer for 2021 – 2022 was Ron Mintz, Principal and Senior Municipal Investment Analyst in Vanguard's Investment Management Group. Together with Neene Jenkins Executive Director at JPM Chase Asset Management, Mr. Mintz will chair the NFMA's 2021 Annual Conference. To view the full list of 2021 NFMA Board members, go to About Us/Governance. Information on the 2021 Annual Conference will be released in coming weeks.

SIFMA Issues Updated MSRB Rule G-17 Model Risk Disclosure Documents.

New York, NY, January 13, 2021 – SIFMA today announced updates to its set of G-17 Model Risk Disclosure Documents to help municipal securities underwriters comply with the recently amended requirements for disclosure to municipal issuers set forth by the revised interpretive guidance to Municipal Securities Rulemaking Board (MSRB) Rule G-17.

The new documents update existing risk disclosures required for complex municipal securities financings, including floating rate notes, fixed rate bonds, interest rate swaps, forward delivery bonds, tender offer bonds and variable rate demand obligations (VRDOs).

"SIFMA created our G-17 model underwriter documents in 2012 to assist underwriters in their compliance with the Rule. In May 2020 we revised our G-17 model underwriter disclosure documents to reflect the changes the MSRB made to the guidance, and we now offer updated versions of model risk disclosures as well," said Bernard Canepa, vice president and assistant general counsel, SIFMA. "The latest versions include clearer drafter's notes to make it easier to utilize the model documents, address the transition away from LIBOR with ARRC fallback language, and add the disclosure of additional risks not previously included in the model documents."

The MSRB established a compliance date of March 31, 2021 (extended as a result of the COVID-19 pandemic) for its amended and restated guidance regarding the fair dealing obligations underwriters owe to issuers of municipal securities under MSRB Rule G-17, which covers the conduct of both municipal securities and municipal advisory activities.

SIFMA recommends that underwriters update their internal processes and continue to educate their public finance departments and issuer clients about the coming changes. SIFMA also plans to introduce six new model risk disclosures in the near future to further assist underwriters in complying with Rule G-17.

SIFMA Municipal Securities Markets Documents.

Follow the links below to view the model documents and other resources in SIFMA's Municipal Securities Markets Standard Forms and Documentation Library.

SIFMA Updates MSRB Model Disclosure Documents: Cadwalader

SIFMA updated model disclosure documents for municipal security underwriters. The new model disclosure documents address updated requirements (see prior coverage) under MSRB Rule G-17 ("Conduct of Municipal Securities and Municipal Advisory Activities").

Specifically, SIFMA modified existing risk disclosures necessary for complex municipal securities financings, such as (i) floating rate notes, (ii) fixed rate bonds, (iii) interest rate swaps, (iv) forward delivery bonds, (v) tender offer bonds and (vi) variable rate demand obligations. Additionally, SIFMA provided guidance to address the transition away from the London Inter-Bank Offered Rate (or "LIBOR").

As previously covered, SIFMA's G-17 model disclosure documents and drafting guidance are composed of two disclosure letters that reflect underwriters' amended fair dealing obligations. According to SIFMA, the disclosure letters apply to:

- "Sole or Senior Managing" underwriters for the purposes of (i) making standard disclosures and (ii) the self-disclosure of conflicts; and
- co-managing underwriters regarding the self-disclosure of conflicts.

SIFMA encouraged underwriters to (i) update relevant internal processes in connection with the revised model disclosure documents and (ii) continue to inform clients and public finance departments of upcoming compliance changes. SIFMA stated that it intends to introduce six new model risk disclosures in order to further facilitate underwriters' compliance with Rule G-17.

The compliance date for the updated Rule G-17 requirements is March 31, 2021 (see prior coverage).

Cadwalader Wickersham & Taft LLP

January 13 2021

SIFMA Updates Model Documents for Libor's End.

The Securities Industry and Financial Markets Association updated its model disclosure documents to help dealers through complex financings as the London Inter-bank Offered Rate (Libor) is set to phase out this year.

SIFMA released those updated documents Wednesday to help dealers comply with Municipal Securities Rulemaking Board Rule G-17 on fair dealing, reducing legal drafting costs and to increase their confidence in compliance.

The group specifically revised six of its Rule G-17 model disclosure documents for risk disclosure including floating rate notes, fixed-rate bonds, interest rate swaps, forward delivery bonds, tender offer bonds and variable rate demand obligations.

SIFMA created its Rule G-17 Model Disclosure Documents in 2012 and said it was time to update them with upcoming changes such as the Libor transition. The Secured Overnight Financing Rate is expected to replace Libor by the end of this year.

In April, the Alternative Reference Rates Committee released its fallback language, which it said was meant to provide a robust waterfall that would allow for a conversion to SOFR-based rates.

"The latest versions include clearer drafter's notes to make it easier to utilize the model documents, address the transition away from Libor with ARRC fallback language, and add the disclosure of additional risks not previously included in the model documents," said Bernard Canepa, vice president and assistant general counsel at SIFMA.

Some of those additional risks include extending the settlement risk to fixed-rate bond disclosure and the impact of the Securities and Exchange Commission?s money market reforms to its VRDO disclosure documents.

Since 2010, the Securities and Exchange Commission has adopted reforms to reduce investor runs on money market funds in times of financial crisis. Reforms adopted in 2014 made a significant impact on money market funds, particularly funds that invest in municipal securities such as VRDOs, SIFMA wrote in its VRDO disclosure document.

SIFMA last updated its model documents in May 2020 to respond to changes to Rule G-17's interpretive guidance approved by the SEC in November 2019. Once in effect those changes will reduce the volume of disclosures issuers receive from underwriters at the beginning of a deal, which many in the market agreed had become too voluminous and wordy to be useful.

Due to the coronavirus, the compliance date for the updated interpretive guidance has been pushed to March 31, 2021 from Nov. 30, 2020.

SIFMA wanted to make its model documents more user-friendly with clearer drafter?s notes and instructions, to help with the transition of Libor and additional risks.

"After making several important revisions to our G-17 underwriter model disclosure documents in May, we thought it was important to revisit the risk disclosures that were created in 2012," Canepa said. "It had been a while so we wanted to look at them again."

The group also plans to release six additional new risk disclosures soon.

By Sarah Wynn

BY SOURCEMEDIA | MUNICIPAL | 01/14/21 02:24 PM EST

Libor Transition is a 2021 SEC Priority for the Muni Market.

The 2021 priorities for the Office of Municipal Securities at the Securities and Exchange Commission are the transition away from Libor and improving the timeliness of financial disclosures.

Rebecca Olsen, director of the Office of Municipal Securities, highlighted the Libor transition in a presentation Wednesday in which she noted that the addition any other priorities will have to await the appointment of a new SEC chairman.

Gary Gensler, the former chairman of the Commodity Futures Trading Commission, has been widely reported as President-elect Joe Biden's expected choice. Whoever is nominated by Biden will require Senate confirmation and could be weeks away from taking office.

Olsen's office, meanwhile, is moving ahead on the Libor transition and issued a detailed advisory Friday to the municipal securities market.

Olsen told members of the Government Finance Officers Association Debt Committee on Wednesday that the new advisory is focused "on both municipal issuers and municipal advisors."

"According to a statement released by the Alternative Reference Rate Committee last March, there is approximately $44 billion with outstanding publicly-offered municipal securities that are Libor based," Olsen said.

Olsen added that "all-new municipal issuers may be exposed in many other ways, including private equity funds, notes, bank loans, derivatives and other credit agreements or financial instruments that use Libor as a reference rate."

The SEC advisory highlights how the discontinuation of Libor could have a significant impact on the municipal securities market, stating that its discontinuation "may present a material risk for many issuers of municipal securities and other obligated persons."

The advisory said municipal obligors should consider whether any state laws constrain their ability to replace Libor with an alternative reference rate. They also should consider the tax consequences of the transition and its impact on hedge floating-rate investments. They also should consider whether they are familiar with the process by which any of their outstanding debt obligations referencing Libor can be amended and if those amendments are reasonably feasible within the timeframe anticipated for the Libor transition.

"Municipal obligors should consider the potential actions available to mitigate these risks, including the repercussions of not taking the steps necessary to effect an orderly and timely transition, in anticipation of Libor's discontinuation," the SEC's Office of Municipal Securities said. "Risks that could arise in connection with the Libor transition are also relevant to other municipal securities market participants, including those who advise municipal obligors."

The advisory "urges municipal obligors to identify existing contracts that extend past 2021 to determine their exposure to Libor."

"Potentially affected contracts include, but are not limited to, municipal bonds, notes, bank loans, derivatives, leases, installment sales agreements, other credit agreements and financial instruments, commercial contracts (e.g., contracts with vendors, suppliers, service providers, other contractors, employees, and others), and investments held by municipal obligors. To avoid unanticipated risks, municipal obligors should consider taking appropriate steps in connection with any existing Libor-based contracts to resolve potential issues arising from Libor?s discontinuance as soon as practicable."

For new contracts, the SEC advises using an alternative reference rate, or if Libor usage is continued, to include fallback language published by the Alternative Reference Rates Committee or the International Swaps and Derivatives Association (ISDA).

During Wednesday's GFOA Debt Committee meeting, Richard Li, public debt specialist for the City of Milwaukee, pointed out to Olsen that there are minors differences in the fallback language released by ARRC and ISDA.

"The differences potentially introduce basis risk if you have a hedge transaction," Li said.

"I don't know that the SEC has a view," responded Olsen. "I haven't spoken with anyone about it." Olsen said she would check on what the SEC's position might be.

By Brian Tumulty

BY SOURCEMEDIA | MUNICIPAL | 01/13/21 02:33 PM EST

SEC Settles Charges Against Municipal Underwriter for Unfair Practices and Misleading Advertising in Connection With its Distribution of New Issue

Securities: Ballard Spahr

Summary

The U.S. Securities and Exchange Commission (SEC) announced that it has settled charges against an underwriter, its owner, and chief compliance officer for violations of MSRB Rules G-21 on misleading advertising and G-17 on fair dealing.

The Upshot

According to the December 22, 2020, SEC Order implementing the settlement:

- During the period in question, the underwriter sold roughly 76 percent of the par value of its offerings to broker-dealers, rather than directly to investors, with 35 percent of the par value of those offerings sold to a single broker dealer—who then resold the bonds to investors at prices higher than the initial offering prices. According to the SEC, this practice conflicted with representations made by the underwriter to the issuers about its distribution capabilities.
- The SEC asserted that the underwriter's practice of using broker-dealers to resell underwritten bonds resulted in pricing that created profits for the broker-dealer intermediaries that would have been captured by the issuer had the bonds been sold directly to investors at those prices.
- MSRB rules, in and of themselves, do not prohibit an underwriter from selling new issue municipal securities to broker-dealers—but the SEC has articulated a position about these practices and the theoretical harm they could cause municipal issuers.

The Bottom Line

The SEC's use of fair dealing and advertising rules to promote regulatory goals that cannot be regulated directly should be noted by underwriters who sell new issue municipal securities to broker-dealers in order to manage their risk to capital, especially in volatile interest rate environments or where the demand for the issue is weak.

As a result of this Order, underwriters should review the materials they use to respond to issuer RFPs for underwriting services and their internet advertising content. Underwriters should also consider if and under what circumstances they should disclose to municipal issuers the SEC's views of the potential harm to issuers of the pricing dynamics described above.

While the Order effectively mandates additional Rule G-17 disclosures to municipal issuers about their distribution practices when they deviate from other representations, the SEC may be moving toward a view that underwriters should make these Rule G-17 disclosures even in the absence of contrary representations, if they are underwriting bonds for smaller inexperienced issuers who are not represented by municipal advisors in the pricing process. It is unclear whether the Order is a harbinger of increasing scrutiny by the SEC of underwriter pricing and distribution practices for issuers unrepresented by municipal advisors. The Order also articulates the SEC's views of the important role they feel a municipal advisor plays in assisting municipal issuers, especially smaller unsophisticated issuers, in pricing underwritten transactions.

FULL ALERT

The U.S. Securities and Exchange Commission (SEC) announced that it has settled charges against an underwriter, its owner, and chief compliance officer for violations of MSRB Rules G-17 and G-21. According to the December 22, 2020, SEC Order implementing the settlement, during the time period in question, the underwriter sold roughly 76 percent of the par value of its municipal securities to broker-dealers, rather than directly to investors, with 35 percent of the par value of those offerings sold to a single broker-dealer—who then resold the securities to investors at prices higher than the initial offering prices.

The SEC found that, notwithstanding this "regular practice," the underwriter at the same time represented on its website and in RFP responses to issuers that the underwriter had "an extensive customer base which would allow it to locate suitable investors for the bonds and sell the bonds at competitive interest rates" among other similar representations.

According to the Order, because underwriters must make truthful and accurate representations about their capacity and resources to perform their underwriting services and not misrepresent or omit material facts, the SEC found that the underwriter's practice was a violation of MSRB's Rule G-17 on fair dealing. The SEC also alleged that the underwriter violated MSRB's Rule G-21 on advertising because its website is considered a professional advertisement, and the statements about its distribution capabilities were false and misleading.

The Order described the SEC's position concerning the effects that these practices may have on issuers and the pricing of new issue municipal securities. According to the SEC, the underwriter's practice of using broker-dealers to resell underwritten municipal securities creates the risk that an issuer's securities would not be sold at competitive interest rates, because the broker-dealer's commission is added to the initial offering prices, resulting in higher prices and lower yields. Under this reasoning, if the underwriter has sold the municipal securities directly to investors at those same prices and yields, the issuer could potentially receive more in proceeds or realize lower yields. MSRB rules, in and of themselves, do not prohibit an underwriter from selling new issue municipal securities to broker-dealers.

Although the SEC may not have a direct path to eliminating the intermediary profits of broker-dealers in this context absent an unrelated rule violation—in this case alleging misleading advertising under MSRB Rules G-21 and fair dealing violations under G-17—the SEC has articulated a new position about these practices and the theoretical harm they could cause municipal issuers.

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by the Municipal Securities Regulation and Enforcement Group

January 14, 2021

SEC OMS Publishes Staff Statement on LIBOR Transition in the Muni Securities Market: NABL

Today the SEC Office of Municipal Securities published a staff statement on LIBOR Transition in the Municipal Securities Market.

If you interested in reading it, please find the statement posted here.

Thank you.

————————————
Jessica Giroux
National Association of Bond Lawyers
Washington, DC
(202) 503-3300

MSRB Announces Members of 2021 Board Advisory Groups.

Washington, DC – The Municipal Securities Rulemaking Board (MSRB) today announced the members of its continuing advisory groups. In all, 31 market professionals will share their municipal market and regulatory perspectives while serving on the MSRB’s Compliance and Municipal Fund Securities Advisory Groups.

“We are grateful that such a broad and diverse group of individuals volunteered their time and expertise to help inform the MSRB’s initiatives,” said Frank Fairman, Board member and chair of the 2021 Compliance Advisory Group.

Manju Ganeriwala, Board member and chair of the 2021 Municipal Fund Securities Advisory Group noted, “In forming the advisory groups, we take into consideration geographic diversity, gender and racial representation, and the incredible variety of firms and organizations that participate in the municipal securities market. We will continue striving to create advisory groups that are truly reflective of the market we serve."

Continue reading.

Date: January 15, 2021

Contact: Leah Szarek, Chief External Relations Officer
202-838-1500
lszarek@msrb.org

SEC Settles Charges Against Municipal Underwriter for Unfair Practices and Misleading Advertising in Connection With its Distribution of New Issue Securities: Ballard Spahr

Summary

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- The SEC asserted that the underwriter's practice of using broker-dealers to resell underwritten bonds resulted in pricing that created profits for the broker-dealer intermediaries that would have been captured by the issuer had the bonds been sold directly to investors at those prices.
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The Bottom Line

The SEC's use of fair dealing and advertising rules to promote regulatory goals that cannot be regulated directly should be noted by underwriters who sell new issue municipal securities to broker-dealers in order to manage their risk to capital, especially in volatile interest rate environments or where the demand for the issue is weak.

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The SEC found that, notwithstanding this "regular practice," the underwriter at the same time represented on its website and in RFP responses to issuers that the underwriter had "an extensive customer base which would allow it to locate suitable investors for the bonds and sell the bonds at competitive interest rates" among other similar representations.

According to the Order, because underwriters must make truthful and accurate representations about their capacity and resources to perform their underwriting services and not misrepresent or omit material facts, the SEC found that the underwriter's practice was a violation of MSRB's Rule G-17 on fair dealing. The SEC also alleged that the underwriter violated MSRB's Rule G-21 on advertising because its website is considered a professional advertisement, and the statements about its distribution capabilities were false and misleading.

The Order described the SEC's position concerning the effects that these practices may have on issuers and the pricing of new issue municipal securities. According to the SEC, the underwriter's practice of using broker-dealers to resell underwritten municipal securities creates the risk that an issuer's securities would not be sold at competitive interest rates, because the broker-dealer's commission is added to the initial offering prices, resulting in higher prices and lower yields. Under this reasoning, if the underwriter has sold the municipal securities directly to investors at those same prices and yields, the issuer could potentially receive more in proceeds or realize lower yields. MSRB rules, in and of themselves, do not prohibit an underwriter from selling new issue municipal securities to broker-dealers.

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January 15, 2021

[MSRB Input on Strategic Goals and Priorities.]

SUMMARY

SIFMA sent comments to the MSRB regarding their request for input on its strategic goals and priorities. SIFMA welcomes this opportunity for a constructive conversation on the direction of the MSRB, particularly at the start of Mark Kim's tenure as CEO and his outreach to various stakeholders. Below SIFMA provides high-level feedback on particular priorities identified by Mr. Kim as they relate to the MSRB's mission.

Read the letter.

ABA Offers Feedback on MSRB's Strategic Goals.

In response to a request from the Municipal Securities Rulemaking Board seeking industry input on its strategic goals, the American Bankers Association yesterday submitted a letter providing several recommendations. Among other things, the association said that MSRB should consider the various budgetary hurdles for banks when adopting new technology, adding that "ABA believes the evolution of technology and its costs will continue to be challenging for banks as the pace, magnitude, and implementation of regulation will prove to be resource-intensive."

Additionally, ABA recommend that MSRB prioritize transparency and flexibility in implementing regulations and supported a transition plan to return to a 15-member board. ABA also recommended MSRP work with industry when it beta-tests any potential new interface to the Electronic Municipal Market Access system that provides information about municipal bonds and bond prices.

ABA JOURNAL

JANUARY 12, 2021

MSRB Contribution Disclosure Requirements for Dealers and MAs.

Did you know that the MSRB requires dealers and MAs to disclose information in connection with contributions they make to officials of political parties, and bond ballot referendum committees?

Learn more about these disclosures.

SEC Adopts New Framework for Fund Valuation.

Read the Article.

Vedder Price PC | USA | 4 Jan 2021

NFMA 2021 Officers and Board Announced.

The NFMA is pleased to announce that Anne Ross, Principal Consultant, Muni Credit & Compliance Advisors, LLC, has been elected NFMA Chair for 2021. She succeeds Nicole Byrd, Senior Investment Professional at Nationwide Mutual Insurance, who served as 2020 NFMA Chair. Rachel Barkley, Senior Vice President at Loop Capital Markets, has been elected Vice Chair, and will also chair the Industry Practices Committee. Mark Capell, Managing Vice President and senior underwriter at BAM, will continue his role of Secretary and Education Chair. Elected Treasurer for 2021 – 2022 was Ron Mintz, Principal and Senior Municipal Investment Analyst in Vanguard's Investment Management Group. Together with Neene Jenkins Executive Director at JPM Chase Asset Management, Mr. Mintz will chair the NFMA's 2021 Annual Conference.

The 2021 Annual Conference will employ a virtual platform for 2021 and will be held on May 12 & 13. To view the full list of 2021 NFMA Board members, go to About Us/Governance.

Information on the 2021 Annual Conference will be released in coming weeks.

Outlook 2021: SEC to Focus on Price Transparency, Muni Advisors and Disclosure Enforcement.

The Securities and Exchange Commission's enforcement activity will have a strong focus on issuer disclosure, municipal advisors, and pay-to-play practices in 2021.

Despite changes not only in presidential administrations but a new SEC chair a new director of enforcement, sources expect the SEC to stay vigilant if not more intense in its enforcement actions.

"The core organizing principle is that we want to pursue, and we prioritize, cases where there is a clear risk of investor harm,? said LeeAnn Gaunt, chief of the SEC's Public Finance Abuse Unit. "We also consider it a key part of our mission to protect issuers, particularly small, infrequent issuers, from abusive practices by municipal advisors and broker-dealers."

In 2020, the SEC brought numerous cases against MAs and broker-dealers.

Prominently, the SEC continued a two-year crackdown of individuals and broker-dealers firms involved in “flipping” arrangements in 2020. Since 2018, there were multiple cases brought involving individuals and firms posing as retail investors to gain priority access to new-issue municipals. The bonds were then “flipped” for profit.

The SEC also charged a charter school in 2020 for misleading investors in a $7.6 billion municipal bond offering. In April, the SEC charged the CEO and director of finance of a public charter school with misleading investors.

“Investor protection is our mission and is always our primary focus,” Gaunt said. “Although new leadership does bring change, I think everyone appreciates the importance of the municipal securities market and supports enforcement where there are abuses in that market.”

In 2021, MA enforcement and issuer disclosure will continue to be active, Gaunt said. The SEC will be focused on fraud in primary offerings, especially with distressed issuers. The SEC is also concerned about muni advisors’ breaches of fiduciary duties, and staff prioritizes those cases, Gaunt said.

The SEC is also still seeing issues with firms and individuals providing municipal advice to issuers without registering as such, Gaunt said. In September, the SEC settled charges with consultant Irene Carroll after the regulator found she provided municipal bond advice to charter schools without registering as an MA.

The SEC will also focus on the lack of transparency and pricing of municipal securities, former SEC lawyers say.

“It all goes back to the idea, that equity security, like corporate stock and so forth, the staff has always believed and some commissioners that there is not the same liquid, robust market that regularly makes pricing available,” said Peter Chan, partner at Baker McKenzie and former SEC enforcement lawyer.

“The past year has shown that the SEC wants to use its enforcement power to address this concern,” Chan added. “There will be more to come.”

A new SEC chair will be chosen by President-elect Joe Biden this year and confirmed by the Senate. Former Chair Jay Clayton departed at the end of the year and t Director of Enforcement Stephanie Avakian also left. These moves are common as a new administration rolls in.

Changes in top seats will not change the aggressiveness of the SEC?s enforcement, and if anything will bring more intensity, Chan said.

“With the new administration with a Democrat president, the expectation is that enforcement will be at minimum just as aggressive if not more aggressive in activity and the level of focus and energy,” Chan said.

A Democratic administration also tends to lead with a view that the SEC should be more aggressive in overall enforcement and SEC chairs appointed by Republicans historically want to protect the market, Chan said.

Changes in administration don’t mean much to the muni market specifically.

“These changes in the administration don’t necessarily mean a big shift in policy – at least in the muni world it’s a little more steady,” said Dave Sanchez, senior counsel at Norton Rose Fulbright. “Ultimately it is a positive that folks can have a little more security of where the SEC is likely to go and where their focus will be because it’s probably not going to dramatically change.”

A new SEC chair also won?t have a material impact on muni enforcement. Sanchez said.

“You’re going to see the priorities that have been identified by the Public Finance Abuse unit, as well as the Office of Municipal Securities, continue to be prominent without having any external interference,” Sanchez said.

Sanchez expects that muni enforcement will be focused on the transition to LIBOR, disclosure issues, issues related to COVID-19 disclosures and cybersecurity.

“It’s the big general themes, but there might be some more specific focus on current topics that inform those themes,” Sanchez said.

Other sources said it was difficult to determine what role the next SEC chair would have.

“Clayton was a corporate guy but was definitely focused on disclosure, but it?s hard to say,” said Rebecca Lawrence, senior counsel at Ballard Spahr.

Before joining the SEC, Clayton was a partner at Sullivan & Cromwell LLP where he was a member of the firm’s Management Committee and co-head of the firm’s corporate practice.

Whoever is in charge next though will be focused on more timely financial disclosure from issuers. Clayton keenly focused on that issue as chair demanding more timely and interim information from states and local governments. That issue has been ongoing for the past few decades.

Into 2021, the SEC is likely to keep an eye on MA enforcement since it is still a relatively newly-regulated group, Lawrence said. The Dodd-Frank Act of 2010 subjected non-dealer MAs for the first time to a federal regulatory regime and required all MAs to have a fiduciary duty to put issuers? interests before their own.

As for broker-dealers, the SEC may focus on enforcing Regulation Best Interest, Lawrence added. Reg BI strengthens the broker-dealer standard of conduct beyond existing suitability obligations and makes it clear that a broker-dealer may not put its financial interest ahead of a retail investor. It also requires broker-dealers and investment advisers to state clearly facts about their relationship with their customers, including financial incentives. That rule went into effect during the summer of 2020.

By Sarah Wynn

BY SOURCEMEDIA | MUNICIPAL | 11:38 AM EST

SEC Action on Misleading COVID-19 Disclosures: Implications for the Municipal Market - Ballard Spahr

Summary

The U.S. Securities and Exchange Commission (SEC) announced earlier this month it settled charges against a corporate issuer of registered securities for misleading disclosures about the impact of the COVID-19 pandemic on its business operations and financial condition in connection with its required Form 8-K filings.

The Upshot

- The SEC alleged the company's Forms 8-K were materially false and misleading because in the context of a press release attached to a Form 8-K filing that said its restaurants were "operating sustainably," the company failed to disclose financial hardships.
- While municipal issuers are not subject to required Form 8-K filings, the SEC has strongly urged the municipal market to provide voluntary disclosures to Electronic Municipal Market Access (EMMA) in the light of COVID-19.
- The settlement is the SEC's first enforcement action against a public company for misleading COVID-19 disclosures.

The Bottom Line

The Order—as well as other prior SEC actions—signifies the SEC may not hesitate to scrutinize issuers' pandemic-related disclosures, which could have implications for municipal issuers.

FULL ALERT

The U.S. Securities and Exchange Commission (SEC) announced earlier this month it settled charges against a corporate issuer of registered securities for misleading disclosures about the impact of the COVID-19 pandemic on its business operations and financial condition in connection with its required Form 8-K filings (the Order).

The Order, as well as other prior SEC actions, signifies the SEC may not hesitate to scrutinize issuers' pandemic-related disclosures, which could have implications for municipal issuers.

In the Order, the SEC alleged that the company violated Section 13(a) of the Exchange Act and Rules 13a-11 and 12b-20 thereunder, which collectively require an issuer of a registered security to file accurate reports to the Commission on Form 8-K that contain material information necessary to make the required statements made in the reports not misleading.

The SEC alleged that in March 2020 the company's Forms 8-K were materially false and misleading because in the context of a press release attached to a Form 8-K filing that said its restaurants were "operating sustainably," the company failed to disclose the following:

- A letter the company sent to each of its restaurant landlords stating that the company was not going to pay rent for April 2020.
- The company was losing approximately $6 million in cash per week.
- It had only approximately 16 weeks of cash remaining.

In a press release accompanying the Order, the SEC included a reminder about the Corporate Issuer Statement of April 8, 2020, on the importance of disclosure. See our 2020 Mid-Year Newsletter for a recap of SEC statements and disclosure guidance related to COVID-19 for municipal issuers and market participants.

While municipal issuers are not subject to required Form 8-K filings, the SEC has strongly urged the municipal market to provide voluntary disclosures to Electronic Municipal Market Access (EMMA) in light of COVID-19.

SEC Chairman Clayton and Rebecca Olsen, Director of the Office of Municipal Securities, issued a public statement (Public Statement) on May 4, 2020, encouraging municipal issuers and conduit borrowers to voluntarily disclose future prospects regarding financial and operating status in light of the effects of, and economic and operational uncertainties created by, COVID-19. The Public Statement set forth examples of types of COVID-19 related disclosures Clayton and Olsen believe would be most beneficial for investors and the marketplace.

As an acknowledgement of the potential exposure municipal issuers and conduit borrowers face in making statements to the financial markets, Clayton and Olsen said in the Public Statement that they would not expect good faith efforts to provide "appropriately framed" current and forward looking information would be second guessed by the SEC. See our white paper on how to appropriately frame forward looking statements.

However, the omission of negative material facts such as those described in the Order presents a clear path to SEC scrutiny, especially in the context of another statement in a press release that the company was operating sustainably. The same set of facts outside a COVID-19 situation could be problematic—in both a primary offering document or a voluntary disclosure, regardless of the subject matter of the disclosure.

Ballard Spahr LLP

by the Municipal Securities Regulation and Enforcement Group

Rebecca Lawrence & Teri Guarnaccia

December 30, 2020

Applications Open for GFOA Executive Board.

GFOA's Executive Board Nominating Committee is seeking candidates to fill five at-large positions and the position of president-elect for GFOA. All candidates must be active GFOA members and would serve three-year terms beginning in June 2021. Please apply online using the link below by February 5, 2021.

APPLY

MSRB Soliciting Applications for Four Positions On Its Governing Board.

The MSRB is soliciting applications for four positions on its governing Board.

Learn more about the application process and how Board members set regulatory policy, authorize rulemaking, and oversee market transparency systems and operations.

SEC Does Not Plan to Extend TCE.

Major Advocacy Win for BDA

Following an extensive advocacy campaign, which included nearly a dozen meetings and multiple letters in opposition, the BDA has today learned that the SEC **does not plan to extend the Temporary Conditional Exemption for MA's.**

In a letter to Representative French Hill (R-AR), SEC Chair Jay Clayton, while explaining the reasoning for the original implementation of the Order stated, *"At this time, I do not expect the Commission to extend this temporary relief."*

The letter can be viewed here.

The response comes after the Congressman, working with the BDA, wrote the Commission in opposition of the TCE and questioned the Chairman during a recent House Financial Services Committee Hearing.

****All BDA Advocacy Against Exemption Can be Viewed Here**

Since learning of the initial PFM letter and the follow-up letter from NAMA to the SEC, the BDA has made this our top priority and taken many steps in order to combat the misinformation represented. BDA conducted more in-person meetings and filed more letters to the SEC than any other group.

The result was exemptive relief that was dramatically pared back from the SEC's original proposal in October 2019 and one that remained temporary.

Bond Dealers of America

December 22, 2020

Bloomington Firm Faces SEC Penalties Over Municipal Debt Practices.

A Bloomington investment banking firm and its owner will pay $200,000 in fines for not telling its municipal bond clients about business practices that ultimately reduced the proceeds from their offerings.

The Securities and Exchange Commission on Wednesday announced settled charges against First Midstate Inc., based in downtown Bloomington, and its owner Paul Brown.

The SEC says First Midstate falsely told clients that it had an extensive customer list that would allow it to sell bonds to investors at competitive interest rates. In reality, First Midstate had a limited customer base, and it sold many of the offerings it underwrote to other broker-dealers, not to investors, the SEC said. The purchasing broker-dealer then marked up the bonds and resold them to investors at higher prices—and corresponding lower yields, according to the SEC.

The SEC points to 101 offerings, totaling $198 million, that were sold off to a single broker-dealer between 2014 and 2018. Had First Midstate sold those bonds directly to investors at those more competitive prices, about $1.4 million could have flowed back to issuers as an increase in bond proceeds, the SEC said. Instead, that $1.4 million became profit for the broker-dealers.

In one example from the SEC order, the commission said Brown and Midstate facilitated a $9.47 million bond issue with a First Midstate fee of $283,153 (2.99% of the PAR value of the issue). Brown then resold the bonds to a broker within 22 minutes. That dealer made another $66,638 in fees after marking up the interest on the bonds and selling them. The SEC said the bond issuer did not know the second fee was likely given First Midstate's business practices.

First Midstate did not disclose to customers that its practice was to sell many of the bonds it underwrote to broker-dealers during the public offering, if it did not receive orders from investors, the SEC said. The firm did not disclose that this practice presented a risk to competitive pricing for their bond.

The SEC also noted that since all but one of Brown and Midstate's clients in the investigation were too small to have a separate bond advisor, the firm had an additional obligation to educate the municipalities on the complete terms of transactions.

In the settled charges announced Wednesday, First Midstate and Brown do not admit or deny the SEC's findings. But they have agreed to the order finding that they willfully violated the fair dealing and advertising provisions of federal securities law. In addition to the $200,000 in civil penalties, First Midstate is also required to hire an independent compliance consultant.

The SEC announcement and order do not identify the impacted clients; First Midstate's municipal clients are primarily Illinois school districts, SEC records show. Municipalities often raise capital by issuing bonds, or debt, that are indirectly sold to the public through an underwriter.

A message left with First Midstate was not immediately returned Wednesday.

WGLT.ORG

By RYAN DENHAM | DEC 23, 2020

SEC Proposes Amendments to Reg ATS for Government Securities ATSs.

The Securities and Exchange Commission (SEC) proposed to amend Regulation ATS under the Securities Exchange Act of 1934 for alternative trading systems (ATSs) that trade government securities or repurchase and reverse repurchase agreements on government securities (Government Securities ATS). The SEC proposed to eliminate the exemption from compliance with Regulation ATS for Government Securities ATSs, and to require such ATSs, among other things, to

- Disclose information about their manner of operations and the ATS-related activities of the registered broker-dealer or government securities broker or government securities dealer that operates the ATS and its affiliates on new Form ATS-G;
- Comply with the Fair Access Rule under Rule 301(b)(5) of Regulation ATS if the ATS meets certain volume thresholds in US Treasury Securities or in a debt security issued or guaranteed by a US executive agency or a government-sponsored enterprise (Agency Securities); and
- Comply with Regulation Systems Compliance and Integrity (Reg SCI) if the ATS meets certain volume thresholds in US Treasury Securities or Agency Securities.

The SEC also issued a concept release on the regulatory framework for electronic platforms that trade corporate debt and municipal securities. The SEC requested comment on the proposed amendments to Regulation ATS and the concept release within 60 days after publication of the proposal in the Federal Register.

Continue reading.

Wilmer Cutler Pickering Hale and Dorr LLP – Andre E. Owens, Bruce H. Newman and Cherie Weldon

December 17 2020

MSRB Seeking Applications for Governing Board.

The MSRB is seeking applications for four positions on its governing Board.

Listen to what a former public representative enjoyed about her tenure.

Joint Letter on Alternative Reference Rates Committee's Legislative Proposal.

SUMMARY

We are writing to make you aware of an issue that, if left unaddressed, could have significant consequences not only for the State of New York and its residents, but for U.S. and global markets. Avoiding further unnecessary disruptions will be especially important as the economy seeks to recover from the damage done from the pandemic. As you are likely aware, the regulator of LIBOR, an interest rate benchmark used in an estimated $200 trillion of financial transactions, has stated that LIBOR will end and warned that market participants should prepare for the risk that it may be discontinued as soon as the end of 2021. However, many existing contracts either do not address a permanent end to LIBOR or have ambiguous fallback language that could dramatically alter the economics of hundreds of thousands of contracts.

This legal uncertainty could create complex problems for parties or courts to sort out, and create great uncertainty in financial markets. Many of the financial products and agreements that reference LIBOR are governed by New York law. It is because of this, and New York's critical role in financial markets, that we urge your consideration of the Alternative Reference Rates Committee's legislative proposal.

Read the Letter.

SIFMA Statement on Transition From LIBOR to Alternative Rates and ARRC Model Law for New York State.

New York, NY, December 16, 2020 – SIFMA today issued the following statement from SIFMA president and CEO Kenneth E. Bentsen, Jr. on the transition from LIBOR to alternative rates, in support of the letter from the ARRC on its model law for New York State:

“The transition from LIBOR to alternative rates is a top priority for the financial services industry. SIFMA supports market, legislative and regulatory efforts to ensure a smooth transition, while avoiding market disruption and legal uncertainty. We continue to work as part of the Alternative Reference Rate Committee on issues such as resolution of legacy transactions, development of a term rate, and socialization in the cash markets. Notably, the ARRC developed a model law for New York to help transition ‘tough legacy’ contracts that are difficult or practically impossible to amend, which SIFMA fully supports and urges New York to pass.

“SIFMA is also discussing the issue with Congress including possible federal legislation modeled on the NY law while continuing to advocate for the passage of NY state legislation. Notwithstanding those efforts, we continue to advocate for transition to new reference rates such as SOFR consistent with the end 2021 timeline, and the best practice recommendation of the ARRC. There is much to be done in that window, and regulators have made clear that the usage of LIBOR in new transactions needs to end next year.”

BDA 2021 Policy Focus.

The BDA is the established advocate and thought leader in Washington, DC for the US bond markets. No other group is as focused or aggressive and below is an example of the BDA’s bond market policy focus as we roll into 2021

For more information please visit www.bdamerica.org or contact us at 202-204-7900.

2021 Federal Policy Focus:

- Promote municipal bonds through federal infrastructure legislation
- Ensure the SEC does not resurrect the TCE for MAs
- Corporate syndicate settlement and SEC net capital rule
- BondMarkets 2020 – Comprehensive recommendations for regulation of the US bond markets
- SEC re-evaluation of the MA Rule
- Remote work and review of FINRA and MSRB rules
- Maintain opposition to TRACE Pilot Program as proposed by FIMSAC
- FINRA Rule 4210, including BDA, approved amendments
- Press the MSRB to reform its fee structure and budget

We look forward to representing you in the new year!

Bond Dealers of America

December 16, 2020

IRS Revenue Procedure 2020-44: Floating Rate Fallback Flexibility from the Feds - McGuire Woods

The IRS recently released Revenue Procedure 2020-44 ("**Rev. Proc. 2020-44**") which provides helpful relief to taxpayers by providing that if a contract referencing an IBOR is modified to incorporate specific ISDA or AARC fallback language for the replacement of IBORs, such modification will not cause certain adverse tax consequences, such as exchange treatment under Section 1001 of the Tax Code, or the legging out or termination of integrated transactions under Treasury Regulation Sections 1.1275-6, 1.988-5(c) or 1.148-4(h).

This is particularly significant for tax-exempt debt instruments with a LIBOR based interest rate that may otherwise be treated as "reissued" for federal income tax purposes as a result of the addition of such language, and any derivative transactions (such as interest rate swaps) that are treated as "integrated" with a debt instrument for tax purposes.

As we wrote about here, to support the transition from IBORs the AARC published fallback language for inclusion in the terms of certain newly issued and outstanding cash products, including floating rate notes, bilateral business loans, syndicated loans, securitizations, adjustable rate mortgages, and variable rate private student loans (the "**AARC Fallbacks**"). The fallback language generally provides a mechanism for determining the replacement benchmark rate that supplants the current benchmark rate.

Likewise, on October 9, 2020 ISDA posted its Supplement number 70 to the 2006 ISDA Definitions (the "**ISDA Supplement**") to facilitate the inclusion of new IBOR transition fallback provisions in derivative transactions entered into on or after January 25, 2021, and its final ISDA IBOR Fallbacks Protocol to facilitate adoption of the ISDA Supplement by parties to legacy derivative contracts (the "**ISDA Protocol**"). An "**ISDA Fallback**" is the set of terms provided in any one of sections one through six in the Attachment to the ISDA Protocol.

On October 9, 2019, the Treasury Department and the IRS published proposed regulations on the tax consequences of modifying debt instruments, derivative contracts, and other contracts to replace IBORs or add fallback provisions to IBORs (the "**Proposed Regulations**"). The ARRC later recommended guidance on the tax consequences of modifying a contract as provided in the ISDA Protocol and AARC Fallbacks and the Treasury Department and IRS have accepted those recommendations in issuing the interim guidance in Rev. Proc. 2020-44.

Under Rev. Proc. 2020-44 certain reasonably necessary and technical deviations from the specific terms of an AARC Fallback or an ISDA Fallback are permissible.

Rev. Proc. 2020-44 is effective for modifications to contracts occurring on or after October 9, 2020 and before January 1, 2023. A taxpayer may, however, rely on Rev. Proc. 2020-44 for modifications occurring before October 9, 2020.

While this guidance is very helpful in providing taxpayers with certainty upon adding fallback language to a new or existing contract, it doesn't absolve the parties from analyzing the tax consequences of an actual transition from an IBOR to a new rate. At that point taxpayers will need to look to the guidance in the Proposed Regulations (or whatever form the guidance is in at that point) to determine the tax consequences. The Proposed Regulations currently require a new rate to be any one of several rates that are listed in the Proposed Regulations (including SOFR) and if an AARC Fallback or ISDA Fallback results in a new rate that is not on the list there could be adverse tax results.

By Robert A. Kaplan, Emery B. McRill & Kay McNab on December 8, 2020

Fitch: New US Dollar Libor Deadline Doesn't Guarantee a Smooth Transition

Fitch Ratings-New York/London-01 December 2020: Pushing the Libor transition deadline for the U.S. dollar (USD) market back 18 months would lessen the risk of disorderly outcomes at YE21 but using this extra time productively is the key to a smooth transition, Fitch Ratings says. Primary markets have yet to shift to alternative indices, regulators and legislators might need to facilitate orderly transition for hard-to-fix legacy contracts and liquidity needs to develop in derivatives based on the Secured Overnight Financing Rate (SOFR).

ICE Benchmark Administration Limited (IBA) on Monday announced a consultation that could see the cessation of the widely used one-, three-, six- and 12-month USD Libor reference delayed to end-June 2023. IBA will also consult on ceasing publication of one-week and two-month USD Libor at end-2021, in line with the original timetable.

Additional preparation time should avoid the potential operational and market disruption if all USD Libor settings ceased publication after 31 Dec 2021. As we have previously noted, delays in creating a robust SOFR-based derivatives market and the failure to develop a SOFR term rate sufficiently far in advance of cessation could materially increase risks to financial institutions arising from transition, while legacy Libor exposure is significant, particularly in structured finance.

The IBA consultation appears part of a coordinated effort by regulators to avoid such disruption. The UK Financial Conduct Authority (FCA), which regulates IBA as Libor's administrator, and the Federal Reserve Board (the Fed) both welcomed the prospect of 'a clear end-date' for USD Libor that left enough time to deal with legacy contracts where amending fallback language remains difficult, partly by reducing the number of affected contracts as most of these would mature before cessation. The backing of U.S. and UK regulators illustrates the magnitude of the transition challenges facing USD market participants.

Addressing legacy contracts also depends on moving primary market activity from USD Libor to SOFR or other alternative indices. SOFR adoption has been uneven and lagged other markets (sterling issuance largely references the Sterling Overnight Index Average), although most recent USD primary market issuance has included Alternative Reference Rates Committee (ARRC) fallback language, which will make the process of switching to SOFR in the future less challenging.

Delaying USD Libor cessation would allow more time for liquidity to develop in the SOFR-based derivatives market that remains a fraction of size of the interest rate derivatives market referencing Libor. This could support ARRC's efforts to build a term reference rate by the middle of 2021, facilitating more primary market issuance referencing SOFR. ISDA has published a protocol to include fallbacks in legacy derivative contracts referencing Libor. A delay would give market participants additional time to make the necessary amendments (adoption is voluntary). It would also leave more time to enact possible state or federal legislation to reduce litigation and operational risks from legacy contracts.

However, an extension would not automatically mean a smooth transition in mid-2023. We believe the slower shift to using SOFR as the benchmark rate for newly originated dollar cash products has reflected a ‘wait-and-see’ approach from some market participants, as well as SOFR’s lack of credit spread and term structure. Proactively embracing workable solutions would reduce, rather than simply delay, disruption.

The ‘wait-and-see’ approach also reflects a less forceful approach by U.S. banking regulators relative to their UK counterparts, particularly in the transition’s early stages, although U.S. regulators have increased efforts to make sure risks are addressed. The Fed, Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation said in response to IBA’s announcement that they ‘encourage’ banks to stop using Libor in new contracts as soon as possible and no later than end-2021.

SEC Updates Framework for Fund Fair Valuation Practices: Ropes & Gray

On December 3, 2020, the SEC issued a release adopting Rule 2a-5 (the “Rule”) under the 1940 Act (the “Release”).1 The Rule is intended to “address valuation practices and the role of the board of directors with respect to the fair value of the investments of a registered investment company or business development company.” The Rule will permit a fund’s board to designate the fund’s primary investment adviser to perform the fund’s fair value determinations, which will be subject to board oversight and certain reporting and other requirements intended to ensure that the board receives the information it needs to oversee the investment adviser’s fair value determinations. Most notably:

- The Rule specifies the minimum requirements of a program for determining the fair value of fund investments in good faith for purposes of the 1940 Act.
- The Rule permits a fund’s board2 to formally designate the fund’s primary investment adviser as its “valuation designee” to perform fair value determinations for the fund.3
- If a fund’s investment adviser is designated as the board’s fair valuation designee, the Rule provides that the investment adviser will be subject to board oversight and detailed reporting, recordkeeping and other requirements intended to enhance the board’s oversight of the investment adviser’s fair value determinations.
- The Release rescinds certain previously issued fair valuation guidance, including guidance on the role of a fund’s board in determining the fair value of fund investments.
- The Rule defines the criteria for concluding that a market quotation is “readily available,” which is currently undefined under the 1940 Act or rules thereunder. The definition will apply ***for all*** 1940 Act purposes, including Rule 17a-7 transactions. As a result, depending on further guidance from the SEC regarding the status of various no-action letters and/or potential revisions to Rule 17a-7, Rule ***17a-7 may no longer be available*** for cross trades in most fixed income securities and other securities without “readily available market quotations” as defined in the Rule beginning no later than the compliance date.

The Rule reflects some modifications from the April 2020 proposing release (the “proposing release”), largely to address issues raised regarding more prescriptive elements of the initial proposal. We have noted changes from the proposing release in the footnotes to this Alert.

SUMMARY OF THE RULE

Requirements to determine fair values in good faith. The Rule provides that determining the fair value of a fund's portfolio investments in good faith requires:

1. Periodically assessing any material risks associated with fair value determinations, including material conflicts of interest, and managing those identified valuation risks.
2. Establishing and applying fair value methodologies by performing each of the following, taking into account the fund's valuation risks (a) selecting and applying in a consistent manner an appropriate methodology for determining (and calculating) the fair value of fund investments, including specifying the key inputs and assumptions specific to each asset class or portfolio holding, (b) periodically reviewing the appropriateness and accuracy of the methodologies selected and making any necessary changes or adjustments thereto and (c) monitoring for circumstances that may necessitate the use of fair value. A selected methodology may be changed "provided [the new] methodology is equally or more representative of the fair value of fund investments."4
3. Testing the appropriateness and accuracy of the fair value methodologies that have been selected, including identifying the testing methods to be used and the minimum frequency with which such testing methods are to be used.
4. Overseeing and evaluating any pricing services used, including establishing the process for approving, monitoring and evaluating each pricing service provider and initiating price challenges.5

Valuation designee. A fund's board may choose to designate the fund's primary investment adviser as its "valuation designee" to perform the fair value determinations of any or all fund investments by carrying out all of the functions required in items 1–4 above, subject to the board's oversight.6 The definition of valuation designee expressly excludes a fund's sub-adviser.

Oversight and reporting. If a fund's board designates the fund's investment adviser as its valuation designee, the Rule requires the board to oversee the investment adviser with respect to its fair value determinations, and the investment adviser is required to:

1. Inform the board in writing of the titles of the persons responsible for determining the fair value of the fund's portfolio holdings, including the particular functions for which they are responsible and any material changes to the roles or functions of these persons.
2. Reasonably segregate fair valuations from the fund's portfolio management "such that the portfolio manager(s) may not determine, or effectively determine by exerting substantial influence on, the fair values ascribed to portfolio investments."7
3. At least quarterly, provide the board in writing with any reports or materials requested by the board related to the fair value of the fund's investments or the investment adviser's process for fair valuing fund investments, as well as a summary or description of material fair value matters that occurred in the prior quarter, including: (a) any material changes in the assessment and management of valuation risks, including material changes in conflicts of interest of the investment adviser (and any other service provider), (b) any material changes to, or material deviations from, the fair value methodologies employed and (c) any material changes to the process for selecting and overseeing pricing services, as well as any material events related to the investment adviser's oversight of pricing services.
4. At least annually, provide the board in writing with an assessment of the adequacy and effectiveness of the investment adviser's process for determining the fair value of the designated portfolio of investments, including (a) a summary of the results of the testing of fair value methodologies employed and (b) an assessment of the adequacy of resources allocated to the process for determining the fair value of the fund's investments, including any material changes

to the roles or functions of the persons responsible for determining fair value.8

5. Notify the board of the occurrence of matters that materially affect the fair value of the fund's investments, including any significant deficiency or material weakness in the effectiveness of the investment adviser's fair value determination process or material errors in the calculation of a fund's NAV (each a "material matter"), within five business days after the adviser becomes aware of the material matter (or shorter period determined by the board), along with timely follow-on reporting as the board may determine to be appropriate.9 According to the Release, this "standard is similar to that of 'material compliance matter' found in rule 38a-1."10

Recordkeeping. The Release simultaneously adopts companion Rule 31a-4 regarding records related to fair value determinations.11 Rule 31a-4 requires an investment adviser to maintain "appropriate" documentation to support its fair value determinations, as well as the various periodic reports to a fund's board described above.12 Existing Rule 31a-2 already requires a fund to maintain "all schedules evidencing and supporting each computation of net asset value of the investment company shares." However, the Release states that "[w]hile some records currently required to be maintained . . . may be the appropriate documentation to support fair value determinations in some circumstances, they may not always be sufficient to meet that standard." The Release also acknowledged that a separate recordkeeping rule would ensure that a recordkeeping failure does not mean that a board has not fair valued in good faith.

Definition of "readily available." Under Section 2(a)(41) of the 1940 Act, if a market quotation is "readily available" for a portfolio holding, it must be valued at its market value. If market quotations are not readily available, a holding's value is its "fair value as determined in good faith by the board." However, the term "readily available" was not previously defined in the 1940 Act or rules thereunder. To fill this gap, the Rule provides:

> For purposes of section 2(a)(41) . . . a market quotation is readily available only when that quotation is a quoted price (unadjusted) in active markets for identical investments that the fund can access at the measurement date, provided that a quotation will not be readily available if it is not reliable.

The Release notes that ASC Topic 820 defines level 1 inputs as "[q]uoted prices (unadjusted) in active markets for identical assets . . . that the reporting entity can access at the measurement date" and states that the Rule's definition

> is consistent with the definition of a level 1 input in the fair value hierarchy outlined in U.S. GAAP. Thus, under the final definition, a security will be considered to have readily available market quotations if its value is determined solely by reference to these level 1 inputs. Fair value, as defined in the Act and further defined in rule 2a-5, therefore must be used in all other circumstances.

Thus, for purposes of the Rule, for a quotation to be "readily available," a security's value must be determined solely by reference to level 1 inputs under U.S. GAAP. The Release specifically states that evaluated prices, indications of interest and accommodation quotes would not be "readily available market quotations" for purposes of the Rule. The Release notes that whether a market quotation would be "unreliable" is also informed by U.S. GAAP, noting that "we will generally presume that a quote would be unreliable under [the Rule] where it would require adjustment under U.S. GAAP or where U.S. GAAP would require consideration of additional inputs in determining the value of the security."

Additionally, the Release states that the Rule's definition of readily available market quotations will apply in all contexts under the 1940 Act and the rules thereunder, including Rule 17a-7. The Release recognizes that, as a result, certain transactions that could formerly have been effected in reliance on Rule 17a-7 may no longer be deemed to have readily available market quotations and, therefore, may not be eligible for trading in reliance on Rule 17a-7. The Release cites certain SEC staff no-action letters that permitted transactions involving municipal fixed-income securities in reliance on Rule 17a-7 where market quotations were not readily available and the transaction was effected at a price provided by an independent pricing service.13 The Release goes on to state that the SEC staff is "reviewing these letters to determine whether these letters, or portions thereof, should be withdrawn [and] [s]eparately, consideration of potential revisions to rule 17a-7 is on the rulemaking agenda. We welcome input from the public as we undertake our consideration of rule 17a-7."

Unit investment trusts. The Rule provides that, if the initial deposit of portfolio securities into a UIT occurs after the Rule's effective date, the UIT's trustee or depositor is responsible for carrying out the requirements to determine fair values in good faith (i.e., items 1–4 above). If the initial deposit occurs before the Rule's effective date, and an entity other than the fund's trustee or depositor has been designated to carry out the fair value determinations, that entity must carry out those requirements.

Board oversight. The Release provides extensive guidance on board oversight of the fair value determination process where it designates a valuation designee under the Rule. Following are selected excerpts:

> Where the board designates a valuation designee to perform fair value determinations under the final rule, the board will fulfill its continuing statutory obligations through active oversight of the valuation designee's performance of fair value determinations and compliance with the other requirements of the final rule.
>
> Boards should approach their oversight of the performance of fair value determinations by the valuation designee of the fund with a skeptical and objective view that takes account of the fund's particular valuation risks, including with respect to conflicts, the appropriateness of the fair value determination process, and the skill and resources devoted to it.
>
> The board should view oversight as an iterative process and seek to identify potential issues and opportunities to improve the fund's fair value processes.
>
> We expect that boards engaged in the process would use the appropriate level of scrutiny based on the fund's valuation risk, including the extent to which the fair value of the fund's investments depend on subjective inputs. . . . As the level of subjectivity increases and the inputs and assumptions used to determine fair value move away from more objective measures, we expect that the board's level of scrutiny would increase correspondingly.
>
> [C]onsistent with their obligations under the Act and as fiduciaries, boards should seek to identify potential conflicts of interest, monitor such conflicts, and take reasonable steps to manage such conflicts.
>
> Boards should probe the appropriateness of the valuation designee's fair value

> processes. In particular, boards should periodically review the financial resources, technology, staff, and expertise of the valuation designee, and the reasonableness of the valuation designee's reliance on other fund service providers, relating to valuation.
>
> Boards should also consider the type, content, and frequency of the reports they receive . . . While a board can reasonably rely on the information provided to it in summaries provided by the valuation designee and other service providers in conducting appropriate oversight, it is incumbent on the board to request and review such information as may be necessary to be informed of the valuation designee's process for determining the fair value of fund investments. Further, if a board becomes aware of material matters . . . we believe that in fulfilling its oversight duty the board must inquire about such matters and take reasonable steps to see that they are addressed.

EFFECTIVE AND COMPLIANCE DATES

Rules 2a-5 and 31a-4 become effective 60 days after publication of the Release in the Federal Register.14 The compliance date will be eighteen months following the effective date. The Release provides that funds will have the option of complying with the Rules before the compliance date once the Rules become effective. However, to promote regulatory consistency, the Release states that any fund that elects to rely on Rules 2a-5 and 31a-4 before the compliance date may rely only on those rules, and may not also rely on other SEC guidance and staff letters and other guidance that will be withdrawn or rescinded on the compliance date.

In addition, on the effective date, the SEC will rescind ASRs 113 and 118, various no-action letters and staff guidance identified in the Release, as well as the "Last paragraph of Section III.D.2.(a) and the entirety of Section III.D.2.(b) of the 2014 Money Market Fund Release"15 and "Valuation Guidance Frequently Asked Questions (FAQ 1 only)." The rescinded portions of the 2014 Money Market Fund Release and FAQ 1 contain the SEC and SEC staff's identical assertions that "a fund's board of directors has a non-delegable responsibility to determine whether an evaluated price provided by a pricing service, or some other price, constitutes a fair value for a fund's portfolio security."

OBSERVATIONS

Readily available market quotation definition. The Release states that the Rule's definition of readily available market quotations will apply in all contexts under the 1940 Act and the rules thereunder, including Rule 17a-7. As noted in the Release, "[f]or a fund to engage in a cross trade under Rule 17a-7, the security first must have a 'readily available market quotation' and then the transaction must meet the other conditions of that rule." As noted above, the Release also indicates that evaluated prices, indications of interest and accommodation quotes would not be "readily available market quotations" for purposes of the Rule. This suggests that – depending on further guidance from the SEC, including the results of the SEC's review of the line of no-action letters permitting transactions effected at prices provided by independent pricing services and any revisions to Rule 17a-7 – funds may no longer be able to effect cross trades in most fixed income securities in reliance on Rule 17a-7 beginning no later than the Rule's compliance date. This would have a major impact on the current cross trading practices of many fund complexes.

Separately, through a line of no-action letters,16 the SEC staff has permitted various affiliated persons, at least one of which is a fund, to effect in-kind transactions in which transferred securities are valued identically by the participants for purposes of determining their NAVs (such that neither participant experiences an artificial loss or gain simply due to different valuation procedures). The no-action letters did not exclude securities that were valued for NAV purposes based upon independent pricing services from being transferred in these transactions, and the industry has not interpreted the no-action letters as containing such an exclusion. It is not obvious why pricing service prices may be relied upon by funds in these affiliated transactions but not in Rule 17a-7 transactions.

Changes in selected methodology. The Rule provides that a fair valuation methodology may be changed "if a different methodology is equally or more representative of the fair value of fund investments." (Emphasis added). In some cases, it may be difficult to conclude with any certainty that a new method will be at least as representative of fair value as its predecessor. The wording of the Rule suggests that, if a new methodology proves inferior, the determinations based on the new methodology could be deemed a violation of the Rule. The Release draws on ASC Topic 820-10--5-25, which the SEC describes as "requiring consistent application of valuation techniques, but providing that a change in a valuation technique . . . is appropriate if the change results in a measurement that is equally or more representative of fair value." It is not clear whether a reasonable determination at the time a methodology is changed suffices and avoids ex post criticism and even strict liability.

Segregation of portfolio management personnel. The Release added text to the segregation requirement to clarify that the segregation of portfolio management staff is intended to prevent portfolio managers from exerting undue influence on the fair values ascribed to portfolio investments. Nonetheless, the SEC recognized in the Release that portfolio managers can participate "in the process of fair value determinations because of the unique insights that portfolio management may have regarding the value of fund holdings." Permitting portfolio management to participate in fair valuations, while assuring that that participation does not amount to substantial influence may be difficult, especially if judged in hindsight. This is may be an area where the industry will want to seek clarification from the SEC staff.

Significant deficiency or material weakness. In 2007, following a directive of the Sarbanes-Oxley Act, the SEC adopted a release in which it defined, for purposes of Regulation S-X, the terms "significant deficiency" and "material weakness." The Rule requires an investment adviser to notify a fund's board of the occurrence of matters that materially affect the fair value of the fund's investments, including any significant deficiency or material weakness in the effectiveness of the investment adviser's fair value determination process ("material matter," which the Release states is a standard "similar to that of 'material compliance matter' found in rule 38a-1"), and the Release notes that material matters under the Rule "would generally include, for example, material weaknesses and significant deficiencies as defined in [Regulation S-X] that are related to fair value determinations."

Both defined terms in Regulation S-X concern internal controls over financial reporting and underlie Rules 30a-2 and 30a-3 under the 1940 Act. However, it remains unclear how accounting rules, which apply in the context of preparing financial reports and to a discrete set of fund holdings at the end of a financial reporting period over a period of up to 60 days, translate to the daily calculations of the fair value of a significantly greater number of fund holdings over a much shorter time horizon.17 At a minimum, the expertise of individuals performing daily fair value determinations may differ from the expertise of individuals preparing financial reports and assuring compliance with Rules 30a-2 and 30a-3.

A requirement, not a safe harbor. While perhaps less prescriptive than the SEC's recent liquidity risk management and derivatives risk management rules, the Rule imposes a mandatory, minimum framework for fair valuations. Many commenters had recommended that the proposed rule be recast as a non-exclusive safe harbor or otherwise be reworked to provide greater flexibility but, in rejecting these recommendations, the Release notes that it was "important to establish a minimum and consistent framework for fair value practices across funds." While the Rule was unanimously approved by the SEC's commissioners, Commissioner Hester M. Peirce issued a statement observing that "[a]long with many commenters, I see value in allowing fund boards the freedom to tailor their valuation assessment processes to their funds' individual needs and circumstances by redrawing the provisions of rule 2a-5 as a non-exclusive safe harbor" and that "[t]he prescriptive nature of the rulemaking could stifle fund boards' and advisers' initiative and innovation."

Fair value policies and procedures. Although the Rule omits the specific provisions in the proposing release that would have separately required that a fund adopt written policies and procedures addressing the determination of fair value, funds and investment advisers will still need to consider changes to existing fair value polices and procedures that are reasonably designed to prevent violation of Rules 2a-5 and 31a-4. The Release notes that, because Rules 2a-4 and 31a-4 are new rules under the 1940 Act with new fair value determination requirements, and given the intrinsic relationship of the Rules to the board's own statutory functions relating to valuation, the fair value policies and procedures must be approved by the board pursuant to Rule 38a-1.

Determining when a market quotation is no longer reliable. As adopted, the Rule changed a requirement in the proposing release to the effect that a fair valuation program must include "criteria for determining when market quotations are no longer reliable." To explain this change, the Release states that "to satisfy the requirement to monitor for circumstances that may necessitate the use of fair value . . . boards and valuation designees would have to take into account the circumstances that may cause market quotations to be no longer reliable." In addition, the Release notes that requiring, in advance, "a list of specific criteria for determining when market quotations may no longer be reliable could limit the board's or valuation designee's flexibility."

* * *

If you would like to learn more about the issues in this Alert, please contact your usual Ropes & Gray attorney contacts.

1. The Release also includes new Rule 31a-4 under the 1940 Act, which addresses recordkeeping requirements relating to the Rule.
2. The Rule provides that "board" means either the fund's entire board of directors/trustees or a designated committee composed of a majority of directors/trustees who are not interested persons of the fund.
3. In a change from the proposing release, a fund's board may not assign fair value determinations to one or more sub-advisers. As adopted, the Rule permits a board to designate, as its "valuation designee," (i) the fund's adviser or (ii) if the fund does not have an investment adviser, an officer or officers of the fund. The definition of valuation designee expressly excludes a fund's sub-adviser. The second option is available only to an internally managed fund. In this Alert, we assume that a board's valuation designee will be the fund's primary investment adviser. Unit investment trusts ("UITs"), which do not have a board or an investment adviser, normally rely on the trustee or depositor to perform fair value functions and, as discussed below, are treated separately under the Rule.
4. This is a change from the proposing release, which did not include the proviso. In another change from the proposing release, the Release omits a requirement that would have required the board or investment adviser to consider the applicability of the selected fair value methodologies to types of investments a fund does not currently own but in which the fund intends to invest.
5. This is a change from the proposing release, which would have required a fund to adopt and implement written policies and procedures addressing the determination of the fair value of fund

investments that are reasonably designed to achieve compliance with the requirements described in items (1)–(4). The Rule does not include this requirement. In the Release, the SEC recognized that, with the adoption of the Rules 2a-5 and 31a-4, Rule 38a-1 would require the adoption and implementation of written policies and procedures reasonably designed to prevent violations of the Rule's requirements.

6. The Rule provides that a board may "designate" a valuation designee (to perform fair value determinations), which is a change from the proposing release's use of the word "assign." In the Release, the SEC stated that "[s]ome commenters believed that the term 'assign' could suggest that the board has completely delegated the entire valuation function and related obligations to the adviser." For internally managed funds, which do not have an investment adviser, the definition of valuation designee permits an officer or officers of the fund to be the valuation designee. In this Alert, we assume that a board's valuation designee will be the fund's primary investment adviser.
7. In a change from the proposing release, the Release added the quoted text because the Release simultaneously deleted "process of making," which preceded "fair market valuations." In the Release, the SEC recognized that portfolio managers may have "unique insights . . . regarding the value of fund holdings" and, therefore, limited the segregation requirement to focus on undue influence. The Release indicates that ascribing fair values to portfolio investments based solely on information provided by the portfolio manager would not satisfy the segregation requirement.
8. The Rule requires that these items be reported annually to a board. This is a change from the proposing release, which would have required quarterly reports of these items. In another change from the proposing release, the Rule clarifies that the annual assessment may contain a summary of testing results and removes a requirement, which appeared in the proposing release, to report service provider changes or price overrides as per se material events related to the investment adviser's oversight of pricing services.
9. This is a change from the proposing release, which specified a maximum of three business days instead of five. The Release acknowledges that the materiality of some matters may not be immediately apparent. The Release provides that the valuation designee should promptly determine the materiality of matters it identifies consistent with its fiduciary duties and then notify the board within five business days after determining that the matter is material. If a valuation designee has not been able to determine a valuation matter's materiality after 20 business days of becoming aware of the matter, the Release indicates that the SEC would expect the designee to then notify the board of its ongoing evaluation of the matter within five business days.
10. The Release states that material matters in this context would generally be matters about which a fund board "would reasonably need to know in order to exercise appropriate oversight of the valuation designee's fair value determination process," including matters that "could have materially affected" the fair value of the fund's investments.
11. In a change from the proposing release, the Release does not specify the newly required records in the text of the Rule. Instead, the SEC adopted Rule 31a-4. If a fund's board does not designate a valuation designee, the fund is required to maintain the appropriate documentation to support its fair value determinations.
12. In another change from the proposing release, the Release states that appropriate documentation does not require detailed records relating to the specific methodologies that a pricing service applied nor the assumptions or inputs used by such pricing service. However, consistent with the proposing release, the Release states that "the requirement to maintain appropriate documentation to support fair value determinations should include documentation that would be sufficient for a third party, such as the [SEC] staff, not involved in the preparation of the fair value determinations to verify, but not fully recreate, the fair value determination."
13. See, *e.g.,* United Municipal Bond Fund, SEC No-Action Letter (pub. avail. Jan. 27, 1995) and

Federated Municipal Funds, SEC No-Action Letter (pub. avail. Nov. 20, 2006).
14. As of the date of this Alert, the Release has not been published in the Federal Register.
15. Money Market Fund Reform; Amendments to Form PF, Rel. No. IC-31166 (Jul. 23, 2014) ("2014 Money Market Fund Release").
16. See, *e.g.*, Signature Financial Group, Inc., SEC no-action letter (pub. avail. Dec. 28, 1999) and GE Institutional Funds, SEC no-action letter (pub. avail. Dec. 21, 2005).
17. A similar observation was made in the ABA Comment Letter, which was cited in the Release.

December 9 2020

Ropes & Gray LLP

Using EMMA to Identify Timing of Annual Financial Disclosures.

Why does the Submission Calculator on EMMA® not use the issuer's continuing disclosure agreement due date?

Learn that and more by watching our on-demand webinar, Using EMMA to Identify Timing of Annual Financial Disclosures.

What US Municipal Securities Issuers Should Know About LIBOR Transition: Norton Rose Fulbright

The UK Financial Conduct Authority has warned that the London Interbank Offered Rate (LIBOR for short) is not likely to be published after 2021. What will happen to LIBOR-based municipal securities, loans, and derivatives that extend beyond 2021 if and when LIBOR goes away? The contracts could be remediated by pending New York and possible federal LIBOR relief legislation. For new contracts, municipal securities issuers and conduit borrowers may be asked to incorporate a new "hard-wired" fallback rate recommended by ARRC or ISDA. For existing (or legacy) contracts, they may soon be asked to enter into bilateral amendments or, in the case of derivatives, to adhere to a recently announced ISDA remediation protocol. What should they do to protect themselves?

Read the Norton Rose Fulbright article.

Signals or Noise in November for LIBOR Transition? - McGuire Woods

Several remarks and releases by public officials and significant regulatory bodies in the first weeks of November garnered significant attention by financial institutions trying to discern next steps in the wind-down of USD LIBOR.

Fed Support for Synthetic USD LIBOR?

First, at a November 10 Senate Banking Committee hearing, Federal Reserve Board Governor Randal K. Quarles, who also serves as the Board's Vice Chair for Supervision, answered questions from legislators about how the Federal Reserve plans to address so-called "legacy" LIBOR-based contracts that are not due to mature until after the end of 2021, which is the presumptive end date for the publication of LIBOR by the ICE Benchmark Administration ("IBA").

In particular, in response to a question from Senator Toomey (R-PA), Governor Quarles explained that the Federal Reserve was working on "a mechanism that would allow those so-called legacy contracts, the great bulk of them, to mature on their existing basis without having to be re-negotiated and shifted to a new rate." He added that the Federal Reserve had been discussing such a "mechanism" with private banks, UK regulators, and the Financial Stability Board, an international body that monitors and makes recommendations about the global financial system. Governor Quarles did not reveal anything about the mechanism itself, however, other than to say that a "variety" of options were being considered. Our informal rendition of his exchange with Sen. Toomey, from the hearing video, is in the margin.[1]

Two days later, in testimony before the House Financial Services Committee, Governor Quarles gave a similar answer in response to questions from Rep. Patrick McHenry (R-NC), namely that that the Federal Reserve was working on "a way to allow those legacy contracts to … mature on their existing terms," and that it expected to "publicly define the way forward to address that" within the next few months. Governor Quarles added that while legislation might "ultimately" be required to deal with legacy contracts, the Fed at the moment was trying to "allow those contracts to mature before we have a legislative solution for the so-called hard tail.[2]

Finally, at the same House hearing, Governor Quarles agreed with Rep. Brad Sherman (D-CA) that there would be "significant disruption" if there is "no solution at all … when LIBOR stops." But he repeated his belief that "there is a way that we can combine current measures that allow the bulk of the existing contracts to mature on their existing terms and then save legislation for the hard tail when we've had time to think about it."[3]

Those comments sound a bit like the notion of "synthetic LIBOR", which was advanced a few years ago by the UK Financial Conduct Authority ("FCA") as a way to deal with Sterling LIBOR in difficult-to-transition holdover contracts – essentially establishing a credit spread over a substitute rate (SONIA in the case of Sterling) published on the same "screen" as Sterling LIBOR (such that contract references to the IBA screen for Sterling LIBOR would land on SONIA + a margin). The FCA has pushed forward with this idea to clean up and deal with laggard contracts, and under legislation currently pending in the UK, the FCA would have broad authority to implement synthetic LIBOR as the fix for Sterling LIBOR contracts.

This works for Sterling LIBOR because its successor (SONIA) has a well-established forward swaps market (over half of the $18 trillion notional value of Sterling swaps in the first half of 2020 were SONIA linked), but would have significant obstacles for US Dollar LIBOR, with less than 1% of the $63 trillion in US Dollar forward swaps traded in the same period linked to SOFR (the presumptive USD LIBOR successor). Given that problem, market participants spent the week or so following his comments wondering what sort of Fed remedy those comments implied.

Not surprisingly, that was one of the first questions put to David Bowman, Sr. Advisor to the Board of Governors of the Federal Reserve, in the November 20 ARRC "office hours". He (appropriately) declined to read those tea leaves for the call participants.

Legislative Solution Back in the Foreground?

Fed Governor Quarles' comments on LIBOR transition legislation also highlight a recent uptick in activity on a "legislative fix" in the New York State legislature and the US Congress. While buzz around legislative solutions seemed largely dormant for much of the year, ARRC favored legislation was finally introduced in the New York State Senate on October 28, and it has been reported that a similar draft bill is also circulating in Congress. Check back in coming weeks for highlights on the substance of those legislative items.

IBA Consultation

Adding to the noise this past week was the November 18 announcement by the IBA of a consultation on its plan to terminate publication of all LIBOR tenors denominated in Sterling, EURO, Swiss Franc and Yen after December 31, 2021. US Dollar LIBOR was conspicuously absent from this list, which could be read to suggest that the demise of US Dollar LIBOR may not take place concurrently with those other currencies. This was also raised during the November 20 ARRC office hours call and (again appropriately) no speculation as to motive was offered. It should be noted, however, that the IBA have reiterated their warning that market participants should not expect US Dollar LIBOR to continue to be published beyond December 31, 2021.

So do these comments and announcements signal a shift in US Dollar LIBOR transition timing, or potential US Dollar LIBOR remediation options, or both? Or are they just understandable noise in a lengthy, complex and technically difficult process along the currently plotted path? Likely the latter but the timing and substance of US Dollar LIBOR transition continues to evolve.

McGuireWoods is continuing to monitor the evolving developments regarding legacy contracts and other LIBOR-transition subjects.

[1] The exchange with Sen. Toomey begins at about the 48:30 mark at the hearing video:

> Sen. Toomey: "I'm mostly concerned about orphan contracts, those contracts that have existed in some cases for years and extend into the future, and they assume a LIBOR index is available for ongoing payments. What are we going to do about these orphan contracts … [that] don't end until after the date on which we expect LIBOR to no longer be operative?"
>
> Gov. Quarles: "I think we need to consider a mechanism that would allow those so-called legacy contracts, the great bulk of them, to mature on their existing basis without having to be re-negotiated and shifted to a new rate … . I think there are a variety of ways to do that. The banks have been discussing that, we've been discussing it with banks. It's an international issue as well [so] we've been discussing it through the F[inancial] S[tability] B[oard] and directly with the U.K. which has a special responsibility for LIBOR, and that within the next month or two we should have a plan to share to address that."

[2] The exchange with Rep. McHenry begins in the hearing video at about the 51:45 mark.

> Rep. McHenry: "We want a clear understanding of the path forward on LIBOR. … Can you give us some assurance of your process going forward?"
>
> Gov. Quarles: "… The issue you raised is an important one from a stability point of view, which is that there are a lot of legacy contracts that currently rely on LIBOR that we need to define a path forward for after the end of 2021. The transition for new contracts is going pretty smoothly. The legacy contract is the big issue there … I think finding a way to allow those legacy contracts to continue for at least some period, to allow the

> bulk of those legacy contracts to mature on their existing terms without a significant change would probably be the best way forward, and we are working on a method to do that. There are a variety of different ways that one could do that, but I would expect over the next couple of months to be able to publicly define the way forward to address that."
>
> Rep. McHenry: "Do you have a legislative request, or a need for legislative action by the Congress?"
>
> Gov. Quarles: "I think the ultimate transition will ultimately require a legislative element, but at this point I think the answer would be no because I think what we want to try to do is find a way to allow those contracts to mature before we have a legislative solution for the so-called hard-tail."

[3] The exchange with Rep. Sherman begins in the hearing video at about the 1:15:30 mark.:

> Rep. Sherman: "What would be the consequence of simply not having any regulatory or legislative solution, would this result in a lot of class action lawsuits, etc.?"
>
> Gov. Quarles: "If there were no solution at all, yes, when LIBOR stops there'd be significant disruption. I think there is a way that we can combine current measures that allow the bulk of the existing contracts to mature on their existing terms and then save legislation for the hard tail when we've had time to think about it."

By Donald A. Ensing, Susan Rodriguez, Jennifer J. Kafcas & Joseph J. Reilly on November 25, 2020

LIBOR Termination May be Postponed to 2023: Day Pitney

On November 30, 2020, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corp. and the Office of the Comptroller of the Currency issued a joint statement (the Joint Statement) on LIBOR transition. The purpose of this statement was to encourage banks to transition away from U.S. dollar LIBOR (USD LIBOR) as soon as practicable while providing sufficient time for many USD LIBOR-based contracts to mature before USD LIBOR experiences disruption.

- *Extension of USD LIBOR.* ICE Benchmark Administration, in its capacity as administrator of USD LIBOR, will consult on its intention to extend publication of USD LIBOR (other than one-week and two-month tenors) by 18 months. Instead of discontinuing publication on December 31, 2021, USD LIBOR (other than one-week and two-month tenors) would continue to be published until June 30, 2023.
- *LIBOR Phase Out.* Even though USD LIBOR would continue to be published through June 30, 2023, the Joint Statement calls on banks to cease entering into new contracts that use USD LIBOR as a reference rate by no later than December 31, 2021, and if practicable, as far in advance of that deadline as possible. Should banks enter into new contracts before that deadline that use USD LIBOR as a reference rate, those banks are encouraged to include clearly defined alternative reference rate provisions.

- *Avoiding Market Disruption.* The Joint Statement notes that extending the publication of certain USD LIBOR tenors for an additional 18 months would allow most legacy USD LIBOR contracts to mature in accordance with their terms without disruption.
- *Impact on Documentation.* Financial institutions are already including USD LIBOR replacement language in their contracts, so this extension should have little impact on documentation of new contracts. However, this extension could help avoid an onslaught of amendments to legacy contracts at the end of 2021 that would overwhelm borrowers and lenders alike.

Day Pitney Alert

December 1, 2020

Day Pitney Author(s) Michael W. Kaufman, Namita Tripathi Shah

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S&P: SOFR Emerging As Alternative To LIBOR In U.S. Debt Markets

Key Takeaways

- SOFR has emerged as the leading rate to replace dollar LIBOR, which is now scheduled to phase out for new-issue transactions by December 2021 and for most legacy transactions with active maturities by June 2023.
- Based on data from the Federal Reserve Bank of New York and earlier repo transaction data since the late 1990s, SOFR has been tracking closely with dollar LIBOR.
- The historical time series analysis between the two benchmark rates shows a positive average and median of LIBOR over SOFR.
- Because only daily SOFR rates currently exist, compounding is typically used for this new rate and helps smooth out most of the volatility in daily rates.

Following the July 2017 announcement by the U.K.'s Financial Conduct Authority that the London Interbank Offered Rate (LIBOR) cannot be assured following 2021, there has been significant discussion around replacement benchmark rates in financial markets. A recent consultation published by the ICE Benchmark Administrator and supported by the U.S. Federal Reserve has proposed to continue dollar LIBOR quotes for the most actively used maturities on legacy transactions until June 2023. Furthermore, U.S. bank regulatory agencies have recently stated that banks should stop using dollar LIBOR in new contracts "as soon as practicable" and, in any event, by Dec. 31, 2021. For U.S. debt instruments (including structured finance securities) with dollar LIBOR exposures and maturities beyond 2023, this will mean changes to benchmark interest rates. While market participants are working to build provisions for alternative benchmarks in new transactions, one source of continued uncertainty centers around legacy transactions where fallback language varies widely.

In the U.S. the Federal Reserve Bank of New York ("the Fed") has developed, and is now publishing on a daily basis, the Secured Overnight Financing Rate (SOFR). Although there are a number of differences with LIBOR, this near-risk-free rate has been viewed by many as the leading replacement rate in U.S. financial markets for dollar LIBOR, similar to how the Sterling Overnight Index Average Rate (SONIA) has been a replacement rate for Sterling LIBOR in the U.K. While SOFR has been published since April 2018, the Fed has released a longer time series, from August 2014 to March 2018, with modeled pre-production estimated data on SOFR that now underlie the official rate publication. Outside the U.S., central banks and financial market authorities have also been charting courses toward new replacement benchmarks set to become active by 2021.

Continue reading.

4 Dec, 2020

NFMA White Paper on Best Practices in Cybersecurity Risk Disclosure for State & Local Governments in Municipal Offerings.

On November 30, 2020, the NFMA released the final version of its paper on cybersecurity risk disclosure.

- White paper, dated November, 2020
- Press release, dated November 30, 2020

SEC Needs to Take 'Bottom to Top' Review of Fixed Income Markets: Crenshaw

The next chairman or chairwoman will likely "take a hard look at the commission's approach to ESG," Crenshaw said.

Once Securities and Exchange Commission Chairman Jay Clayton departs at year-end, the four member agency — which will consist of two Republicans and two Democrats — can likely find bipartisan agreement on fixed income market structure issues, according to SEC Commissioner Caroline Crenshaw.

"Right now, our fixed income markets are regulated using a regime that … has been imported from the equity markets," Crenshaw, a Democrat, said Friday during the virtual Georgetown Financial Markets Quality Conference. "This can cause problems. Fixed income securities are traded in a very different way."

The commission should take "a bottom to top look at the corporate and muni markets. … We need to understand how these bonds are actually traded and how these things are happening on the ground as we build a regulatory system around it," Crenshaw said.

SEC Commissioner Elad Roisman, a Republican, added that "there is still a lot we can do when it comes to fixed income."
Retail investors, Crenshaw said, "have more exposure, perhaps more than anyone else, to municipal bonds, both directly and indirectly through various funds."

The SEC, she continued, needs "to do a better job of ensuring that all investors have the information they need to make the best investment decisions they can. It's especially an issue for retail investors because they often don't have access to the same type of information that nonretail investors have access to.

"That's true across all products, but it's especially true in the muni markets where a lot of bonds are thinly traded and there's very little pre-trade transparency."

Next SEC Chair's Priorities

The next chairman or chairwoman will likely "take a hard look at the commission's approach to ESG," especially those focused on climate risk, Crenshaw said.

Added Roisman: ESG is "a conversation that will be ongoing; it's one that I can't imagine we're not going to be having."

ThinkAdvisor

By Melanie Waddell | November 23, 2020 at 11:45 AM

Broker-Dealer Settles Charges of MSRB Trade Reporting Failures.

A broker-dealer settled FINRA charges of failing to accurately report trades to the MSRB.

In a Letter of Acceptance, Waiver and Consent, FINRA determined that the broker-dealer did not report its trades in increments of seconds, as required under MSRB Rule G-14 ("Reports of Sales or Purchases"). According to the Letter, for an approximately three-year period, the firm reported all trades as being done at "00" seconds, rather than the exact number of seconds. This resulted in 147,000 trade reporting violations. Further, FINRA found that the firm had 167 manual trade reporting failures also involving failure to report the correct time of trade. These reporting failures also resulted in violations of MSRB Rule G-8 ("Books and Records to be Made by Brokers, Dealers, and Municipal Securities Dealers and Municipal Advisors").

FINRA also determined that the broker-dealer violated MSRB Rule G-27 ("Supervision") by failing to follow the requirements under its written supervisory procedures to (i) execute a comparison between the firm's records and corresponding contra party trade reports to ensure the accuracy of the times of trade it reported and (ii) specify the frequency of its review of its trade reports, and designate a supervisor for such review.

To settle the charges, the broker-dealer agreed to a (i) censure and (ii) $25,000 fine ($15,000 for the MSRB Rule G-14 and G-8 violations and the balance for the MSRB Rule G-27 violations).

Commentary

When technology is not working, that failure creates the capacity for a remarkable number of violations; e.g., in this instance, 147,000 violations due to the technology failure vs. 167 errors due to the manual process failure. Of course, the technology is indispensable, but the numeric difference in the number of failures really illustrates the importance of having compliance procedures that review the end results of technology processes.

Cadwalader Wickersham & Taft LLP – Steven D. Lofchie

November 20 2020

Municipal VRDO Class Action Survives Banks' Request for Dismissal.

Financial institutions should work with outside counsel to ensure that their internal policies and external actions minimize conduct that may violate state and Federal laws and regulations, and incentivize employees to reward high ethical standards

On November 2, the United States District Court for the Southern District of New York (SDNY) largely denied a motion to dismiss a class action lawsuit brought by the cities of Philadelphia and Baltimore (collectively, the Plaintiffs) in May 2019. The Plaintiffs brought the action on behalf of themselves as well as other municipal issuers of variable rate demand obligations (VRDOs) against several large banks (the Banks). Plaintiffs allege that beginning in April 2009 and continuing through November 2015 (the Class Period), these banks collectively forced state and local governments to pay inflated interest rates on the bonds and notes issued as VRDOs in derogation of the Sherman and Clayton Antitrust Acts, as well as various state laws. The Banks deny the allegations and claim that they are baseless.

Judge Jesse M. Furman ruled that the Federal antitrust claims, as well as some of the state law claims, could continue.

Background

Publicly-Financed Projects

At issue in the lawsuit are the Banks' alleged improper remarketing practices in connection with bonds and notes issued by state and local governmental entities, as well as other public agencies and authorities. Issuers use these bonds/notes to finance projects including, but not limited to, economic development, education, hospitals, housing, transportation, and utilities.

Public Support

Certain VRDO bonds and notes are secured by tax revenues – generally, corporate and personal income taxes, sales taxes, and property taxes from individual and corporate taxpayers in the respective jurisdictions.[1] Other VRDOs are secured by revenues generated from a particular community project being financed. Some such examples include: (i) tenant rents for affordable housing, (ii) medical charges for hospitals, (iii) mortgage payments for single family housing, (iv) utility payments for electric, water, and sewer systems, (v) landing fees/passenger ticket charges for airports, (vi) tolls for bridges and highways, (vii) fares for mass transit, (viii) tuition for colleges and universities, (ix) property taxes for K-12 education, and (x) assorted local taxes and user fees for libraries, government buildings, police and fire stations, and parks.

To incentivize projects with a valuable community purpose, the Federal government provides a tax exemption on the bonds/notes to investors. For a project to qualify for the exemption, the Internal Revenue Code requires that for-profit companies have a limited role in these financed projects. Notably, unlike most other bond markets, there is an even split between corporate investors and individual investors of municipal bonds/notes as individual investors benefit from the Federal (as well as state and local) tax-exemptions, are often utilized for an individual's retirement savings and, importantly, provides monies to build and maintain beneficial projects to the community at large.

VRDO Structure

General

VRDO bonds are issued on a long-term basis but have short-term interest rates that reset on a periodic basis, typically weekly. Accordingly, VRDOs are very attractive for governmental entities as they can borrow long-term at generally lower short-term rates. VRDOs also offer flexibility to investors, who can exit the investment on a weekly basis through a remarketing agent. Here, remarketing agents are required to remarket the bonds to other investors. Alternatively, if there are no investors willing to purchase the VRDOs, the bonds are 'put' back to a rated bank. Both the remarketing agent and the bank providing liquidity (the Liquidity Bank), which are typically the same or affiliated entities, charge fees for their services. These fees must be added to the favorable interest rates to obtain the true cost of the borrowings to the governmental entities.

Interest Rate Swaps

Even though governmental entities (and their taxpayers) appreciate low interest rates, governmental entities generally are averse to variable rate risk, which can increase or decrease on a weekly basis. For this same reason, many homeowners do not like having adjustable rate mortgages, especially in a low fixed-rate environment. Accordingly, to assure that interest rates do not fluctuate, the Banks often provide parallel interest rate swaps so that the governmental entities take limited interest rate risk while the Banks take the variable rate risk.

However, there are numerous risks associated with swaps. These risks include, but are not limited to, basis risk, counterparty risk, and termination risk. Generally, governmental entities are not familiar with many of these risks. And these risks are often not fully explained by the Banks themselves. In general, in a falling interest rate environment (such as what has been occurring since the Great Recession, and exacerbated by the pandemic), interest rate swaps can be a significant drain on the resources of governmental entities. Additionally, conspiracies to manipulate interest rates (as allegedly occurred in this dispute) are the frequent subject of many of the cases cited by this court. Indeed, in resolving this motion, the court relied on several prior cases that involve Banks and other market participants manipulating interest rate swaps and other financial/commodity markets.[2]

Although the court discusses testimony from a Bank insider that VRDOs are a relatively low margin product for the Banks, interest rate swaps have historically been a very high margin product for banks offering swaps. Indeed, interest rate swaps have historically generated a significant percentage of large bank profits. For that very reason, such banks often encourage governmental entities to tie VRDOs to swaps. By this arrangement, the banks gain tremendous profits (and resultant banker bonuses), while the government reduces its perceived risks associated with VRDOs instead of undertaking a straight fixed rate bond deal or a VRDO with an interest rate cap.[3]

Remarketing Agent Role

In most remarketing agreements, the banks have two primary obligations. First, they must reset the VRDOs weekly interest rate at the *lowest possible rate* that would permit the bond to trade at par. Second, as mentioned above, the banks must remarket the VRDOs to other investors at the *lowest possible rate* when existing investors decide to exit the investment. Remarketing agreements can also generally be terminated by the governmental entities at will. If, for example, a governmental entity is not satisfied with a bank's remarketing efforts, then the governmental entity might want to replace the bank with another remarketing agent.

Liquidity Bank Role

If the banks, as remarketing agents, are unable to find another investor, the Liquidity Banks are required to purchase the tendered, but unremarketed, bonds. This contractual obligation between the banks, as Liquidity Banks, and the governmental entities is typically called a letter of credit and reimbursement agreement. The interest rate for a tendered, un-remarketed, bond that is held by the Liquidity Bank typically ranges from 10-15%, a significant increase from the low current 1-3% interest rate on VRDO bonds. Notwithstanding this high rate, Liquidity Banks prefer not to hold un-remarketed bonds, as doing so typically indicates that the transaction has some sort of underlying issue.

Importantly, a bond with a drawn letter of credit would require that additional capital be set aside by the Liquidity Bank. In essence, this un-remarketed bond would then, generally, be characterized as a defaulted bond by the Liquidity Bank. Banks try to avoid this situation at all costs.

Market Disruptions

Lehman Brothers' bankruptcy filing in September 2009 caused tremendous upheavals in the VRDO market. In 2008, $116.3 billion of VRDO bonds were issued by municipal issuers.[4] In contrast, in 2009, $32.3 billion of VRDO bonds were issued by these issuers, a decrease of 72%. [5] This general decreasing trend continued in each subsequent year of the Class Period. [6] One reason for these significant decreases was the failure of many banks to maintain satisfactory credit ratings. The decline in the banks' credit ratings forced governmental issuers to pay the un-remarketed bond rate of 10-15%, causing significant financial strains on government resources.

As these upheavals occurred in the midst of the housing crisis, Arent Fox was brought in to help develop the Temporary Credit and Liquidity Program (TCLP) with the US Department of Treasury, the Federal Housing Finance Agency, Fannie Mae and Freddie Mac, and state housing finance agencies throughout the country. This $8 billion program replaced the Liquidity Banks' liquidity facilities with facilities jointly provided by Freddie Mac and Fannie Mae.

State and local housing finance agencies are tasked with supporting affordable housing. This task became difficult (if not impossible) due to, among other things, the parallel banking crisis, which required these housing finance agencies to devote their limited resources to pay much higher interest rates on their VRDO bonds rather than developing new affordable housing and supporting existing housing projects. This prompted the creation of TCLP, along with a program to facilitate the issuance of new bonds during this crisis period – the $16 billion New Issue Bond Program (NIBP), which the Firm also helped develop and implement. Although the TCLP program was scheduled to terminate in 2012, it was extended through 2015, the end of the Class Period. The primary reason for an extension was that the Liquidity Banks were reluctant to provide liquidity during this tumultuous period for certain governmental issuers.

Alleged Antitrust Conspiracy

As alleged in the Class Action Complaint, the Banks, which served as remarketing agents for approximately seventy-five percent of all VRDOs issued in the United States, conspired not to compete against each other.

Philadelphia and Baltimore claimed that the Banks shared information regarding proprietary information, such as VRDO Bank inventory levels and planned changes to the VRDOs' base interest rates, in an effort to keep interest rates on VRDOs artificially high. According to the Complaint, collusion existed at all levels across each bank, ranging from senior personnel in Municipal Securities Groups, to the remarketing desks below these groups, down to sales desk personnel. [7]

As detailed in the Complaint, agents of the Banks communicated regularly, frequently, and in great detail. They often shared confidential and sensitive information relating to the VRDO issues. In some instances, the Banks are alleged to have shared the specific rates they were planning to set.

Ultimately, a related whistleblower complaint was filed, which led to the Securities Exchange Commission (SEC) opening a formal investigation in November 2015, and the Department of Justice (DOJ) starting its own investigation in 2016.

SDNY Rulings

Antitrust Claims

The bulk of the court's decision dealt with the Federal antitrust claims, which were ultimately upheld. The court stated that, during the Class Period, there was a plausible argument that the Banks "conspired *not* to compete against each other in the market for remarketing services." Needless to say, this type of alleged anticompetitive behavior is precisely the type of conduct contemplated and prohibited by the Clayton Act and the Sherman Act more than 100 years ago.

Rate Manipulation

In setting the initial rate, weekly rate resettings, and the rate upon tender of VRDOs, the Banks are supposed to consider the individual characteristics of the bonds (*e.g.,* issuer financial strength, security, Liquidity Bank credit rating), market conditions and investor demand, rather than Bank inventory levels or profits.

Here, the court determined that by resetting the VRDO base rates on a regular and arbitrary basis, the Banks had coordinated the rate reset of a large number of VRDOs in violation of the Federal antitrust laws. In fact, Judge Furman found the Banks' conduct to be both "deceptively simple" and "effective," as the interest rates during the Class Period for VRDOs were alleged to be nearly seventy-five percent higher than the rates would have been absent the Banks' conduct. The court also determined that the coordination of interest rates ceased shortly after the SEC and DOJ investigations began. In the court's view, this timing indicated that the Banks had stopped coordinating their illicit rate-setting practices in direct response to the investigations.

Collusive Activities

Although pending investigations may not, standing alone, satisfy an antitrust plaintiff's pleading burden, the court held that government investigations may be used to bolster the plausibility of these claims and allegations of rate manipulation. Thus, the court concluded that there were enough facts in the complaint to survive the motion to dismiss.

The court also found that allegations of Bank misconduct constituted "plus factors" – circumstantial evidence demonstrating, by inference, the existence of a price-fixing conspiracy.[8] For example, the court found that the regular communications and exchange of information between the Banks demonstrated that they were able to (and did) coordinate their rates to ensure that none of the Banks broke ranks from the conspiracy. The court also ruled that each of the Banks had a motive to engage in the alleged scheme.

In addition, the court also determined that that the Banks had used a third-party pricing service (J.J. Kenny Drake Inc.) until 2012 to telegraph to each of the Banks the collective view of where the base rate should settle for the Banks in remarketing bonds.[9]

Accordingly, the court held that Philadelphia and Baltimore had satisfied their burden, and ruled that the antitrust claims could continue against all defendants.

State Law Claims

Breach of Contract

Philadelphia and Baltimore also brought several breach of contract claims against the Banks based on Pennsylvania and Maryland state law. The court determined that several of the Banks had not entered into contracts with either city, served as their remarketing agents, or otherwise had any role at all in facilitating a contractual relationship with the cities. Accordingly, the court granted the motion to dismiss the breach of contract claims as to each of these “Non-Counterparty Banks.”

However, the court denied the motion to dismiss as to the remaining Banks that *had* entered valid remarketing agreements with the cities (the “Counterparty Banks”). The court held that Plaintiffs sufficiently pled that these “Counterparty Banks” *had* breached their contracts with Plaintiffs by failing to fulfill a contractual obligation under the remarketing agreements to use their *best efforts* – a high standard in the municipal bond market – to reset the interest rates of the VRDOs based on prevailing market conditions, and to remarket the bonds at the lowest rate possible that would allow the bonds to trade at par.

Breach of Fiduciary Duty

Philadelphia and Baltimore also brought several breach of fiduciary duty claims against the Banks. However, as it had done with the Non-Counterparty Bank breach of contract claims, the court dismissed the fiduciary duty claims against the Non-Counterparty Banks, ruling that they had no fiduciary or confidential relationship with either of the Plaintiffs. The disposition of the remaining fiduciary duty claims varied based on the applicable state law.

Unjust Enrichment

Finally, the Complaint also included claims for unjust enrichment against all of the Banks. The court reasoned that both Pennsylvania and Maryland law required the Plaintiffs alleging unjust enrichment to show that the validity of a contract itself is actually disputed. Here, the court noted that none of the Banks disputed the *validity* of the remarketing agreements. Rather, the dispute involved the *performance* stemming from the contracts. Accordingly, the court ruled that the unjust enrichment claims against the Counterparty Banks, which were duplicative of the breach of contract claims, must be dismissed.

The court also dismissed the unjust enrichment claims against the Non-Counterparty Banks, holding that both Plaintiffs failed to plausibly allege, as Pennsylvania and Maryland law requires, that these Banks had been enriched at their expense. Rather, as Judge Furman determined, neither Plaintiff had conferred a direct benefit to any Non-Counterparty Bank.

Statute of Limitations

The applicable statute of limitations for the claims brought in this case ranged from two to six years. The statute of limitations is tolled in each relevant jurisdiction where allegations plausibly allege that the Banks concealed their misconduct, and the Plaintiffs’ ignorance of the concealed misconduct was not a product of their own lack of reasonable diligence. Accordingly, the court held that the alleged misconduct conduct was secret and covert by its very nature, and further ruled that a determination of the Plaintiffs’ diligence in uncovering this conspiracy was premature at the pleadings stage.[10]

Takeaways

Even though Plaintiffs' lawsuit, as well as the DOJ and SEC investigations, are ongoing, banks and other market participants can already draw certain key lessons from the case. Crucially, the case demonstrates that banks and other financial institutions are vulnerable to Federal antitrust claims based on their conduct in financial markets, especially where (as here) courts consider circumstantial 'plus' factors to infer the existence of price-fixing conspiracies.

Financial Institutions

Accordingly, financial institutions should ensure that they have policies in place that prevent anticompetitive conduct similar to what is alleged to have occurred in this case.

In particular, financial institutions should be mindful of communications with other institutions that could imply horizontal conspiracies. Where necessary, financial institutions should retain outside counsel to develop policies and procedures to prevent or, at a minimum, immediately identify improper conduct *before* it develops into a bank-wide or industry-wide problem.

Additionally, all financial institutions, and particularly those that deal with bonds, swaps and other financial instruments, should be cognizant of the ability of municipalities and corporate borrowers to sue them for contractual breaches where there are plausible breaches of the underlying financing agreements. Here, too, financial institutions should work with outside counsel to ensure that their internal policies and external actions minimize conduct that may violate state and Federal laws and regulations, and incentivize employees to reward high ethical standards.

Governmental Entities and Conduit Borrowers

In addition, as always necessary, governmental entities, as well as conduit borrowers (including corporations and, in particular, not-for-profit corporations), should retain sophisticated, experienced and independent counsel and financial advisors to assure an independent review of VRDOs and the associated derivatives instruments so as to avoid repeating the turmoil impacting these instruments during the Great Recession. This is crucial for all financings, and not just VRDOs.

We can always hope…

[1] Due to the COVID-19 pandemic and resultant economic dislocations, general sales and selective sales taxes have likely been most affected, severely straining the financial wherewithal of municipal issuers. The impact will likely not be completely apparent until the end of such governmental entities' fiscal years (typically June 30th). The ten (10) most affected states, in order of highest percentage of tax revenues from these taxes (ranging from 61.7% to 85.1%), are:

1. Texas 6. Tennessee
2. South Dakota 7. Mississippi
3. Florida 8. Indiana
4. Nevada 9. Ohio
5. Washington State 10. Hawaii

In addition, due to disruptions in the oil and gas industry as a result of the pandemic, related severance taxes may also be adversely impacted. The states with significant severance taxes, in order of priority highest percentage of tax revenues from these taxes (ranging from 31.7% to 52.5%), are:

1. North Dakota 2. Alaska 3. Wyoming

Source: "Share of tax revenue in the United States by source FY 2019, by state," Statista (June

2020).

[2] In deciding the Banks' motion to dismiss, the court relied on several recent SDNY cases involving interest rates swaps. *See Gelboim v. Bank of Am. Corp., In re Interest Rate Swaps Antitrust Litig.*, 823 F.3d 759 (2d Cir. 2016) (finding that an inter-bank conspiracy was plausibly alleged); *Sonterra Capital Master Fund Ltd. v. Barclays Bank PLC*, 366 F. Supp. 3d 516 (S.D.N.Y. 2018) (denying a motion to dismiss where defendants allegedly colluded to share information, coordinate rate submissions, and engaged in manipulative trading practices); *Alaska Electr. Pension Fund v. Bank of Am. Corp.*, 175 F. Supp. 3d 44 (S.D.N.Y. 2016) (relating to manipulation of ISDAfix, a rate recently confirmed with the Federal Reserve Board of St. Louis (FRED), that as best as it can tell, is derived from LIBOR); and *In re LIBOR-Based Fin. Instruments Antitrust Litig.*, 27 F. Supp. 3d 447 (S.D.N.Y. 2014) (dismissing unjust enrichment claims against non-counterparty defendants).

In addition, the court also relied on a separate line of SDNY cases involving other types of market manipulations. *See In re Foreign Exch. Benchmark Rates Antitrust Litig.*, 74 F. Supp. 3d 581 (S.D.N.Y. 2015) (holding that consolidated complaint adequately established antitrust injury); *In re Commodity Exchange, Inc., Gold Futures & Options Trading Litigation*, 328 F. Supp. 3d 217 (S.D.N.Y. 2018) (holding that class failed to state antitrust conspiracy claim); *In re GSE Bonds Antitrust Litig.*, 396 F. Supp. 3d 354 (S.D.N.Y. 2019) (holding that alleged price-fixing conspiracy was inherently self-concealing so as to constitute fraudulent concealment); and *In re Platinum & Palladium Antitrust Litig.*, No. 1:14-CV-9391 (GHW), 2017 WL 1169626 (S.D.N.Y. Mar. 28, 2017) (finding a conspiracy plausibly alleged).

[3] In contrast to a swap which has no up-front cost (though potential substantial costs over time), an interest rate cap has an up-front cost (though with no costs over time) but is often limited to a period shorter than the tenor of the underlying bonds. In deciding between a swap and a cap, the governmental entity will often decide to go with the 'free' product (i.e., a swap). It should be emphasized that most banks do not even volunteer a cap option due to its limited profit potential for the bank (and the banker).

[4] The Bond Buyer.

[5] Id.

[6] Id.

[7] Parallel allegations against banks and other institutions were made in the SDNY cases referenced by the court in Footnote 2 above.

[8] *See Bell Atl. Corp. v. Twombly,* 550 U.S. 544, 556 (2007).

[9] This is consistent with many of the SDNY cases referenced in Footnote 2 above.

[10] Here, the court also ruled that, at the pleading stage, discovery would be appropriate for the parties to develop their claims and defenses. *See In re Issuer Plaintiff Initial Pub. Offering Antitrust Litig.*, No. 00-CV-7804 (LMM), 2004 WL 487222, at *4 (S.D.N.Y. Mar. 12, 2004) (denying motion to dismiss where relevant statute of limitations had been tolled due to alleged covert rate-fixing conspiracy).

Arent Fox

December 3, 2020

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Regulator Joint Statement Highlights Need to Move on from LIBOR (But For Some, Not Necessarily to SOFR) - McGuireWoods

On November 6, 2020, Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency ("OCC"), and the Federal Deposit Insurance Corporation ("FDIC") (collectively, the "Agencies") issued a joint "Statement on Reference Rates for Loans" (the "Joint Statement").

The Takeaway: You don't have to go to SOFR, but you can't stay here. The Agencies expect banks to include fallback language in existing LIBOR loan contracts and "begin transitioning loans away from LIBOR without delay," but recognize that the "use of SOFR is voluntary" and that a more credit sensitive alternative may be more appropriate for some banks. Although the Agencies have recognized the desire by some banks for a more credit-sensitive alternative to SOFR as a replacement for LIBOR, they have also been clear that they won't be recommending any particular credit sensitive alternative, in contrast to the ARRC's recommendation of SOFR. The Agencies note that "[b]anks should assess the appropriateness of alternative reference rates in light of their funding costs and their customers' needs." So while money center banks and syndications markets continue to trend towards SOFR, the Agencies have made clear that banks in other market segments have regulatory leeway to continue to evaluate other options and alternatives.

But why might SOFR not fit all shapes and sizes?

Stress Test:

The Joint Statement foregrounds an ongoing undercurrent of discussions by some banks focused on potential issues with SOFR as an index rate in times of economic stress. In a September 23, 2019 letter to the Agencies, a group of banks highlighted the squeeze that many banks would feel during times of economic stress with a portfolio of SOFR indexed loans:

- LIBOR is an unsecured credit sensitive rate, so that in times of economic distress, as the cost of funds for banks rise, the yield on banks' portfolio of LIBOR indexed loans also rises; thus, with LIBOR indexed loans, bank lending and borrowing rates tend to move in concert; HOWEVER
- SOFR is a secured nearly "risk free rate" (overnight rate for borrowing secured by U.S. Treasury securities), and as such during times of economic distress, "SOFR (unlike LIBOR) will likely decrease disproportionately relative to other market rates as investors seek the safe haven of U.S. Treasury securities."

With a portfolio of SOFR based loans, banks will bear the risk that in times of economic distress, their cost of funds will go up but interest income will go down, squeezing banks' net interest income. The tendency of borrowers to draw down credit lines and hoard cash during economic crisis amplifies the potential problem.

Credit Sensitivity Group:

The Agencies responded to that letter by organizing a Credit Sensitivity Group ("CSG"), which conducted four workshops over the summer (June 4, 2020, July 22, 2020, August 12, 2020 and August 27, 2020) to vet and discuss the issue, summaries of which can be found here. Additional working sessions are scheduled for November 18, 2020 and a TBD December date to continue discussions around developing a credit sensitive component to help address the disconnect between SOFR and bank cost of funds under conditions of economic distress. However, in a public letter from the Agencies on October 21, 2020 and in advance of the next CSG working sessions, the Agencies made clear that "the official sector does not plan to convene a group to recommend a specific credit-sensitive supplement or rate for use in commercial lending products."

Challenges to Credit Sensitivity / "Dynamic" Spreads:

Constructing a "dynamic" adjustment to SOFR to account for ongoing changes in credit quality was weighed by the ARRC early on, but discarded in favor of the currently recommended "static" spread adjustment added to SOFR to approximate LIBOR (i.e., a spread determined and fixed at the point in time that LIBOR is discontinued). In electing to go with a static spread adjustment, the ARRC recognized that dynamic spread adjustment formulations suffer many of the same IOSCO compliance problems as LIBOR itself: (a) limited transactions in normal times that could be used to calculate the spread adjustments, (b) even more limited transactions in periods of stress and (c) an unstable sample of firms that borrow in unsecured wholesale markets, resulting in borrower-based variability. Nevertheless, market participants continue to explore ways mitigate the risks posed by SOFR movement during economic stress.

As the clock winds down on LIBOR, ISDA rolls out its IBOR Benchmark Fallback Protocols for swaps and the syndicated loan market moves toward hardwired fallbacks to SOFR, the demand by some banks for a more credit-sensitive alternative to LIBOR continues to generate both discussion and recognition by the Agencies.

By Donald A. Ensing & Susan Rodriguez on November 18, 2020

McGuireWoods LLP

The Transition Out of LIBOR: What State and Local Governments Should be Discussing with Their Financing Teams

The London Interbank Offered Rate (LIBOR) is a global benchmark interest rate calculated daily, and is the most widely used benchmark in the capital markets. State and local governments often see this rate in swaps/derivatives products intertwined with municipal debt, as well as in floating rate notes, lease contracts, bank loans, direct placements, and other types of financings and credit enhancements.

LIBOR will be phased out over the rest of 2020 and on December 31, 2021, will cease publication. Therefore, state and local governments need to know that existing contracts that reference LIBOR will need to be revised to perform as intended and new contracts will have to reference a new benchmark, such as the Secured Overnight Financing Rate (SOFR).

The Federal Reserve along with the Federal Reserve of New York, has established a working group with GFOA and other stakeholder groups – the Alternative Reference Rates Committee (ARRC) – to ensure a transition for the financial markets from LIBOR to a new rate, the Secured Overnight Financing Rate (SOFR). In some cases, state and local governments may see other rates used for some financing products.

To help governments best understand and address these changes, below are a list of questions that you should discuss with your financing team to ensure that as new benchmark rates take hold, these changes do not trigger rate revisions or other provisions that cause a financial disruption to the government/government entity.

Questions Issuers Should Ask Internal and External Finance Team

Does my jurisdiction have any LIBOR exposure?

Review contracts to identify contract terms and what exposure the government has with the impending change in the reference rate, LIBOR. Identify entity's outstanding/legacy financial products that may be predicated on the LIBOR rate:

- Swaps/derivatives
- Floating rate notes
- Bank loans
- Direct placements
- Letters of credit
- Purchasing cards
- Lease Contracts
- Investment Products, including Guaranteed Investment Products (GICs)

What do I do if I find LIBOR referenced?

Discuss with finance team – including counsel, swap advisor, and municipal advisor – the changes that may need to occur in these legacy contracts. Most swap/derivatives contracts are based on the standard terms contained in the International Swaps and Derivatives Association (ISDA) Master Agreement and related documents. The ISDA Master also contains a Fallback Protocol, which was recently revised and released on October 23, 2020. Discussing the new protocol with your Qualified Independent Representative (QIR) and your financing team is essential for your governmental entity. Members are encouraged to adhere to the protocol to modify contracts to reflect the change from LIBOR to SOFR or other rate using the ISDA LIBOR Fallbacks Protocol. NOTE that the fallback protocol includes a provision for ISDA to issue a "cutoff date." Failure to adhere in a timely manner will result in unnecessary complications.

In bank loans and direct placements, discuss with the bank/counterparty the replacement rate that will be used for these contracts and request to review with the bank/counterparty any financial penalties that could occur.

Governments may also have investments that are tied to LIBOR rates. Members should review investments and discuss any that do reference LIBOR with your financing team, including investment adviser.

What else should I think about if I find LIBOR referenced and need to make changes to my contract?

If approval from a governing body is needed to make changes with the contract, allow enough lead-time to have the contract reviewed and suggested changes made by members of the finance team to the governing body for approval.

How do I report the transition from LIBOR on my financial statements?

Identify any accounting matters, such as GASB 93 that need to be addressed when making changes to the contract and the reference rate. Governments should address these and other accounting and financial reporting implications that result from the replacement of an IBOR.

Is this a material event that should be disclosed?

Discuss with bond counsel/disclosure counsel if contract changes trigger a material event filing or if the entity should submit a voluntary disclosure filing in EMMA regarding contract changes away from LIBOR.

What else should I ask if the exposure originates back over a decade?

Some contracts may be in place that pre-date the passage of the Dodd Frank Act in 2010 that now requires, under Commodity Futures Trading Commission (CFTC) rules, that state and local governments and entities to use a Qualified Independent Representative (QIR)/Swap Advisor when engaging in derivative products. Governments need to have a QIR in place to assist them with some legacy transactions if changes are made, and for any new swap transactions.

Should I engage any professional particularly suited to assist?

When discussing derivative and swap transactions with the entity's municipal advisor, ensure that the municipal advisor is qualified and understands the breadth of this market. Governments may need to engage the services of a swap advisor (QIR) to assist them with these transactions, which could be a different party than the entity's municipal advisor.

While the Department of the Treasury and IRS has provided guidance that changing LIBOR to SOFR in a financing does not constitute a new bond issuance, governments should discuss contract changes with bond counsel/tax counsel to address tax integration matters and ensure there are no federal tax compliance concerns.

What should I do if my entity will be engaging in a transaction within the next year?

When looking to engage in NEW swaps/derivatives, floating rate note transactions, bank loans or direct placements, discuss with your financing team and counterparties what reference rate will be used in the contract. Governments are advised to NOT accept continued use of LIBOR in new contracts, which could trigger the need for changes after 2021 and with that, possible additional fees.

Government Finance Officers of America

Financial Accounting Foundation Names Five New Members to the Board of Trustees.

Norwalk, CT—November 17, 2020 — The Financial Accounting Foundation (FAF) Board of Trustees today announced the appointment of new Trustees Timothy L. Christen, Lynnette Kelly, Richard N. Reisig, Sarah E. Smith, and Robin L. Washington. All appointees' terms will begin January 1, 2021 and conclude on December 31, 2025.

The FAF is the parent organization of the Financial Accounting Standards Board (FASB) and the Governmental Accounting Standards Board (GASB).

“Together with the Board of Trustees, I am pleased to welcome Tim, Lynnette, Rick, Sarah, and Robin,” said FAF Chair Kathleen L. Casey. “Their varied backgrounds, experience, and skill sets will ensure a continued diversity of perspective, which is critical for the FAF in directing the appropriate stewardship of the FASB and GASB in carrying out their standard-setting missions.”

The new appointees will fill vacancies left by retiring members Charles M. Allen, Christine M. Cumming, Eugene Flood Jr., Kenneth B. Robinson, and Diane M. Rubin whose terms conclude on December 31, 2020.

“On behalf of the FAF, I want to acknowledge the contributions of Chuck, Christine, Gene, Ken, and Diane and thank them for their dedication and service. I would like to also extend an additional note of appreciation to Christine for her service as secretary and treasurer and to Diane for her role as vice chair,” noted Ms. Casey.

Below are brief biographical sketches of the appointees:

Timothy L. Christen is the Chairman of the Board of Baker Tilly International Ltd. He has over 30 years of experience in the public accounting profession including serving as Chairman of the AICPA. Tim most recently served as Chairman and CEO of Baker Tilly US LLP, a role that he held between 1998 and 2016. He is currently serving as a member of several additional boards, including CPA.com, a subsidiary of the AICPA, where he serves as Chairman of the Compensation and Audit Committees, privately held Sub-Zero Group, and NYSE listed Mayville Engineering Company where he serves as Chairman of the Audit Committee and member of the Nominations and Governance Committee. He has also been recognized as one of the “100 Most Influential People in Accounting Profession” by Accounting Today and was included on the list of “Most Admired US Managing Partners” by Inside Public Accounting.

Lynnette Kelly is the former President and Chief Executive Officer of the Municipal Securities Rulemaking Board (MSRB). She has over 30 years of business, legal, regulatory, compliance, and technology experience in the fixed income markets. During her tenure at MSRB, she increased the level of transparency in the municipal securities market with her oversight of the launch of the MSRB’s Electronic Municipal Market Access (EMMA) website, which is the official source of municipal market data and documents. Ms. Kelly is NACD Directorship Certified and sits on the board for the University of Chicago Harris School of Public Policy Center for Municipal Finance and for Caretech Inc. Ms. Kelly is also involved with various charitable organizations that provide educational opportunities to disadvantaged students including the Bishop John T. Walker School for Boys, the CUES schools in Omaha, Nebraska, the Washington, D.C. Professional Enrichment Academy, and the Economic Club of Washington, D.C.

Richard N. Reisig is the Chief Executive Officer for Anderson ZurMuehlen & Company, P.C. He has over 38 years of experience as an auditor and consultant on accounting, tax, and financial reporting issues working for private companies, not-for-profits, and local governmental entities. He has had extensive involvement in standard-setting, including as a member of the FASB’s Private Company Council and in various leadership roles with the AICPA and National Association of State Boards of Accountancy (NASBA). He has served on the Montana Board of Public Accountants including two appointments as Chair. Mr. Reisig received the George D. Anderson Distinguished Service Award from the Montana Society of CPAs and was elected to leadership roles on various civic and community boards, including Special Olympics of Montana and for multiple entities for Montana State University. He currently serves as the at-large Director for the NASBA.

Sarah E. Smith is the former Chief Compliance Officer and Chief Accounting Officer for Goldman Sachs Group, Inc., where she currently serves as a Senior Advisor. She has over 40 years of experience in the accounting and auditing profession, including nearly 25 years with Goldman Sachs Group, where she was a long-term member of the Management Committee. She also served on several Goldman Sachs committees including the Reputational Risk Committee, Client and Business Standards Committee, Investment Policy Committee, Risk Committee, and the Steering Committee on Regulatory Reform. Ms. Smith is a member of the Institute of Chartered Accountants in England and Wales and attended City of London University.

Robin L. Washington is the former Executive Vice President and Chief Financial Officer for Gilead Sciences, Inc. She has over 30 years of experience as a preparer of financial statements, with wide-ranging experience across the healthcare and technology sectors. Ms. Washington currently serves on multiple corporate boards, including Alphabet Inc., the parent company of Google, Inc., Honeywell International Inc., and Salesforce.com. Ms. Washington also serves on multiple non-profit boards including the University of California, San Francisco Benioff Children's Hospital of Oakland, the University of Michigan Presidents Council, and Ross Business School Advisory Board, as well as the Graziadio School of Business and Management at Pepperdine University.

A complete list of the Board of Trustee members can be found at www.accountingfoundation.org/trustees.

BDA Policy Brief: Post Election Update on GSE Reform

Fixed Income – Insights: BDA Policy Brief – Post Election Update on GSE Reform

BOND DEALERS OF AMERICA

NOVEMBER 19, 2020

BDA Washington Weekly: Lame Duck Session Begins

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November 20, 2020

GASB Proposes New Implementation Guidance to Assist Stakeholders with Application of its Pronouncements.

Norwalk, CT, November 17, 2020 — The Governmental Accounting Standards Board (GASB) today proposed implementation guidance in the form of questions and answers intended to clarify, explain, or elaborate on certain GASB pronouncements.

The Exposure Draft, *Implementation Guidance Update—2021*, contains proposed new questions and answers that address application of GASB standards on leases, fiduciary activities, and other topics. The Exposure Draft also proposes amendments to previously issued implementation guidance.

The GASB periodically issues new and updated guidance to assist state and local governments in applying generally accepted accounting principles (GAAP) to specific facts and circumstances that they encounter. The GASB develops the guidance based on:

- Application issues that are raised during due process on GASB Statements
- Questions it receives throughout the year, primarily from governments and auditors, and
- Topics identified by members of the Governmental Accounting Standards Advisory Council and other stakeholders.

The guidance in Implementation Guides is cleared by the Board and constitutes Category B GAAP.

The Exposure Draft is available on the GASB website, www.gasb.org. The GASB encourages stakeholders to review the proposal and provide comments by February 15, 2021. Information about how to comment can be found at the front of the Exposure Draft.

Real-Time Financial Reporting Improves Muni Bond Markets.

A team of researchers from the UO Department of Finance found three-fold benefits when the gap in trade reporting in municipal bond markets changed from a full day to fifteen minutes after implementation of the Real-Time Transaction Reporting System.

Their findings demonstrate that municipalities can benefit from the real-time reporting system through more efficient capital markets, creating benefits for society because municipal bond offerings fund infrastructure investments that often improve quality of life, education and public safety.

In "The Difference a Day Makes: Timely Disclosure and Trading Efficiency in the Muni Market," which was published online ahead of print in the Journal of Financial Economics, the authors John Chalmers and Z. Jay Wang, professors of finance in the Lundquist College of Business at the University of Oregon, and Steve Yu Liu, who earned a doctorate at the UO and is now with the Department of Business and Information Technology at the Missouri University of Science and Technology, assess the reporting system's impact on muni markets.

By assessing data surrounding the time that Real-Time Transaction Reporting System was implemented, the study demonstrates how real-time price discovery has transformed municipal bond trading, investing and, potentially, the cost of financing civic projects. The researchers argue that faster and more accurate disclosure in the $4 trillion over-the-counter municipal bond market leads to efficiencies that are likely to benefit investors, issuers and ultimately taxpayers.

"First, we find a significant reduction in transaction costs that varies with investor sophistication," they wrote in the paper. "Second, we find significant increases in municipal trading volume across the liquidity spectrum. Third, we find that dealers increased market-making activities after the introduction of the Real-Time Transaction Reporting System."

An alternative explanation for the findings, they noted, is that they could reflect overall improvement in access to information in over-the-counter markets due to the increased use of online resources in the period surrounding the implementation of the real-time reporting system. To address this concern, the authors selected a subset of corporate bonds as a control group.

These corporate bonds were not subject to similar changes in disclosure requirement in the sample period and should have captured the impact of common improvements to the over-the-counter markets. By comparing the changes in trading costs between the municipal bonds and the control group, the authors were able to isolate the effects of Real-Time Transaction Reporting System, apart from other factors.

More timely disclosure in the municipal bond markets was a particular boon to investors, with the average trading costs declining by 30 basis points or 14 percent. Interestingly, they noted, the impact of the real-time reporting varies significantly across investor sophistication. While retail investors benefited mainly from a reduction in dealer's costs of intermediating trades, sophisticated traders were able to take advantage of more timely trading information and negotiate better trading terms with dealers, reflecting improved bargaining positions.

The authors also studied the impact of the reporting system on bond dealers' market making activities. They find an increase in trading volume for all bond liquidity groups sorted by pre-RTRS trading volume. Consistent with this, the researchers found, dealers committed more capital and were more actively engaged in intermediating municipal bond trading in the post-RTRS period. These findings alleviate concerns that bond dealers may decrease market-making efforts due to deteriorating bargaining positions.

While switching to real-time reporting incurs additional costs, the research suggests that the sacrifices are likely to be well worth it for both investors and bond dealers. Further, by taking costs out of the system and improving investor welfare, municipalities benefit.

—By Michael Maiello, for the Lundquist College of Business

November 11, 2020

GFOA Working Group Focusing on Libor Transition.

The Government Finance Officers Association has formed a working group to help issuers prepare for the phase-out of Libor at the end of 2021.

The group of around a dozen issuers, bankers, broker-dealers, bond attorneys, and municipal advisors will meet Tuesday for their second time to sort out their priorities for educating the public finance community.

"We're all looking at it from our different perspectives at what we can do in our respective roles to get the word out about the Libor transition and that the issuers who have that exposure are aware of it," said Cindy Harris, chief financial officer of the Iowa Finance Authority who is chairing the working group.

The working group plans to meet every other week to develop instructions to guide participants in the municipal bond market to make the transition.

“I feel that the Libor transition is probably not on the top of people’s minds,” said Harris, “Even if they have Libor they may think it’s not as pressing a matter to deal with than a lot of the other challenges they are having to deal with in their jurisdiction. That’s why I think it’s good to get the word out that this is coming sooner than people may think. If you are changing contracts, you may need board approvals to do that. And that may need a month or two of lead time.”

The International Swaps and Derivatives Association announced Oct. 23 its IBOR Fallbacks Supplement and IBOR Fallbacks Protocol.

“While fallbacks aren’t designed to be a primary means of transitioning from Libor and other IBORs, they do mean a critical safety net will be in place for those participants that still have exposure to IBORs when a cessation or non-representativeness announcement is made,” ISDA General Counsel Katherine Tew Darras said in a speech Monday.

ISDA said the supplement amends its standard definitions for interest rate derivatives to incorporate robust fallbacks for derivatives linked to certain IBORs, with the changes coming into effect on January 25, 2021. From that date, all new cleared and non-cleared derivatives that reference the definitions will include the fallbacks.

“During this period the fee is free for non-primary dealers,” said Harris. “After January 25, new transactions will automatically contain the fallback language via the supplement. However, adherence to the protocol after January 25 for legacy contracts will incur the $500 fee. To avoid the fee, issuers can also execute bilateral amendments.”

The $500 fee applies to each legal entity unless they have agency authority.

Additionally, ISDA said the protocol will enable market participants to incorporate the revisions into their legacy non-cleared derivatives trades with other counterparties that choose to adhere to the protocol. The protocol has been open for adherence since the Oct. 23 date of the announcement and also becomes effective on Jan. 25 with the supplement.

By the end of next month, the United Kingdom’s Financial Conduct Authority is expected to officially declare Libor as nonrepresentative, which will establish an endpoint for this reference rate.

Harris said the endpoint will be used as a reference date for establishing a five-year lookback for a new reference rate.

“The announcement date will determine the five-year median window for purposes of calculating the fallback rate spread adjustment,” Harris said. “The spread adjustment is based on the median five-year historical difference between LIBOR and SOFR compounded over each corresponding period.”

Harris said GFOA is likely to advise issuers to consult with their swap advisor or qualified independent representative (QIR) to help them navigate that transition.

Harris said she intends to have her swap advisor perform a historical five-year regression of the Secured Overnight Financing Rate (SOFR) plus the spread for Libor and a separate calculation using the SIFMA rate as an alternative.

“GFOA will ramp up its effort to get the word out about Libor,” she said. “The industry will also try to get together some guiding principles and not create new resources, but to aggregate them.”

The group also wants to make the resources understandable to issuers who may only have used Libor occasionally and aren’t familiar with the terminology.

In addition, the GFOA debt committee has a subgroup that reviewing GFOA's best practices to determine is any updates are needed.

By Brian Tumulty

BY SOURCEMEDIA | MUNICIPAL | 11/10/20 01:43 PM EST

[Hawkins Advisory: Rev. Proc. 2020-44, Advance Guidance for Certain Transitions from IBORs]

The Treasury Department and the Internal Revenue Service have provided advance guidance in Rev. Proc. 2020-44 to allow the implementation of fallback regimes developed by the Alternative Reference Rate Committee and the International Swaps and Derivatives Association to facilitate the orderly transition away from interbank offered rates in certain contracts. This transition is expected to occur at the end of 2021 in accordance with the announcement made by the Financial Conduct Authority, which regulates and oversees the London Interbank Offered Rate. To the extent a contract is modified in accordance with such fallback regimes, under Rev. Proc. 2020-44 the modification will not result in a taxable event to either the investor or the issuer.

The attached Hawkins Advisory describes the provisions of Rev. Proc. 2020-44 as they apply to issuances of tax-exempt bonds.

[Read the Hawkins Advisory.]

[MSRB Compliance Corner: Fall 2020]

[Read the Newsletter.]

[MSRB Seeks Board of Directors Applicants.]

Washington, DC – The Municipal Securities Rulemaking Board (MSRB), the self-regulatory organization established by Congress to safeguard the $4 trillion municipal securities market, will solicit applications for four positions on its Board of Directors for the 2022 fiscal year. Selected candidates will be elected to four-year terms beginning October 1, 2021, where they will have the opportunity to oversee the organization's strategic initiatives to support an evolving market through effective regulation, modernized technology and big data.

"Our goal is to create a Board that is diverse, inclusive and reflective of the wide variety of perspectives that contribute to the field of public finance. To help encourage individuals to apply, we are soliciting applications earlier and keeping the application window open for longer than in prior years," said Board member Caroline Cruise. Cruise serves as chair of the Board's Nominating Committee, which is focused exclusively on the nominating process for new members now that the Board has split its Nominating and Governance Committee into two separate committees.

The Board is charged with setting regulatory policy, authorizing rulemaking, enhancing market transparency systems and overseeing operations for the organization. The Board is currently overseeing MSRB strategic initiatives that include modernizing the MSRB Rule Book to reduce compliance burdens; modernizing and enhancing the free Electronic Municipal Market Access (EMMA®) website and related market transparency systems; and delivering value to the municipal market through data. Board members are compensated for their service.

Board Composition

The FY 2022 Board will have 15 total members as the Board transitions to a smaller size. The reduced size of the Board is one of several significant governance enhancements developed during the Board's special review of governance in FY 2020, which also resulted in tightened standards of independence for public members and a lifetime service limit for Board members. [MSRB Rule A-3] outlines requirements for all applicants to the Board, including specific eligibility requirements to serve as a public or regulated Board member.

The Board will elect two public and two regulated representatives to join a Board that will consist of eight members who are representatives of the public, including investors, municipal entities and other individuals not regulated by the MSRB and seven members from firms that are regulated by the MSRB, including representatives of broker-dealers, bank dealers and non-dealer municipal advisors. With respect to the two public member positions, the MSRB is particularly interested in individuals employed by state and local issuers. With respect to the two regulated member positions, the MSRB is required to select at least one municipal advisor who is not affiliated with a broker-dealer or bank dealer firm.

Qualified individuals representing the diversity of the country and a broad array of market perspectives and organizations are encouraged to apply for membership on the Board. All applicants must be knowledgeable of matters related to the municipal securities market.

Application Details

The application form will become available on the MSRB Board of Directors Application portal beginning December 1, 2020 and accepted through February 5, 2021. [Download a copy of the application form for reference.] Additional details on the Board application process are available on the MSRB's website [here]. Questions regarding the application and selection process should be directed to Sara Ahmadzai, Senior Manager, Corporate Governance and Board Administration, at 202-838-1341 or sahmadzai@msrb.org.

Date: November 12, 2020

Contact: Leah Szarek, Interim Chief External Relations Officer
202-838-1500
lszarek@msrb.org

[8 Big Banks in Murky Waters, To Face U.S. Cities' Allegations.]

Eight big banks in the United States are likely to be sued in a class action lawsuit filed by Philadelphia and Baltimore, per Reuters. Per U.S. District Judge Jesse Furman in Manhattan, the cities are permitted to move on with anti-trust claims against banks suing over their marketing of variable-rate demand obligations (VRDOs) from 2008 through 2016.

Allegations

Per the cities' allegations, eight banks, including affiliates of Bank of America BAC, Barclays Plc BCS, Citigroup C, Goldman Sachs GS, JPMorgan JPM, Morgan Stanley MS, Royal Bank of Canada RY and Wells Fargo WFC, have conspired and forced state and local governments for paying higher interest rates on a particular type of tax-exempt municipal bond — VRDOs.

Further, Philadelphia and Baltimore claimed that the colluded move reduced the available funds for hospitals, power and water supplies, schools, transportation and other essential municipal services.

With short-term interest rates, VRDOs are long-term bonds which are reset weekly. Moreover, early redemption is allowed for investors, while banks need to re-market these bonds at the lowest possible rates to other investors.

These banks have been alleged of sharing proprietary information related to bond inventories and colluded rate changes leading to deterred redemptions. Furthermore, banks succeeded to charge millions of dollars in remarketing and service fees for "effectively doing nothing" on this move.

Notably, Philadelphia and Baltimore issued $1.67 billion and $261 million of VRDOs, respectively.

In his decision, Furman said the cities offered "reason to believe that defendants stood to gain by participating in the rate-fixing scheme and that the scheme was possible only with defendants' coordinated efforts."

No comments have been received from the banks' spokespersons. Lawyers for the plaintiffs also had no immediate comment.

Conclusion

Amid the coronavirus pandemic-induced economic slowdown, which has dampened financials of all sectors, banks have come under the purview of new allegations. A landmark judgment should be specifically put forward to terminate such collusions and shrewd practices in the future, bring justice to the sufferers, and punish the wrongdoers. While the settlement of the issues will put to rest investigations and bring reprieve to the banks, this comes as a huge blow to their financials.

Yahoo Finance

by Priti Dhanuka

November 3, 2020

Judge Allows Cities' Class Action Over Bond Rate Conspiracy to Proceed.

A federal judge has allowed to proceed a class action antitrust suit filed against eight banks for conspiracy to fix rates on tax-exempt municipal bonds.

On November 2 Judge Jesse M. Furman of the U.S. District Court for the Southern District of New York denied the banks' motions to dismiss in *City of Philadelphia v. Bank of America Corp.*

The class action complaint filed by the cities of Philadelphia and Baltimore alleges that the banks — Bank of America, JPMorgan Chase, Wells Fargo, Citigroup, Barclays, Goldman Sachs, Morgan

Stanley, and the Royal Bank of Canada — conspired not to compete against each other and to set, almost daily, artificially high interest rates on state and local municipal bonds between 2008 and 2016. The artificially high rates were estimated to be around 75 percent above what the plaintiffs would have otherwise paid, costing governments, schools, hospitals, and charities potentially billions of dollars, according to the complaint.

The alleged conspiracy surrounds the issuance of variable rate demand obligations (VRDOs), which are tax-exempt bonds with interest rates reset periodically, typically weekly. Bond issuers contract with banks as remarketing agents (RMAs) that are required to seek the lowest possible rates when selling bonds on behalf of the borrowers when the rates are reset or when an investor redeems a bond. If a rate is too high above the market, a bond issuer may find a new RMA to secure lower rates, and the bank loses a client. If the rate was set too low, bondholders would redeem their bonds and the RMAs would incur the costs of remarketing the bonds or holding them on their books.

The cities cite testimony from a former managing director at Citigroup, former senior RMA personnel at JPMorgan, and a former RMA at Wells Fargo who claim that communications between the banks happened regularly by telephone, in-person meetings, and Bloomberg messaging technology.

“A former senior RMA official at JPMorgan confirmed that it was a ‘dirty little secret’ that RMAs would talk to each other about rates and would ask other RMAs questions like, ‘Are you placing this paper’ — referring to a particular VRDO — ‘and if so, what will be the rate?’,” Furman wrote in his opinion.

The cities also cite statistical evidence supporting their argument. The issue was first raised by a whistleblower, which prompted an investigation and subpoenas from the SEC and the Department of Justice in 2015 and 2016.

The cities analyzed the bond interest rates between 2008 and 2016 and found that the rates set by different banks clustered around each other during those years and diverged following the SEC and Justice Department subpoenas. The results of a regression model showed that the rates were nearly 75 percent higher than they would have been otherwise, according to the cities.

The class action suit states that there are thousands of members of the class throughout the country that were affected by the coordination between the banks.

The lawsuit was initially set in motion by Minneapolis-based municipal adviser Johan Rosenberg, who filed false claims act lawsuits in Illinois, Massachusetts, and California and was first identified by The Bond Buyer.

A pretrial conference is set for December 17.

In *City of Philadelphia v. Bank of America Corp.* (No. 19-01608), Philadelphia is represented by attorneys from Wollmuth Maher & Deutsch LLP; Quinn Emanuel Urquhart & Sullivan LLP; and Susman Godfrey LLP. Baltimore is represented by Susman Godfrey LLP. Bank of America Corp. and Merrill Lynch are represented by Wilmer Cutler Pickering Hale and Dorr LLP. Barclays Bank is represented by Skadden, Arps, Slate, Meagher & Flom LLP. Citigroup is represented by Paul, Weiss, Rifkind, Wharton & Garrison LLP. Goldman Sachs is represented by Winston & Strawn LLP. JPMorgan Chase is represented by Covington & Burling LLP. The Royal Bank of Canada is represented by O’Melveny & Myers LLP. Wells Fargo is represented by Jones Day. BMO Financial Group is represented by Katten Muchin Rosenman LLP.

TAX ANALYSTS

BY AARON DAVIS

11/5/2020

EMMA Advanced Search Features.

The EMMA website's advanced search may feature more options than you know. Filters include bond insurance status, credit rating by rating agency, sector and more.

Explore advanced search.

GASB Outlook E-Newsletter Fall 2020.

Read the Newsletter.

SEC Proposes Exemptive Relief From Broker Registration for Finders for Small Companies.

On October 7, 2020, the Securities and Exchange Commission (SEC) proposed to address long-standing questions regarding the applicability of the broker registration requirements to finders for small and emerging businesses.1 Identifying potential investors is one of the most difficult challenges for small businesses trying to raise capital, and finders can play an important role in facilitating small-business capital formation. However, regulatory uncertainty regarding the broker registration requirements for finders has hampered the ability of small companies to make use of finders' services. Responding to the many calls for the SEC to address this lack of clarity, the SEC proposes to grant exemptive relief to permit natural persons to engage in limited activities on behalf of issuers (Finders) without registering as brokers under Section 15 of the Securities Exchange Act of 1934 (Exchange Act). The proposed exemption is intended to provide issuers with greater access to investment capital subject to appropriate investor protections, and to establish clear lanes for both registered broker activity and limited activity by Finders who would be exempt from registration. The SEC has requested comment on the proposed exemption by November 12, 2020.

Proposed Exemptions for Tier I Finders and Tier II Finders

The SEC proposes to exempt from broker registration two classes of Finders: Tier I Finders and Tier II Finders. The proposed exemption for both Tier I and Tier II Finders would be available only when the following seven conditions are met:

- The issuer is not required to file reports under Section 13 or Section 15(d) of the Exchange Act; The issuer is seeking to conduct the securities offering in reliance on an applicable exemption from registration under the Securities Act of 1933 (Securities Act);
- The Finder does not engage in general solicitation;
- The potential investor is an "accredited investor" as defined in Rule 501 of Regulation D, or the

Finder has a reasonable belief that the potential investor is an "accredited investor";
- The Finder provides services pursuant to a written agreement with the issuer that includes a description of the services provided and associated compensation;
- The Finder is not an associated person of a broker-dealer as defined under Section 3(a)(18) of the Exchange Act; and
- The Finder is not subject to statutory disqualification, as that term is defined in Section 3(a)(39) of the Exchange Act, at the time of his or her participation.

Tier I Finders

A Tier I Finder would be defined as a Finder who meets the relevant conditions above and whose activity is limited to providing contact information of potential investors with only one capital-raising transaction by a single issuer within a 12-month period,2 provided the Tier I Finder does not have any contact with the potential investors about the issuer. The contact information may include, among other things, name, telephone number, email address and social media information. Limiting the exemption to this activity is intended to narrow the role of the Tier I Finder to preclude the participation in continuous or multiple sales of securities by persons who are not subject to broker-dealer registration. A Tier I Finder who complies with all the conditions of the exemption may receive transaction-based compensation for the limited broker-dealer services described above without being required to register as a broker under Section 15(a) of the Exchange Act.

Tier II Finders

The SEC also proposes an exemption for Tier II Finders that would permit Tier II Finders to engage in additional solicitation-related activities beyond those permitted for Tier I Finders. A Tier II Finder is defined as a Finder who meets the relevant conditions above and who engages in solicitation-related activities on behalf of an issuer that are limited to (i) identifying, screening and contacting potential investors; (ii) distributing issuer offering materials to investors; (iii) discussing issuer information included in any offering materials, provided that the Tier II Finder does not provide advice as to the valuation or advisability of the investment; and (iv) arranging or participating in meetings with the issuer and investor.3 The SEC generally views solicitation as any affirmative effort to induce or attempt to induce a securities transaction and broadly views these activities of Tier II Finders to constitute solicitation. The SEC states that limiting the proposed exemption to these specified activities associated with solicitation, along with the additional conditions set forth below, is intended to narrow the role of the Tier II Finder to support the proposed exemption.

A Tier II Finder wishing to rely on the proposed exemption also would need to satisfy certain disclosure requirements and other conditions.4 First, the Tier II Finder would need to provide a potential investor, prior to or at the time of the solicitation, disclosures that include:

- the name of the Tier II Finder;
- the name of the issuer;
- the description of the relationship between the Tier II Finder and the issuer, including any affiliation;
- a statement that the Tier II Finder will be compensated for his or her solicitation activities by the issuer and a description of the terms of such compensation arrangement;
- any material conflicts of interest resulting from the arrangement or relationship between the Tier II Finder and the issuer; and
- an affirmative statement that the Tier II Finder is acting as an agent of the issuer, is not acting as an associated person of a broker-dealer and is not undertaking a role to act in the investor's best interest.

The SEC proposes to allow a Tier II Finder to provide the above disclosures orally, provided that the oral disclosure is supplemented by written disclosure no later than the time of any related investment in the issuer's securities. The written disclosures can be provided through either paper or electronic means.

Second, the Tier II Finder also must obtain from the investor, prior to or at the time of any investment in the issuer's securities, a dated written acknowledgment of receipt of the Tier II Finder's required disclosures. The written acknowledgment may be provided through either paper or electronic means.

A Tier II Finder who complies with all the conditions of the proposed exemption may receive transaction-based compensation for services provided in connection with the activities described above without being required to register as a broker under Section 15(a) of the Exchange Act.

Prohibited Activities for Finders

The proposed exemption would apply only with respect to the defined activities for each tier of Finder and is limited to activities solely in connection with primary offerings. A Finder could not rely on this proposed exemption to engage in broker activity beyond the scope of the proposed exemption. For example, a Finder could not:

- be involved in structuring the transaction or negotiating the terms of the offering;
- handle funds or securities or bind the issuer or investor;
- participate in the preparation of any sales materials;
- perform any independent analysis of the sale;
- engage in any "due diligence" activities;
- assist or provide financing for such purchases; and
- provide advice as to the valuation or financial advisability of the investment.

Safe Harbor

The proposed exemption would provide a nonexclusive safe harbor from broker registration for Tier I and Tier II Finders. No presumption would arise that a person has violated Section 15(a) of the Exchange Act if such person is not within the terms of the proposed exemption. Consistent with how questions under Section 15(a) have been evaluated, whether a person is acting as a "broker" and in particular, whether he or she is "engaged in the business" of effecting securities transactions for the account of others will depend on the facts and circumstances of the particular matter. Accordingly, engaging in some of the limited activities falling within the terms of the proposed exemption should not be considered per se to require registration as a broker-dealer if all the requirements of the exemption are not met.

Other Applicable Laws

The proposed exemption would not affect a Finder's obligation to continue to comply with all other applicable laws, including the antifraud provisions of the Securities Act and the Exchange Act, such as the obligations under Section 10(b) and Rule 10b-5 under the Exchange Act, and state law. In addition, the proposed exemption is not intended to affect the rights of the SEC or any other party to enforce compliance with other applicable law, or the available remedies for violations of the law. Further, regardless of whether or not a Finder complies with this exemption, that Finder may need to consider whether he or she is acting as another regulated entity, such as an investment adviser or a municipal advisor. An exemption from the obligation to register as a broker-dealer does not insulate a person from the registration requirements of the Investment Advisers Act of 1940 if such person is acting as an investment adviser.

Request for Comment

The SEC posed 45 specific questions regarding the proposed exemption. In addition to requests for comments on the various aspects of the proposal, the SEC inquired more broadly as to whether there are other areas in which the SEC should provide guidance regarding the applicability of broker-dealer registration requirements to other types of limited-purpose broker-dealers. The SEC also asked whether any staff no-action letters should or should not be withdrawn if the proposed exemption is adopted. Moreover, the SEC asked whether the proposed exemption would have a competitive impact on registered broker-dealers.

Footnotes

1. Securities Exchange Act Release No. 90112 (Oct. 7, 2020), 85 Fed. Reg. 64542 (Oct. 13, 2020) (available at https://www.sec.gov/rules/exorders/2020/34-90112.pdf).
2. The SEC noted that this requirement is similar to the limitation included in Rule 3a4-1 for sales activities by associated persons of an issuer. See Rule 3a4-1(a)(4)(ii)(C) under the Exchange Act (stating that as a condition of the rule, subject to limited exceptions, the associated person of an issuer cannot participate in selling and offering of securities for any issuer more than once every 12 months).
3. A Tier II Finder is not subject to the Tier I Finder's limitation of participating in only one capital-raising transaction by a single issuer in a 12-month period.
4. The disclosure requirements and conditions applicable to Tier II Finders differ from the requirements applicable to solicitors under the SEC's proposed amendments to Rule 206(4)-3 under the Investment Advisers Act of 1940, the Cash Solicitation Rule. See Investment Advisers Act Release No. 5407 (Nov. 4, 2019), 84 Fed. Reg. 67518 (Dec. 20, 2019). The SEC stated that these differences reflect the particular facts and circumstances surrounding the proposed permitted activities for Finders and solicitors, and the characteristics of the applicable regulatory regimes, notably that a solicitor would solicit for an investment adviser and would be subject to oversight by such investment adviser, while a Finder would solicit for an issuer and therefore would not be subject to such oversight.

Wilmer Cutler Pickering Hale and Dorr LLP – Andre E. Owens and Cherie Weldon

October 28, 2020

Goldman, Citi, BofA, Others to Face Muni Bond Price-Fixing Suit.

- **Accuses banks of illegal coordination about price, inventory**
- **Adequately alleges collusion through 'thinly coded questions'**

Bank of America, Citigroup, JPMorgan, Goldman Sachs, and other top banks must face claims that they conspired to fix the price of "variable rate demand obligations," a type of municipal infrastructure bond that can be redeemed at short-term interest rates that are reset weekly, a federal judge in Manhattan ruled Monday.

"Prior to resetting the VRDO interest rates, the banks routinely" shared "their base rates, inventory levels, and planned rate changes," using "thinly coded questions" to coordinate and "ensure that none of them broke ranks," Judge Jesse M. Furman wrote.

Those exchanges reflect "the kinds of forward-looking, price-bearing communications that can support an inference that there was a conspiracy to fix prices," the judge said.

In addition to BofA, Citi, JPMorgan, and Goldman, the proposed class action targets affiliates of Barclays, Morgan Stanley, the Royal Bank of Canada, and Wells Fargo. It's consolidated in the U.S. District Court for the Southern District of New York, where it's being led by the city governments of Philadelphia and Baltimore.

The lawsuit accuses the banks of colluding with one another in an effort to get higher rates for the VRDO bonds than they pledged to in their "remarketing" agreements with the cities that issued them.

The contracts required the banks to set the lowest interest rate that the market would bear. Their scheme was aimed at letting them fix higher rates without being replaced by the issuing cities, which would have found cheaper remarketers in the absence of collusion, the suit says.

The illegal coordination allegedly came to light after the Securities and Exchange Commission and the Justice Department launched investigations in 2015 and 2016, respectively, based on a whistleblower complaint.

The case is *City of Philadelphia v. Bank of Am. Corp.*, S.D.N.Y., No. 19-cv-2667, 11/2/20.

Bloomberg Law

Nov. 2, 2020

To contact the reporter on this story: Mike Leonard in Washington at mleonard@bloomberglaw.com

To contact the editor responsible for this story: Rob Tricchinelli at rtricchinelli@bloomberglaw.com

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Eight Big Banks Must Face U.S. Cities' Allegations of Municipal Bond Collusion.

NEW YORK (Reuters) – A federal judge on Monday said Philadelphia and Baltimore may sue eight big banks for allegedly conspiring to force state and local governments to pay inflated interest rates on a popular type of tax-exempt municipal bond.

U.S. District Judge Jesse Furman in Manhattan said the cities may pursue antitrust claims in the proposed class action over the banks' marketing of variable-rate demand obligations, once a more than $400 billion market, from 2008 to 2016.

Philadelphia and Baltimore said the collusion reduced available funding for hospitals, power and water supplies, schools, transportation and other essential municipal services.

The defendants included affiliates of Bank of America Corp, Barclays Plc, Citigroup Inc, Goldman Sachs Group Inc, JPMorgan Chase & Co, Morgan Stanley, Royal Bank of Canada and Wells Fargo & Co.

VRDOs are long-term bonds with short-term interest rates that typically reset weekly. Investors may redeem the bonds early, and banks must remarket those bonds to other investors at the lowest possible rates.

Philadelphia and Baltimore, which issued a respective $1.67 billion and $261 million of VRDOs, accused the banks of sharing proprietary information about bond inventories and planned rate changes.

They said this dissuaded redemptions, and enabled the banks to charge hundreds of millions of dollars in remarketing and service fees for “effectively doing nothing.”

In his 34-page decision, Furman said the cities offered “reason to believe that defendants stood to gain by participating in the rate-fixing scheme and that the scheme was possible only with defendants’ coordinated efforts.”

Furman also said six of the banks must face breach of contract claims. He dismissed all claims of unjust enrichment.

Spokespeople for the banks declined to comment or had no immediate comment. Lawyers for the plaintiffs had no immediate comment.

The VRDO market exceeded $400 billion in 2009 but has shrunk. S&P Global Ratings recently rated $144.9 billion of the securities.

The case is Philadelphia et al v Bank of America Corp et al, U.S. District Court, Southern District of New York, No. 19-01608.

By Jonathan Stempel

NOVEMBER 2, 2020

Reporting by Jonathan Stempel in New York; Editing by Marguerita Choy

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MSRB Seeks Volunteers for Board Advisory Groups.

Washington, DC – The Municipal Securities Rulemaking Board (MSRB) today announced that it is seeking volunteers for two Board advisory groups for FY 2021: the Compliance Advisory Group (CAG) and the Municipal Fund Securities Advisory Group (MFSAG). In addition, the MSRB is requesting input on potential topics for these advisory groups to take up in FY 2021.

“A particularly impactful way municipal market stakeholders can engage with the MSRB is by serving on one of the Board’s advisory groups,” said Seema Mohanty, Chair of the Board’s Stakeholder Engagement Committee. “For several years, the Board has benefited from the diverse market perspectives and expertise of the members of our advisory groups, and we encourage market stakeholders to volunteer to serve on one of the two FY 2021 groups.”

- **Compliance Advisory Group**
  The MSRB originally established CAG in FY 2018 to provide additional outside expertise and input to the Board to help inform the organization’s long-term strategic goal to facilitate industry understanding of and compliance with MSRB rules.

- **Municipal Fund Securities Advisory Group**
  In FY 2019, the MSRB established MFSAG to provide input to the Board on municipal market rules, practices, transparency, and education related to 529 savings plans and Stephen Beck, Jr., Achieving a Better Life Experience Act of 2014 (ABLE) programs.

The MSRB is now seeking qualified individuals from around the country representing diverse market perspectives and organizations to volunteer for its FY 2021 CAG and MFSAG. The MSRB will accept volunteer submissions through December 15, 2020. In addition, interested individuals are invited to recommend topics they believe the Board's advisory groups should consider addressing in FY 2021.

Learn more about volunteering for FY 2021 CAG and MFSAG and suggesting topics.

Date: October 23, 2020

Contact: Leah Szarek, Interim Chief External Relations Officer
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IRS Releases Guidance on the Transition From LIBOR: Ballard Spahr

The IRS recently released helpful guidance in Revenue Procedure 2020-44 to assist the market's transition from the London Interbank Offered Rate (LIBOR) and other interbank offered rates (IBORs) to alternative reference rates. LIBOR is set to be phased out after the end of 2021.

The Upshot

- The Revenue Procedure provides that the adoption of certain fallback language recommended by the Alternative Reference Rates Commission (ARRC) and the International Swaps and Derivatives Association (ISDA) for contracts with terms referencing an IBOR will not result in a reissuance. The guidance further provides that such modifications will also not be treated as a termination of a qualified hedge or as a disposition or termination of either leg of a hedge transaction. The relief provided by the Revenue Procedure is effective for modifications to contracts occurring on or after October 9, 2020, and before January 1, 2023, but may be relied on for modifications to contracts occurring before October 9, 2020.
- The guidance applies to any of the following modifications:
- The contract is modified to incorporate ISDA Fallback (as that term is defined in Rev. Proc. 2020-44, section 3.02), regardless of whether that modification results from adherence to the anticipated ISDA Protocol to be posted by ISDA on its website or a bilateral agreement between the parties to the contract.
- The contract is modified to incorporate an ARRC Fallback (as that term is defined in Rev. Proc. 2020-44, section 3.01).
- The contract is modified to incorporate the terms of either an ARRC Fallback or an ISDA Fallback with certain deviations that fall into one or more of the following categories: deviations that are necessary to make the terms incorporated into the contract legally enforceable in a relevant jurisdiction; deviations from the terms of an ISDA Fallback that are necessary to incorporate the ISDA Fallback into a contract that is not a Protocol Covered Document (as defined in the ISDA Protocol); deviations to omit terms of an ARRC Fallback or an ISDA Fallback that do not affect the way the contract works; and deviations to add, revise, or remove technical, administrative, or operational terms provided the changes are reasonably necessary to adopt the

ARRC Fallback or the ISDA Fallback.

- This additional guidance was published approximately a year after the IRS published proposed regulations on the tax consequences of the transition to the use of reference rates other than IBORs in debt instruments and non-debt contracts. (REG-118784-18; 84 F.R. 54068; October 9, 2019).
- The Revenue Procedure states that Treasury and the IRS concluded that interim guidance in advance of finalizing the proposed regulations was needed to support the adoption of the ARRC Fallback language that had been provided over the last year and the ISDA Protocol.

The Bottom Line

The bond community should expect to see additional guidance in the next year. The recently released guidance signals that the IRS and Treasury may provide additional relief as necessary to address continuing developments in the transition from LIBOR. The IRS has requested comments. Comments should be submitted in writing on or before December 31, 2022.

Ballard Spahr, LLP

October 19, 2020

COVID-19: Weekly Oversight and Enforcement Report - Week of October 22, 2020

A. Congress

1.The Congressional Oversight Commission released its fifth report, which focuses on the Federal Reserve’s Municipal Liquidity Facility (MLF). The MLF was established to help state and local governments better manage cash flow pressures by purchasing short term notes from them.Commission members disagreed on party lines about the extension of the program, pricing, and whether the Federal Reserve should be acting as a lender of last resort during the pandemic.

2. The Wall Street Journal reported that trucking company YRC Worldwide Inc. has drawn down just over one-third of a promised $700 million in coronavirus relief funds and is preparing a spending plan that will require federal approval for more aid. The Congressional Oversight Commission previously expressed concern about the decision to loan money to the company.

3. House Select Subcommittee on the Coronavirus Crisis Chair Jim Clyburn (D-SC) sent letters to four cargo carriers that received a total of more than $630 million from the Treasury Department in the Payroll Support Program, despite reports of the companies’ financial success during the pandemic. Chair Clyburn called on the cargo carriers either to return the money or to demonstrate that they needed the funds to keep workers on the payroll, as Congress intended.

4. Chair Clyburn released six weeks of White House Coronavirus Task Force reports obtained by the Select Subcommittee.

5. The Chair of the House Subcommittee on Coast Guard and Maritime Transportation Sean Patrick Maloney (D-NY) officially requested additional documents from the CDC amid new reporting that the Trump Administration intervened in a decision on when cruise ships can safely resume sailings. Multiple press reports allege the CDC attempted to extend the “No Sail Order” to Feb. 15, 2021, but following White House involvement, the extension was shortened to the end of this month.

6. Sen. Elizabeth Warren (D-MA) formally requested that the SEC and CFTC conduct an insidertrading investigation after reports that Trump Administra tion officials in February privately gave dire warnings to conservative allies and Republican donors about the risks to the economy from the COVID-19 pandemic while President Trump was publicly optimistic about the impact of the virus.

7. At the request of Senators Warren, Gary Peters (D-MI), and Patty Murray (D-WA), the GAO has agreed to conduct an investigation of the Trump Administration's political interference at the CDC and FDA and to determine whether this interference has violated the agencies' scientific integrity and communication policies.

B. Executive Agencies

1. The SEC has released guidance regarding proper accounting practices due to the COVID-19 pandemic.The SEC has made clear that it does not want companies to use non-GAAP measures as window dressing for bad results. Bill Hinman, Director of the Division of Corporation Finance, warned that companies should not try to calculate lost revenue because of the pandemic, saying it was too subjective to quantify. Highlighting pandemic expenses like hazard pay and cleaning expenses via non-GAAP measures, however, would be acceptable, he said.

2. Four individuals in Florida have been arrested and more than $1.2 million in cash has been seized after a joint state and federal investigation into a significant number of fraudulent unemployment insurance and other CARES Act claims. The four individuals are alleged to have orchestrated a complex scheme whereby they used stolen personal identifying information belonging to Rhode Islanders to apply for benefits, and then had those funds directly deposited into accounts created expressly for receiving the fraudulently obtained payments. The funds were allegedly used to purchase a large collection of high-end jewelry and six firearms.

3. Los Angeles-based rapper Fontrell Baines, who goes by the stage name Nuke Bizzle, was arrested on Friday on federal charges of fraudulently applying for over $1.2 million in benefits under the CARES Act. Bains was arrested after releasing a music video on YouTube and Instagram for a song called "EDD," in which he boasts about payments received from the Californ ia Employment Development Department. Music Video.

C. State Attorneys General

No updates this week.

D. Special Inspector General for Pandemic Recovery (SIGPR)

No updates this week.

E. Pandemic Recovery Accountability Committee (PRAC)

No updates this week.

Wilmer Cutler Pickering Hale and Dorr LLP – John F. Walsh, Brendan R. McGuire, Reginald J. Brown, Brian K. Mahanna, Edward C. O'Callaghan, Jeremy Dresner, Michael J.P. Hazel and Rachel Dober

October 22 2020

MSRB Holds First Quarterly Board Meeting of FY 2021.

Washington, DC – The Board of Directors of the Municipal Securities Rulemaking Board (MSRB) met virtually on October 21-22, 2020 for its first meeting of Fiscal Year 2021, where it discussed a transparent and inclusive approach to long-term strategic planning, next steps in its retrospective rule review and other market topics.

Sustained Focus on Board Governance
The Board begins the 2021 fiscal year with 17 members as it transitions to a smaller Board size and implements other significant governance enhancements developed during the Board's special review of governance in FY 2020. To further the Board's focus on governance and the nominating process for new members, the Board has split its Nominating and Governance Committee into two separate committees.

"A standalone Governance Committee ensures a sustained emphasis on upholding the highest standards of Board accountability and transparency," said Board Vice Chair Julia Cooper. "The Nominating Committee will focus on seeking and selecting four new Board members to join the Board for FY 2022." The MSRB actively seeks out new Board members each year and widely advertises the available positions. Read more about the Board member selection process.

Engaging Stakeholders in Strategic Planning
The FY 2021 Board discussed its approach for developing a long-term strategic plan for the organization and its role in an evolving market.

"As the MSRB welcomes Mark Kim as our new CEO to lead the organization into the future, now is the perfect time to renew our vision and chart a new strategy for the coming years. We look forward to engaging with staff and external stakeholders in a transparent and inclusive process to articulate the MSRB's priorities, including how we can realize the potential of the cloud to serve the market of the future," Cooper said.

The MSRB is seeking a firm to provide facilitation and support services for its strategic planning activities.

Board advisory groups are among the ways the Board taps into stakeholder perspectives and expertise. The Board determined to re-establish two advisory groups for FY 2021 – the Compliance Advisory Group and Municipal Fund Securities Advisory Group. The MSRB will solicit volunteers and topics for consideration in the coming weeks.

The Board also plans to seek input from stakeholders on how to enhance the MSRB's approach to developing and delivering education, including via MuniEdPro®, the MSRB's free online learning platform.

Extending COVID-Related Regulatory Relief
The Board discussed the status of the temporary regulatory relief the MSRB provided in April 2020 as the pandemic created widespread operational challenges. The Board determined to provide an additional extension of time for persons acting in the capacity of a municipal advisor principal to become duly qualified with the Municipal Advisor Principal Qualification Examination (Series 54). The MSRB will make a filing with the Securities and Exchange Commission (SEC) to extend the current compliance obligation timeframe to November 12, 2021 from March 31, 2021.

The Board will continue to monitor the need for further temporary regulatory relief.

Advancing Retrospective Rule Review
As part of the MSRB's ongoing retrospective rule review, the Board directed staff to publish a request for comment on codifying existing guidance for solicitor municipal advisors into a new draft rule to define the duties of municipal advisors that, for compensation, solicit municipal entities and obligated persons for business on behalf of certain other financial professionals.

Other Market Structure Topics
The Board received an update on staff's analysis of transaction costs for fixed-rate municipal securities before, during and after the COVID-19 crisis. The MSRB actively monitors transaction costs for investors buying and selling municipal bonds and in May 2020 published initial findings from the period during the height of pandemic-driven volatility. Access the MSRB's COVID-related market data and analysis here.

The Board also discussed providing MSRB data to inform the SEC's recent concept release on whether and how to change the regulatory framework for electronic trading platforms that trade municipal securities. The MSRB's free Electronic Municipal Market Access (EMMA®) website displays a special indicator for inter-dealer trades executed with or using the services of an ATS. The MSRB also publishes a fact sheet that provides data on inter-dealer transaction activity.

Finally, the Board discussed the transition away from LIBOR and to the Secured Overnight Financing Rate (SOFR) as a standard U.S. reference rate in the debt and derivatives market. Read the MSRB's resource about the switch from LIBOR to SOFR.

Date: October 23, 2020

Contact: Leah Szarek, Interim Chief External Relations Officer
202-838-1500
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A Study In Issuer Abuse - The Wisconsin Public Finance Authority.

One of the best institutions ever created for providing public financing to state and local governments is the municipal bond market. It provides an easy and competitive source of funding for governments, both for their own needs as well as for local projects that create jobs and further investments. Its attraction is that it puts investment decisions affecting local economic well being at the local level, not Washington DC, where such decisions can be best made. Sure there is a lot of inefficiency and abuse, but there are also buyers, the SEC, the IRS and state securities authorities to exercise enough constraints to keep abuses in check.

While one could write a book on abuses of taxpayers caused by the reckless use of municipal debt by local officials, I will focus here on the abuses we run across regularly by private purpose users of the municipal market. The vast majority of defaults are in private purpose municipal bonds. It has been a problem for decades but escaped notice because most such bond issues are small so the losses draw little public notice or comment. In years past we have called out abusive players or practices to alert those in power to correct a problem area. We did this for retirement bond issues and Texas MUDs in the 1980s, staged defaults in the 1990s and then Florida CDDs in the 2000s.

The Wisconsin Public Finance Authority represents a new type of issuer abuse where the consequences are just beginning to appear. The abuse here is that they are authorizing bond issues in which the state of Wisconsin has absolutely no economic interest or need. A superficial look at their authorized issues shows them approving bond issues for 10 different states running in size up to $800 million for the recent American Dream Mall in East Rutherford New Jersey. The only legitimate purpose we can see in these actions is that they are fee driven, but they raise concerns of baser motives. One can also assume that bond underwriters are drawn to this issuer because the approval process is easier. We leave it to others to investigate since the practice undermines the integrity of the entire market.

Questions arise as to how do these bond issues figure in the Federal quota on the volume of bonds a state can issue as tax exempt. Also, how misleading is this for bond buyers and how do they figure in single state bond funds. As for state oversight of bonds issued for projects in that state, does this not undermine their credibility and authority? I don't have answers but I know the burden of proof is on Wisconsin to justify their infringement on the economic development of another state. For example, Texas and Florida have both tightened up on rules for community development projects caused by massive overbuilding. Do we let those developers now go to Wisconsin if local or state authorities are hesitant? The same questions exists for retirement facilities and charter schools. Let's keep municipal financing at home.

Forbes

by Richard Lehmann

Oct 16, 2020

SEC's Proposed Broker-Dealer Exemption May Apply to "Finders" for Municipal Securities: Mintz Levin

Introduction

Today, the SEC published in the Federal Register[1] a proposed notice of an exemptive order (the "Proposal") that would, subject to limitations and conditions discussed below, exempt certain individuals seeking to find investors for private companies, unregistered funds and other non-reporting issuers ("Finders") from federal broker-dealer regulation requirements. Among other things the Proposal would allow Finders to earn commissions or other transaction-based compensation. Although not targeted at municipal securities, the proposal would cover otherwise-eligible finders for most municipal securities as municipal securities generally meet the requirement that the issuer is not a public company for purposes of the Securities Exchange Act of 1934 (the "Exchange Act') and that the securities are exempt from the Securities Act of 1933's registration requirements.

The Exchange Act generally requires any individual or entity engaged in the business of effecting securities transactions to register as a broker-dealer (or, if the broker is an individual, to register as a broker-dealer representative). The burdens and uncertainties surrounding the registration requirements have discouraged many potential Finders from helping issuers raise capital. The Proposal would attempt to alleviate this by exempting two classes of Finders – Tier I Finders and Tier II Finders – from registering under the Exchange Act, based on the activities permitted. The SEC indicated the Proposal's relief is "intended to be narrowly-tailored and seeks to address the capital formation needs of certain smaller issuers while preserving appropriate investor protections."

Tier I Finders

To qualify as a Tier I Finder, a Finder's activities would be limited to providing contact information of potential investors:

- without having any contact with the potential investors about the issuer; and
- in connection with only one capital raising transaction by a single issuer within a 12-month period.

Tier II Finders

The Proposal would permit Tier II Finders to engage in the following activities related to "solicitation"[2]: identifying, screening, and contacting potential investors; distributing issuer offering materials; and arranging or participating in meetings with the issuer and prospective investors. To qualify for the relief, a Tier II Finder would need to provide each potential investor before or early in the solicitation process the following written disclosures:

- the names of and the relationship between the Tier II Finder and the issuer;
- a description of the Tier II Finder's compensation;
- any material conflicts of interest; and
- a statement that the Tier II Finder is acting as the issuer's agent, not associated with a broker-dealer, and "not undertaking a role to act in the investor's best interest."

As a condition on the relief, the Tier II Finder must obtain before each investment a dated written acknowledgment of the investor's receipt of the required disclosures.

Conditions on Both Tiers

The relief for either kind of Finder would apply only if:

- the Finder is a natural person (i.e., not an entity);
- the issuer is not a reporting company under the Exchange Act;
- the transaction is intended to be exempt from registration under the Securities Act of 1933 ("Securities Act");
- the potential investors are, or the Finder reasonably believes the potential investors are, "accredited investors" under Securities Act Rule 501; and
- the Finder's services are pursuant to a written agreement describing the Finder's services and compensation.

Neither Tier I Finders nor Tier II Finders would qualify for the Proposal's relief if they:

- engage in general solicitation;
- help structure the transaction;
- negotiate offering terms;
- handle customer funds or securities;
- have authority to bind the issuer or any potential investor;
- participate in offering material preparation;
- perform independent transaction analysis;
- engage in due diligence;
- assist or provide financing of any securities purchase;
- advise on valuation or advisability of the potential investment;
- are associated with a broker-dealer; or
- are subject to statutory disqualification under the Exchange Act.

Requests for Comment

The Proposal seeks comments on 45 questions, including whether various aspects of the relief are appropriate for investor protection, whether the relief should be subject to the limitations and conditions summarized above, whether certain existing no-action letters granting and denying broker-dealer registration relief should be codified or withdrawn, whether the SEC should issue guidance on related matters (including applicability of broker-dealer registration to private fund advisers and real estate brokers), and how the Tier II disclosure requirements should relate to proposed amendments to the SEC's cash solicitation rule.[3] Comments are due November 12, 2020.

Relation to Existing No-Action Relief and Issuer Safe Harbor

The relief in the Proposal is non-exclusive. It would be additive to and combinable with existing kinds of relief from broker-dealer registration under the Exchange Act, including the safe harbor for associated persons associated with an issuer[4] and the no-action letter granting relief to mergers and acquisition brokers.[5]

Relation to State Broker-Dealer Requirements

Nothing in the Proposal affects requirements to register as a broker-dealer or broker-dealer agent under state "blue sky" securities laws.

Observations

Uncertainties about broker registration present legal risks and obstacles for private companies and funds seeking to engage and incentivize individuals with the requisite industry experience and connections to raise capital. Such uncertainties also may affect capital-raising outreach by or on behalf of smaller issuers or borrowers in the municipal markets. Among other things, not registering when required can: (i) trigger SEC or state enforcement action against a finder for violating registration requirements or against an issuer or investor for aiding and abetting the finder's violations; (ii) give rise to rescission claims by investors solicited by an unregistered finder; and (iii) prevent finders from prevailing on claims to collect fees. The non-exhaustive safe harbor in the Proposal would allow engagements and success fee arrangements not possible today while providing much-needed clarity on which solicitation-related activities require registration and which do not.

The limitations on the narrowly tailored relief in the Proposal will keep it from being useful in many situations that commonly arise. Conditions that would make it challenging for many consulting arrangements to use the relief as proposed include the inability to pay a Finder's entity, structure transactions, help prepare marketing materials, value deals, or perform due diligence. The ban against negotiation could be difficult in practice because soliciting investors often bleeds into discussing terms.

Relief from registering federally with the SEC and FINRA is of limited use if a Finder must still register in one or more states. State adoption of parallel relief under identical conditions would be ideal. In the absence of such parallel state relief. Finders could explore existing finder exemptions under state law, which have their own conditions and restrictions that differ with the Proposal, or other state broker-dealer exemptions and exclusions.

Finally, in the context of municipal issuers, as noted by the SEC in the notice, whether or not a Finder complies with the proposed broker-dealer exemption, he or she may need to consider whether the contemplated activities require registration as a municipal advisor.

Next Steps

Private companies, managers and advisers of private funds, municipal issuers and borrowers and prospective Finders interested in taking advantage of any relief resulting from the Proposal should contact the authors or their Mintz attorney. We stand ready to assess how to pursue the opportunities presented to further clients' business objectives and to help prepare any comment letters that might make the final relief more valuable than the Proposal.

Endnotes

1 Notice of Proposed Exemptive Order Granting Conditional Exemption From the Broker Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934 for Certain Activities of Finders, 85 FR 64542 (Oct. 13, 2020).

2 The Proposal defines "solicitation" broadly as "any affirmative effort to induce or attempt to induce a securities transaction."

3 See Investment Adviser Advertisements; Compensation for Solicitations, Release No. IA-5407 (Nov. 4, 2019), 84 FR 67518 (Dec. 20, 2019).

4 See Exchange Act Rule 3a4-1, 17 C.F.R. § 240.3a4-1.

5 See SEC No-Action Letter re M&A Brokers (Jan. 31, 2014).

By Steve Ganis, Leonard Weiser-Varon

October 13, 2020

SEC Proposes Exemptive Order for Certain Activities of Finders.

On October 7, the U.S. Securities and Exchange Commission (Commission or SEC) released for notice and comment a proposed exemptive order (Notice)1 that would grant conditional exemption from the broker-dealer registration requirements of Section 15(a) of the Securities Exchange Act of 1934 (Exchange Act) for certain activities of "finders." If the Commission issues a final exemption, it would mark the Commission's broadest statement ever about the ability of persons not registered as broker-dealers to take transaction-based compensation for U.S.-based solicitation of investors on behalf of issuers in connection with capital-raising activities, something that historically has been considered a core activity that requires registration as a broker-dealer under the Exchange Act. In addition to potentially easing capital raising for operating company issuers, private fund advisers seeking investors in their funds may also benefit from the exemption if such advisers do not own, or are otherwise affiliated with, a registered broker-dealer.

Background

Although not officially defined in any statute or rule issued by the Commission, a finder is a person who performs some of the activities in the initial stages of a securities transaction that are normally conducted by brokers. For example, a finder may place potential buyers and sellers of securities in contact with one another and receive a fee for its services. Though Section 3(a)(4) of the Exchange

Act defines a "broker" as "any person engaged in the business of effecting transactions in securities for the account of others,"2 the SEC has been historically hostile to the notion of allowing finders to conduct a business — for compensation — of making introductions without broker registration under the Exchange Act.

As recognized in the Notice, the existing law and guidance on finders is varied and inconsistent.3 Although the Commission staff has previously recognized a finders' exception, it has done so in limited circumstances that would not sustain an ongoing business. The Commission itself has not broadly addressed whether and under what circumstances a person may "find" or solicit potential investors on behalf of an issuer without being required to register as a broker, or even whether such activity implicates the Commission's regulatory regime for brokers.4 Instead, market participants have had to look to guidance in SEC enforcement actions and no-action/denial of no-action letters issued by Commission staff. Although some general themes can be distilled from the no-action letters, the relief granted usually depends on the particular set of conditions and policy considerations presented and therefore may not have broader application. In addition, the no-action letters that relate to finders span over decades of market evolution, often rendering the guidance inconsistent. The settled and litigated SEC enforcement actions similarly have presented unusual facts and have had inconsistent results.

Description of the Proposed Exemption5

To provide clarity regarding the guidance on finders, the Commission in its Notice proposes to grant a conditional exemption from the broker-dealer registration requirements of Section 15(a) of the Exchange Act to permit natural persons to engage in certain limited capital-raising activities involving accredited investors. The proposed exemption would create two classes of exempt finders, Tier I Finders and Tier II Finders, that would be subject to conditions tailored to the scope of their respective activities. Tier I and Tier II Finders would both be permitted to accept transaction-based compensation under the terms of the proposed exemption.6

Conditions for Both Tier I and Tier II Finders

Finders (collectively Finders) would be subject to certain conditions. The proposed exemption for Tier I and Tier II Finders would be available only where

- the issuer is not required to file reports under Section 13 or Section 15(d) of the Exchange Act
- the issuer is seeking to conduct the securities offering in reliance on an applicable exemption from registration under the Securities Act of 1933 (Securities Act)
- the Finder does not engage in general solicitation7
- the potential investor is an "accredited investor" as defined in Rule 501 of Regulation D or the Finder has a reasonable belief that the potential investor is an "accredited investor"
- the Finder provides services pursuant to a written agreement with the issuer that includes a description of the services provided and associated compensation
- the Finder is not an associated person of a broker-dealer8
- the Finder is not subject to statutory disqualification, as that term is defined in Section 3(a)(39) of the Exchange Act, at the time of his or her participation

Tier I and II Finders would have to comply with additional requirements as described below.

Tier I Finders

A Tier I Finder would be limited to providing contact information of potential investors in connection with only a *single* capital-raising transaction by a *single* issuer in a 12-month period.9 A Tier I Finder cannot have any contact with a potential investor about the issuer. Neither the Tier I Finder nor the issuer would have any disclosure requirement concerning the Finder's activities or compensation.

Tier II Finders

A Tier II Finder could directly solicit investors on behalf of multiple issuers within a given 12-month period, but the solicitation-related activities would be limited to (i) identifying, screening, and contacting potential investors; (ii) distributing issuer offering materials to investors; (iii) discussing issuer information included in any offering materials, provided that the Tier II Finder does not provide advice as to the valuation or advisability of the investment; and (iv) arranging or participating in meetings with the issuer and investor. In addition, a Tier II Finder must provide appropriate disclosures of the Tier II Finder's role and compensation, which must be made prior to or at the time of the solicitation. Further, the Tier II Finder must obtain from the investor, prior to or at the time of any investment in the issuer's securities, a dated written acknowledgment of receipt of the required disclosures. The Tier II Finder could not be involved in structuring the transaction or negotiating the terms of the offering, handle customer funds or securities, or bind the issuer or investor. The Tier II Finder also could not participate in the preparation of any sales materials; perform any independent analysis of the sale; engage in any "due diligence" activities; assist or provide financing for such purchases; or provide advice as to the valuation or financial advisability of the investment.

The proposed exemption would not affect a Finder's obligation to continue to comply with all other applicable laws, including the antifraud provisions of the Securities Act and the Exchange Act, such as the obligations under Section 10(b) and Rule 10b-5 under the Exchange Act, and state law. In addition, the proposed exemption would not affect the rights of the Commission or any other party to enforce compliance with other applicable law or the available remedies for violations of the law.

Further, regardless of whether or not a Finder complies with this exemption, it may need to consider whether it is acting as another regulated person such as an investment adviser or a municipal adviser. An exemption from the obligation to register as a broker-dealer does not insulate a person from the registration requirements of the Advisers Act if such person is acting as an investment adviser.

Some private fund advisers take the position that their internal marketing activities come within the nonexclusive safe harbor exemption in SEC Rule 3a4-1. Although SEC Rule 3a4-1 has a comparable 12-month restriction as proposed for Tier I Finders, the rule does not permit the payment of transaction-based compensation. As such, the proposed exemption may expand the ability to compensate internal fund marketing personnel.

The proposed order addresses only broker-dealer registration under Section 15(a) of the Exchange Act. It does not address separate "broker-dealer" requirements that could arise under applicable states' so-called "Blue Sky" or securities laws. All states require registration of broker-dealers subject to limited exceptions/exemptions that may not encompass Finders.

Conclusion

Following publication in the Federal Register, there will be a 30-day period for interested persons to comment on the proposal. The Commission provided a chart to further explain the parameters of its proposal, which can be found here.

The prospects for adoption of the proposal are uncertain, and it could be modified in light of comments. The November elections further cloud the prospects of the proposal; both Democratic commissioners voted against issuance of the Notice on investor protection grounds and may eventually oppose adoption of the proposal. That said, the short 30-day comment period may indicate the Commission's intention to move forward before a new administration takes the helm.

1The Notice has not yet been published in the Federal Register but is available here: https://www.sec.gov/rules/exorders/2020/34-90112.pdf.

2 Section 3(a)(4)(A) of the Exchange Act, 15 U.S.C. 78c(a)(4)(A). In accordance with this provision, Section 15(a)(1) of the Exchange Act makes it unlawful for any broker to use the mails or any other means of interstate commerce to "effect any transactions in, or to induce or attempt to induce the purchase or sale of, any security" unless that broker is registered with the Commission. As a result, absent an available exception or exemption, a person engaged in the business of effecting transactions in securities for the account of others is generally a broker required to register under Section 15(a) of the Exchange Act. See Section 15(a) of the Exchange Act, 15 U.S.C. 78o(a).

3 See Notice at 14.

4 See Id.

5 We note the conditions of this proposed exemptive order for Finders differ from the requirements for solicitors under the Commission's proposed amendments to Rule 206(4)-3 under the Investment Advisers Act of 1940 ("Advisers Act"). See Investment Adviser Advertisements; Compensation for Solicitations, Release No. IA-5407 (Nov. 4, 2019), 84 FR 67518 (Dec. 20, 2019) ("Cash Solicitation Rule Proposed Amendments"). These differences reflect the particular facts and circumstances surrounding the proposed permitted activities for Finders and solicitors, and the characteristics of the applicable regulatory regimes, notably that a solicitor would solicit for an investment adviser and would be subject to oversight by such investment adviser, while a Finder would solicit for an issuer and therefore would not be subject to such oversight. See Cash Solicitation Rule Proposed Amendments at 67580.

6 Because the proposed exemption would be limited to natural persons, it is not clear that a natural person could establish an entity to receive its fees.

7 This limit would seem to suggest that a Finder could not participate in a "private" offering conducted under SEC Rule 506(c), which allows the issuer to rely on the private offering exemption in Section 4(a)(2) of the Securities Act even if general solicitation is used.

8 This concept has been construed broadly in a similar context to mean that any person who is employed in a group that owns or controls a registered broker-dealer would, generally, be deemed to be an associated person of the broker-dealer, even if the person does not conduct any activities on behalf of the broker-dealer.

9 This is a comparable requirement to SEC Rule 3a4-1, a nonexclusive safe harbor exemption for certain associated persons of an issuer.

Sidley Austin LLP – James Brigagliano, W. Hardy Callcott, David M. Katz, Laurin Blumenthal Kleiman and Andrew J. Sioson

October 12, 2020

SEC Issues Proposed Order Exempting “Finders” from Registration Requirements.

On October 7, 2020, the Securities and Exchange Commission announced that it had voted 3-2 in favor of a Proposed Exemptive Order granting conditional exemption from the broker registration requirements of Section 15 of the Exchange Act. The exemption would allow “finders” to engage in certain limited activities on behalf of issuers without registering as brokers. The Order seeks to provide the clarity that market participants have sought for many years. It also follows requests to address the issue from government and professional bodies including SEC advisory committees, the American Bar Association, and the U.S. Department of the Treasury. The SEC is requesting public comments on the Order.

Background

Small businesses often find it challenging to connect with investors in the exempt market, particularly in regions lacking robust capital-raising networks and when they seek investment below a level that attracts venture capital or registered broker-dealers. “Finders” can help bridge this gap between businesses and investors.

However, there is insufficient clarity on when a company can properly engage a Finder or a platform that is not registered as a broker-dealer. Generally, brokers must register with the SEC and comply with comprehensive regulation because they act as intermediaries between customers and the securities markets. The Exchange Act defines a “broker” as “any person engaged in the business of effecting transactions in securities for the account of others.” Since the Act does not define what it means to be “engaged in the business” or “effecting transactions,” non broker-dealers are dissuaded from facilitating investment for early stage companies in case they are inadvertently acting as unregistered brokers. At the same time, there may be untapped capital that could help small businesses grow were it not for such regulatory uncertainty.

In the absence of definitional clarity, courts and the SEC currently look to various factors in determining whether a person is a broker. Market participants also look to SEC staff no-action letters for guidance. Unfortunately, none of these sources provide a uniform framework for participants. It is in this context, and in the hope of facilitating capital formation for small and emerging businesses, that the SEC is establishing a limited exemption from the registration requirement.

Proposed Order “Finder” Exemption

The SEC proposes to permit a natural person to engage in certain defined activities on behalf of an issuer without registering as a broker. If a Finder complies with all the ‘general’ and ‘specific’ conditions below, they may assist businesses with capital formation and receive compensation for their services.

General Conditions

The Finder exemption would be available where the following general conditions are met:

- the issuer is not required to file reports under Section 13 or 15(d) of the Exchange Act;
- the issuer is seeking to offer securities under an applicable exemption from registration;
- the Finder does not engage in general solicitation;
- the potential investor is an “accredited investor” under Regulation D or the Finder has a

reasonable belief that the potential investor is an “accredited investor”;
- the Finder and issuer have a written agreement that includes a description of the services provided and associated compensation;
- the Finder is not an associated person of a broker-dealer; and
- the Finder is not subject to statutory disqualification, defined in Exchange Act Section 3(a)(39)

The exemption does not permit potential Finders to engage in any of the following:

- structuring the transaction or negotiating the terms of the offering;
- handling customer funds or securities;
- binding the issuer or investor;
- participating in the preparation of any sales materials;
- performing any independent analysis of the sale;
- engaging in any “due diligence” activities;
- assisting or providing financing for purchases; or
- advising on the valuation or financial advisability of the investment.

Conditions Specific to Tier I and Tier II Finders

The Proposed Order establishes two classes of Finders: Tier I and Tier II. In addition to fulfilling the general conditions above, potential Finders must also comply with requirements specific to each Tier.

A “Tier I Finder” is a Finder who *meets the general conditions and only provides contact information of potential investors for only one capital raising transaction by a single issuer within a 12-month period*. The contact information may include, among other things: name, telephone number, e-mail address, and social media information. The Tier I Finder may not have any contact with the potential investors about the issuer, nor participate in continuous or multiple sales of securities.

A “Tier II Finder” is a Finder who *meets the general conditions and engages in solicitation-related activities for an issuer*. Solicitation is “any affirmative effort to induce or attempt to induce a securities transaction.” Although solicitation is generally prohibited for unregistered persons, the activities below fall under the exemption in the Proposed Order:

1. identifying, screening, and contacting potential investors;
2. distributing offering materials to investors;
3. discussing information included in offering materials, provided that the Finder does not provide advice as to the valuation or advisability of the investment; and
4. arranging or participating in meetings with the issuer and investor.

Prior to or at the time of the solicitation, a Tier II Finder must also disclose to the potential investor:

1. the name of the Tier II Finder;
2. the name of the issuer;
3. the description of the relationship between the Finder and the issuer, including any affiliation;
4. a statement that the Tier II Finder will be compensated for their solicitation activities by the issuer and a description of the terms of such compensation arrangement;
5. any material conflicts of interest resulting from the arrangement between the Finder and issuer; and
6. an affirmative statement that the Finder is acting as the issuer’s agent, is not acting as an associated person of a broker-dealer, and is not undertaking a role to act in the investor’s best interest.

A Tier II Finder may make these disclosures orally if supplemented by written disclosures. Delivery of the disclosures may be evidenced by a dated written acknowledgment, obtained from the investor prior to or at the time of the investment, of receipt of the disclosures. The disclosures and acknowledgment may be in paper or electronic form.

The SEC has prepared a chart that shows the differences between the two tiers of Finders and registered broker-dealers.

Individuals hoping to act as Finders will need to remember that the exemption applies only to the defined activities and not to any related actions, such as facilitating a registered offering, reselling the securities, or selling to unaccredited investors. Furthermore, the exemption does not affect a Finder's obligation to comply with all other applicable laws, including state laws and the SEC's antifraud laws. Naturally, potential Finders will also need to ensure that they fall under the exemption and are not instead required to register with the SEC as a broker. Moreover, individuals falling under the Finder exemption may still be regulated in other ways, for example if they are an investment or municipal advisor.

Michael Best & Friedrich LLP – Betsy T. Voter, Joshua B. Erekson, Michael H. Altman, Kevin C. Timken, Shawn T. Stigler, Melissa M. Turczyn and Iqan E. Fadaei

October 14 2020

COVID-19 Regulatory Actions and Developments - Municipal Advisor: Katten Muchin

Securities and Exchange Commission (SEC)

Date: April 24, 2020

SEC Announces Cross-Divisional COVID-19 market Monitoring Group

The SEC announced the formation of a senior-level internal cross-divisional COVID-19 Market Monitoring Group to assist the Commission with respect to actions and analysis related to the effects of COVID-19 and to respond to requests for information and assistance from regulators and others.

Read the SEC Press Release.

Date: March 26, 2020

Temporary Extension for Updating Form MA

The SEC issued a temporary conditional exemptive order allowing municipal advisors affected by COVID-19 an additional 45 days to file annual updates to Form MA that otherwise would have been due between March 27, 2020 and June 30, 2020, subject to certain conditions. The additional time is available only to municipal advisors that are unable to meet the deadline due to COVID-19.

Read the SEC Order.

Date: March 23, 2020

OCIE Statement on Examinations of SEC Registrants

The SEC's Office of Compliance Inspections and Examinations announced that it has moved to conducting examinations of registrants off-site through correspondence, unless it is absolutely necessary to be on-site.

Read the SEC Order.

Katten Muchin Rosenman LLP

October 14 2020

A Guide to the World's New Benchmarks After Libor.

Here's how to make sense of the dizzying array of acronyms that have sprung up in major markets.

For about 50 years, the London interbank offered rate has helped determine the cost of borrowing around the world, from student loans and mortgages to interest-rate swaps and collateralized loan obligations.

Libor, derived from a daily survey of bankers who estimate how much they would charge each other to borrow, was simple, effective, ubiquitous, and seemingly reliable.

As markets evolved, the trading that helped inform those estimates dried up. In the wake of the 2008 financial crisis, regulators discovered that the banks trusted to set the rates underpinning hundreds of trillions of dollars of financial assets had been manipulating them to their advantage.

Continue reading.

Bloomberg Rates

By Boris Korby, William Shaw, and Alex Harris

August 11, 2020, 12:00 AM PDT

Wall Street Eyes Fix for $345 Billion Libor Dilemma in Debt Swap.

- **Beleaguered benchmark set to be discontinued by end of 2021**
- **FFCB exchanging bonds that can't switch to new reference rate**

A U.S. government-sponsored agricultural lender is seeking to swap $1.9 billion of Libor-linked bonds in a deal backers say could serve as a template for future transactions ahead of the discredited reference rate's planned phase-out.

The Federal Farm Credit Banks Funding Corp. is looking to exchange the securities due between 2022 and 2032 that lack language to account for the end of Libor for notes that will shift to the

Secured Overnight Financing Rate when the beleaguered benchmark expires at the end of next year. There's at least $345 billion of dollar-denominated floating-rate notes set to mature after 2021 that don't have the necessary contractual terms to transition from Libor, according to TD Securities (USA), which is managing the deal.

The swap comes as proposed legislation designed to address the issue makes little headway with New York state lawmakers, raising concerns on Wall Street. The deal is being viewed as something of a trial balloon as bankers, investors and regulators work to avert financial chaos when Libor is phased out. Without a solution, countless floating-rate bonds would effectively convert to fixed-rate notes based on Libor's final print, potentially upending the market and leading to a flood of litigation, according to industry watchers.

The swap "could be a very significant moment for the transition," said Andrew Gray, co-chair of the outreach and communications working group for the Alternative Reference Rates Committee, the Federal Reserve-backed group guiding the U.S. Libor shift. It may cause "a domino effect as other bond issuers seek to incorporate ARRC fallback language through similar bond exchanges."

While issuers could theoretically amend outstanding bonds to address the fallback language issue, floating-rate notes typically require consent from each holder to change their benchmark interest rate, making such efforts impractical.

The FFCB exchange offer began Sept. 24 and is set to expire at 5 p.m. New York time on Oct. 22.

Bondholders often choose to participate in debt swaps rather than risk getting stuck with notes with reduced liquidity, which can weigh on their price.

Still, without unanimous participation the swap will only be a partial fix, according to Anne Beaumont, counsel at Friedman Kaplan Seiler & Adelman LLP.

"They'll still have a complex problem for the bonds that aren't exchanged," she said. "It's not a total solution. You could even say it makes it more complicated as you are likely to have two sets of bonds."

The FFCB raises funds by selling debt to banks, insurers and state and local municipalities. It then provides loans, leases and other services to rural communities and U.S. agriculture businesses, according to its website.

Bloomberg Markets

By William Shaw

October 13, 2020, 8:34 AM PDT

IRS Issues Guidance on Transition From LIBOR to IBORs: NABL

On Friday, October 9, 2020, the US Internal Revenue Service (IRS) released Revenue Procedure 2020-44 (the RP) which provides interim guidance to facilitate the transition from the London interbank offered rate (LIBOR) and other interbank offered rates (IBORs) to alternative reference rates through adoption of fallback language recommended by the Alternative Reference Rates Committee (ARRC) and the International Swaps and Derivatives Association (ISDA).

Specifically, the RP addresses whether modifying existing documents to incorporate fallback language published by the ARRC and ISDA results in a reissuance for federal income tax purposes. The RP states that interim guidance was needed as the U.S. Department of the Treasury (Treasury) continues the process of finalizing related Proposed Treasury Regulations promulgated in 2019 (view the NABL comment letter regarding the Proposed Treasury Regulations here).

The RP is intended to support modifications that follow the ARRC and ISDA fallback language and protocols by providing that such modifications will not cause a reissuance, and applies to bonds, leases, and swaps and certain other contracts referencing an IBOR, as well as to variable rate private student loans that may be based on LIBOR.

The relief under the RP applies only to modifications where a contract is modified to:

- Incorporate an ISDA fallback.
- Incorporate an ARRC fallback.
- Incorporate either of the above, with certain specified deviations, such as deviations to confirm the fallback is enforceable under local law, changes to terms that are not relevant to a particular transaction, adjustments to incorporate ISDA language into a contract that is not otherwise a contract covered by the ISDA protocol, adding or revising technical items necessary to adopt the new language (but the RP relief does not apply to the addition of a term that obligates one party to make a one-time payment (or similar payments) as a substitute for any portion of an ARRC or ISDA fallback).

The RP also provides that such adjustments to a qualified hedge under Treas. Reg. § 1.148-4 will not result in a deemed termination of the qualified hedge.

The RP is effective for modifications to contracts occurring on or after October 9, 2020 and before January 1, 2023. The RP can be relied on for modifications to contracts occurring before October 9, 2020.

View Revenue Procedure 2020-44 here.

SEC Enforcement Approach May Hinge On Election Results.

The next appointed Securities and Exchange Commission is likely to be more polarizing, and the SEC's approach to enforcement will differ depending on who wins the presidential election.

Current SEC Chair Jay Clayton, widely considered a centrist and who is reportedly not interested in continuing in the role, will likely not be reappointed as both President Donald Trump and former Vice President Joe Biden are likely to pick chairs more aligned with their political parties. Importantly, the SEC chair historically does not view municipals as a main priority.

At the end of the day, Clayton was more of a centrist than a lot of other policy people Trump appointed, a securities lawyer said.

"So thematically, I would expect if anything he would have somebody be more right wing," he said. "Basically, although it hasn't really happened in the last 12 years, you might see the SEC chair be a little bit of a more polarized choice, reflecting the increasing polarization of so many of our institutions like the Supreme Court."

If Biden wins in November, there is a good possibility that he will have learned from the mistakes made by the Obama administration when he was vice president. One mistake was appointing too much of a centrist as SEC chair, the securities lawyer said.

Obama appointed Mary Schapiro, an independent, in January 2009, and she was the first woman to serve as the SEC's permanent chair. Under Schapiro, the lawyer said, the SEC failed to aggressively pursue bad actors, including in the municipal space.

The weakest part of Obama's presidency was how he had the ability to make lasting reform, but didn't because most of the people he chose for senior policy positions were anti-regulation and either moderate or right-leaning, the securities lawyer said.

"While you might not need additional regulation, you might need somebody who is leading the financial market who is a little more focused on bringing enforcement actions against the biggest players and the worst behavior," the securities lawyer said.

Mary Jo White, an independent, was nominated by Obama after Schapiro. White had a very strict "broken windows" approach to enforcement. Under her watch the SEC introduced the Municipalities Continuing Disclosure Initiative, which promised underwriters and issuers would receive lenient settlement terms if they self-reported instances over the last five years where issuers falsely stated in offering documents that they were in compliance with their continuing disclosure agreements.

Also under White's leadership, the Enforcement Division brought numerous muni enforcement cases including against the mayor of Harvey, Illinois.

Depending on Trump's pick, a Republican chair is likely to err on the side of guidance and amending rules before taking enforcement action. Under a Democratic chair, the SEC may be more willing to do rulemaking by enforcement, said Peter Chan, a partner at Baker & McKenzie and former SEC enforcer.

"Saying that they will be more aggressive isn't saying that they will be better or worse," Chan said.

In fiscal year 2019, the SEC brought 516 standalone enforcement actions, up from 490 in FY 2018. In FY 2017, 446 enforcement actions were brought by the SEC and in FY 2016 there were 548 standalone enforcement actions, according to the SEC's 2019 annual report.

Municipal issues will likely be a point of bipartisan consensus, such as timeliness of financial documents and pricing transparency in the secondary market. The SEC has long been focused on the timeliness of issuers? financial reporting.

"The way they attack concerns, there may be some difference in approach, but the issues are shared in a bipartisan way," Chan said.

Beyond the municipal bond market, the SEC will be more focused on differences in corporate disclosure, among other topics. The municipal market isn't really the focus of an SEC chair.

"Because of that, if anything in the midst of severe disagreement on other issues, whether it's a Republican or Democratic-appointed chairman, there will be a lot of institutional desire to address the public finance market where there are much less partisan disputes," Chan said.

Chuck Samuels, counsel to the National Association of Health & Educational Facilities Finance Authorities, emphasized that municipal finance is not a significant sector for the SEC. It would be "pure chance" for the next SEC chair to have any experience in municipal finance, he said.

The Senate also has to affirm the next president?s pick. The Senate is currently majority Republican, but that could flip next year. If it does flip, Sens. Elizabeth Warren, D- Mass., or Sherrod Brown, D-Ohio could have an influence on who is next SEC chair.

“There will be a tug of war between the left-wing and the moderates in the Biden administration,” Samuels said.

By Sarah Wynn

BY SOURCEMEDIA | MUNICIPAL | 10/14/20 01:41 PM EDT

Bond Markets Face Big Challenges.

The Libor transition, credit risk in municipal bonds, best execution and remote access for trading platforms are just some of the pressing challenges facing tomorrow’s bond markets, according to fixed income experts.

On Oct. 5, the Securities and Exchange Commission held an open meeting of its Fixed Income Market Structure Advisory Committee (FIMSAC), whose members include investors, bond issuers and dealers, trading venues, academics, data providers and more.

Monday’s meeting of the minds provided not just context around recent events, but also a rare sneak peek into what could become the regulatory agency’s future priorities for the fixed income markets.

What The Meeting Covered

Monday’s sessions ranged far and wide. To start, the committee deliberated how best to define “electronic trading,” so as to allow for a regulatory framework that could be consistent and consistently applied.

That was followed up with in-depth conversations about structural strengths and challenges in the corporate and municipal bond markets; then a postmortem on how bond ETFs fared during the market volatility in March and April. (Spoiler alert: Despite a few isolated bumps, mostly they worked as intended.)

However, one of the most interesting bits came in the closing comments, where FIMSAC members shared where they felt the committee’s future priorities ought to lie.

Generally, the committee agreed that the fixed income market is structurally sound. But it could use a few key updates and modernizations.

Facing The Libor Transition Head-On

One of those modernizations is already taking place: the global phaseout of Libor in favor of the secured overnight financing rate (SOFR).

Currently, the London interbank offered rate, or Libor, is the world’s most widely used benchmark for short-term interest rates, tied to hundreds of trillions of dollars in loans, mortgages, corporate debt, derivatives and other instruments. Libor is calculated by averaging several bank funding rates across five different currencies and seven different borrowing periods, ranging from overnight to one year.

But Libor has some issues. Its calculation methodology is clunky and outdated, and the pool of banks who report their rates has shrunk since the 2008 financial crisis. That's led to greater reliance on subjective estimates and "expert judgment" to calculate moves in the rate. Plus, by the nature of representing banks' average borrowing costs, there is some built-in credit risk to the Libor.

Ushering In SOFR

For those reasons, Libor is being retired in favor of SOFR—at least for dollar-denominated loans and securities. SOFR is a median of overnight cash borrowing rates in the Treasury's repo market.

Yet transitioning from one rate to another isn't as easy as just hitting Ctrl-F on a Word document. An entire indexing and investment infrastructure has been built up around Libor, and thousands of existing financial instruments are foundationally based on the existing reference.

Multiple FIMSAC members pointed to this transition as one of the most pressing concerns of the next year, indicating that there was still a lot of work to be done, both in identifying potential market challenges and addressing any credit-sensitive impacts.

How Best To Protect Best Execution?

Many committee members also expressed concerns about how to improve and ensure best execution across the fragmented fixed income market, where most trades still happen in opaque, over-th--counter matchups.

The potential was floated for additional national best bid and offer (NBBO) regulation for corporate bonds. Such regulation would require brokers to source the best prices when trading on behalf of clients—meaning, they must trade at the highest bid and lowest ask.

Current NBBO regulation only applies to stocks, however, and the equity market is much smaller and more transparent than the bond market.

Whereas the equity market comprises roughly 3,500 securities, there are tens of thousands of corporate bond issues alone, with thousands more launching every year. (One FIMSAC member, academic and former SEC Chief Economist Larry Harris, even brought this up as a potential avenue of further inquiry: How can the agency encourage the issuance of fewer bond securities?)

Fleeting Pricing Confidence

Reggie Browne, principal of market-making firm GTS, also championed the idea of NBBO in fixed income when we spoke to him in March: "You don't have anyone disseminating nationally and instantaneously the best bid/best offer and where the last trade occurred. You have issues around confidence about the ability to transact in corporate bonds." (Read: "Why Many Bond ETFs Now Trading At Discounts.")

Relatedly, other committee members raised the question of how best to disseminate pricing data and data about new issuers, including identifiers, maturity date, coupon and so on. This data is critical for any bond trade, yet access to it can vary substantially depending on which platform is used.

"Without this data, [investors are] hampered in their ability to trade these issues on equal footing," said Lynn Martin, president and COO of ICE Data Services.

A number of committee members suggested improvements to FINRA's over-the-counter real-time price dissemination service, Trade Reporting and Compliance Engine (TRACE), as well as the possible introduction of a corporate bond pricing reference service that would offer impartial, equal access to trading data for all market participants.

Trouble Brewing In Munis?

Notably, several committee members raised concerns about rising credit risk in the municipal bond market.

With the COVID-19 pandemic depressing economic activity across the nation, state and local governments are seeing reduced tax revenues—the same revenues they use to pay off their debt obligations. Should conditions persist or worsen, Mark Kim, COO of the Municipal Securities Rulemaking Board, wonders if these governments will be able to continue making timely payments.

“Munis have proven themselves resilient in the face of shocks, but markets don’t like surprises,” he noted.

Other commenters questioned whether municipals were being fairly rated, given the difficulty in acquiring timely financials from municipalities. Better disclosure for munis is needed, said former SEC chairman Elisse Walter, adding that “fixing that may do much to fix transparency in the municipals market.”

E-Trading Can Be Made More Efficient

Finally, many FIMSAC members pointed to the opportunity and challenge of the market’s increasing reliance on remotely accessed electronic trading (“e-trading”).

E-trading of bonds is nothing new. But when the pandemic struck and lockdowns were implemented overnight, nobody really knew how smoothly trading technology would function in a 100% work-from-home setting. (Read: “For ETFs, Trading Floor Closures Mean Little.”)

Fortunately, it did work, both for bond traders and for dealers. Still, there’s more work to be done in making efficient, secure platforms available across all bond markets—indeed, some illiquid corners of the market still place trades by phone—and to make these platforms accessible to everyone, not just a subset of traders.

“The whole life cycle needs access to this, not just traders, but clients, compliance, risk officers, the variety of participants in the market,” said Tradeweb CEO and Co-Founder Lee Olesky.

“We’re not out of the pandemic yet,” he added. “We still have a ways to go.”

etf.com

by Lara Crigger

October 9, 2020

Muni Bond Market Disclosure: It’s About Time - And Time Is Money

The prior article *A Technology Solution For Muni Bond Disclosure* discussed how new technologies and data science methods are transforming disclosure in the municipal bond market.

This article, the sixth and final piece of a six-part series on investor disclosure in the municipal bond market, outlines how municipalities and authorities pay the very high real dollar cost of inefficient disclosure. Ironically, it is these very borrowers who use this capital market that are the one's with the power to correct many of the market's disclosure problems.

The Cost of Disclosure

Understandably, municipal bond borrowers want the best, lowest interest rates for their bonds. There is grumbling that, for all this talk of disclosure, they don't see it in the underwriting price of their bonds. But to expect efficient pricing when disclosure is reported months late, lacks consistently applied standards and is not structured data? It's like having frosted windows installed and then being upset the view isn't clear.

Continue reading.

Forbes

by Barnet Sherman

Oct 6, 2020

MSRB: Primary Market Disclosures Citing COVID-19 Hit a 15-Week High.

Municipal Securities Market COVID-19-Related Disclosure Summary

Last Updated: Oct 05, 2020 for the Week Ending Oct 04, 2020

MSRB CEO Mark Kim's Remarks at the U.S. Securities and Exchange Commission's Fixed Income Market Structure Advisory Committee (FIMSAC) Meeting.

Meeting Occurred on October 5, 2020.

Good afternoon Chairman Clayton, SEC Commissioners, Commission staff, FIMSAC Chair Heaney and FIMSAC colleagues.

On behalf of the MSRB, I thank you for this opportunity to share the views of the Board on risks in the municipal securities market.

As we have seen from the panel presentations this morning, the pandemic caused a significant dislocation in the municipal securities market.

During this past March and early April, many state and local government issuers did not have access to the primary market and liquidity was scarce due primarily to mutual fund outflows. Secondary market trading in March increased to levels not seen since the financial crisis of 2008-2009.

Fortunately, the dislocation was relatively short-lived, and the muni market showed its resilience in the following months. Liquidity from mutual fund inflows returned to the primary market with issuance volumes and secondary market trading in the months of May and June returning to historical levels.

However, there is one significant risk that the Board would like to take this opportunity to share with the Commission, and that is the risk of credit quality in the municipal securities market.

With the pandemic continuing to dampen economic activity across the country, state and local governments are facing increasing financial pressure with reduced tax revenues.

As you know, these are the very same tax revenues that support the repayment of most municipal bonds.

The Board is monitoring the ongoing impact of the pandemic on state and local governments' revenues and their continued ability to make timely payments of principal and interest on their municipal bond issues.

In our current low interest rate environment, and subsequent spread compression across all rating categories of bonds, it remains challenging for investors to fully evaluate and price credit risk in the municipal securities market. This is especially true for "main street" or retail investors, who remain an important part of the buyer base for municipal securities.

The Board's response to this risk has been to provide the market and investors with greater transparency. We are leveraging technology to analyze the continuing disclosures and event notices submitted by issuers that disclose material information about the impacts of the pandemic on their operations and finances.

We applaud your efforts, Chairman Clayton, and the efforts of the Office of Municipal Securities, to draw attention to the broader issue of disclosure in the municipal securities market.

And we applaud the efforts of state and local government issuers to address this risk by providing the market with more timely and more complete information about the impacts of this pandemic on their finances and operations.

In conclusion, the municipal securities market has proven itself to be resilient in the face of external shocks. But as we all know, markets don't like surprises. And as this pandemic continues to add complexity and uncertainty to the economic outlook of state and local economies, the risk of an unexpected or sudden deterioration in credit quality in the municipal securities market could undermine investor confidence.

Thank you for the opportunity to share the views of the MSRB with the Commission.

SEC Committee Tackles Disorderly Electronic Bond Trade Reporting.

New definition could affect shares of electronic bond trading platforms

Liquidity is key in bond markets, but measuring it has grown more complex as trades move onto competing electronic trading venues. A Securities and Exchange Commission committee this week moved to help.

The Fixed Income Market Structure Advisory Committee proposed the SEC adopt new reporting standards aimed at improving transparency and helping traders decide which electronic marketplaces to frequent.

Stakes are high in the proposed regulatory overhaul for publicly listed electronic bond trading platforms such as MarketAxess Holdings Inc., MKTX 0.70% Tradeweb Markets Inc. TW -0.63% and Intercontinental Exchange Inc., ICE -0.05% or ICE. The exact terms of the definition the SEC adopts could raise or lower each venue's reported market share, and the value of their stocks.

"You can't ignore the importance of this to investors in the electronic trading platforms," said Kevin McPartland, head of market structure research at Greenwich Associates.

The committee proposed the SEC adopt a clear definition of electronic trading in corporate and municipal bond markets. A uniform definition would capture a broader range of trades, avoid double-counting them and standardize reporting across different venues, according to a recommendation released at a committee meeting on October 5.

Unlike stocks, which mostly trade on listed exchanges, bonds trade over the counter, and the electronification of the market has been fragmented as financial technology companies have offered traders competing options to find buyers and sellers.

"The recommendation this week is trying to tackle the fact that electronic venues all report their trading volumes and estimates differently, so it's very difficult for any market participant or regulator to get an accurate picture of what's going on," said Rick McVey, chief executive officer at MarketAxess and a member of the SEC committee.

"Transparency and investor confidence are essential to efficient markets, and considered regulation of fast-growing electronic protocols and platforms makes a lot of sense," Tradeweb CEO Lee Olesky said. A spokesman for ICE declined to comment.

Electronic bond trading has grown since the March market crisis, when investors rushed to raise cash by selling bonds. The increase was sharpest in high-yield bonds, about 22% of which were traded electronically in August compared with 17% in February before the pandemic hit the U.S., according to data from Greenwich.

Still, trading air pockets at the height of the panic exposed liquidity shortfalls in municipal and corporate bond markets. The market freezes renewed concerns about liquidity—a term sometimes used to describe how easily traders can buy and sell at a stable price—but inconsistent reporting of electronic trading has made postmortem analysis more difficult.

"Determining the effect of electronic trading on liquidity conditions and transaction costs over time is difficult," the SEC committee said in its recommendation.

In government bond markets, the yield of the 10-year Treasury rose to 0.784% Wednesday from a close of 0.741% Tuesday, according to data from Tradeweb.

The Wall Street Journal

By Matt Wirz

Updated Oct. 7, 2020 5:24 pm ET

Libor Law Is Adrift in Albany and Wall Street Is Getting Nervous.

- **End of Libor is trouble for many contracts without backup rate**
- **Proposed legislation to address issue has made little headway**

For the past seven months, an arcane financial-markets proposal has been collecting dust in the statehouse halls of Albany, New York. Between the pandemic and the racial-justice protests, lawmakers have been so preoccupied that no one in either chamber has even initiated the legislative process on it.

But to bankers, investors and regulators, this is no run-of-the-mill document. It's a proposal that's crucial to ensuring that a huge swathe of the global financial system, involving deals worth potentially trillions of dollars, doesn't turn into a chaotic, lawsuit-riddled mess when the London interbank offered rate is officially discontinued at the end of next year.

And while that still leaves 15 months to hammer out a solution, Albany is not expected back in session until January, and anxiety is already mounting among those on Wall Street who had originally expected the proposal to sail through the legislative process in the Spring.

So many contracts will fall into legal limbo without the legislation — which would slide a comparable, new rate into deals that don't have provisions for a backup — that bankers say there's really no way to try to renegotiate all of them, or even a fraction of them, in the run-up to Libor's expiration. Which leaves them with little recourse for now beyond lobbying state lawmakers.

"We continue to have conversations with key stakeholders and we're trying to move this forward," said Tom Wipf, vice chairman of institutional securities at Morgan Stanley and chairman of the Federal Reserve-backed group guiding the U.S. Libor transition. "We've put forward something that has broad benefits for a wide range of market participants."

It is certainly rare for a decision like this — with such massive repercussions for the world of finance — to be made in upstate New York.

It's a consequence of the outsize role state law plays in governing the roughly $200 trillion in securities and commercial transactions tied to U.S. dollar Libor. The draft bill would guarantee financial products that lack viable language to deal with the benchmark's end are shifted to a replacement, known as the Secured Overnight Financing Rate. SOFR currently sits at about 0.1%, slightly below three-month Libor.

Global regulators have remained steadfast that the timetable for doing away with Libor remains on track, despite the coronavirus outbreak causing a number of near-term goals and milestones to be pushed back.

Yet it's also clear that there's growing concern over how long the legislative process is taking. The Fed-backed Alternative Reference Rates Committee had originally hoped the "urgently needed" legislation would pass by May.

"Substantial delay or uncertainty may lead to some pricing dislocations" in markets if it persists too deeply into 2021, said Michele Navazio, a partner at law firm Seward & Kissel LLP. "I don't have to emphasize that increased uncertainty often leads to liquidity problems and volatility."

The law would impact everything from adjustable-rate mortgages and municipal debt to collateralized loan obligations and complex financial derivatives.

One of the asset classes most affected would be floating-rate bonds, many of which would effectively be convert to fixed-rate notes based on Libor's final print in the absence of a legislative solution. That's because they typically require unanimous consent from holders to change their benchmark rate.

For about $1.8 trillion of Libor-linked securitizations tied to auto loans, credit card receivables and other types of debt, there's the added risk that the structures and the underlying assets could transition from Libor using distinct methodologies, creating a cash flow mismatch. That could lead to liquidity disruptions and a potential wave of lawsuits.

And it's not just Wall Street that would be affected. There's about $1.2 trillion of adjustable-rate U.S. residential mortgages linked to Libor. Contract language generally gives noteholders discretion to choose a replacement rate. Different lenders could wind up using different benchmarks, leading to unequal outcomes for home owners. The proposed law would encourage all lenders to use the ARRC's recommended fallback rate by offering protection from litigation.

Sponsor Sought

To pass, the draft legislation first needs either a state senator or assembly member to sponsor it. It could alternatively be included as part of a larger bill package, such as the governor's budget. Either way, it would ultimately need to clear both chambers and be signed by the governor to become law.

So far, no backers have stepped forward.

"Failure to get legislation passed can create enormous economic and legal uncertainty in the legacy Libor world," said Priya Misra, head of global rates strategy at TD Securities in New York. "The courts could well be overwhelmed," said Misra, who is TD's representative on the ARRC.

Before she gives her support, Democrat Liz Krueger, chair of the New York Senate Finance Committee who represents the Upper East Side of Manhattan, says she wants the bill to ensure that borrowers with exposure to Libor via consumer products will get the lowest interest rate available among potential replacement benchmarks.

"I want to make sure that the less-represented party doesn't get a fast one pulled off of them," Krueger said. "I'm not really worried that New York state won't watch out for its financial interests in these changeovers, but I don't know whether a million New Yorkers with consumer loans through 300 different banks are really going to be able as a group to watch out for their interests."

If there was a sign of movement on federal legislation, Krueger said it would make sense to wait and see what was happening at the national level before moving forward with a state bill.

"I'm cautiously saying that I am willing to move this kind of bill in New York state, as long as I make sure I'm dotting all the i's and crossing the t's, and that there is a need for it," Krueger said.

No Favoritism

The legislation's backers say the delay risks holding up the wider adoption of SOFR as market participants focus on addressing legacy contracts instead of wider transition planning.

"The longer the uncertainty remains, you just have to say that's obviously a greater risk to the market," said Thomas Deas, chairman of the National Association of Corporate Treasurers and the group's ARRC representative.

He says the draft legislation isn't tilted in favor of lenders. Rather, its recommended fallback language includes a replacement-rate calculation based on SOFR plus a spread adjustment that's designed to ensure the successor rate is as close as possible to what the parties originally intended.

"We're not trying to lower the rate so one party gets an advantage, we're trying to make it value neutral," Deas said. "With all respect to the Senate Finance Committee, we're not trying to give a benefit to anybody."

Legal Concerns

The ARRC has also approached the Office of the New York State Comptroller, the State Division of the Budget, and the Assembly's Ways and Means Committee seeking backers, yet to little avail thus far.

Jennifer Freeman, communications director for the comptroller, said the body had not had detailed conversations on the legislation. The Division of the Budget is currently focused on addressing the pandemic and its economic fallout, and will tackle the proposed legislation at the appropriate time, spokesman Freeman Klopott said in an email.

Helene Weinstein, chair of the Assembly Committee on Ways and Means, didn't respond to multiple requests for comment.

Even if the law is eventually passed, there are concerns among lawyers that it won't be able to prevent a rush of lawsuits as Libor's end approaches.

While many legacy contracts are governed by New York law, those that aren't would likely need separate legislation.

And borrowers or lenders affected by the new law could argue that changing contractual terms retroactively is unconstitutional, according to Jonathan Ching, a partner at Linklaters LLP.

"Given the number of affected parties, it would not be surprising to see all sorts of challenges arise if and when a bill is introduced," Ching said. "The big concern at the moment is that if enacted, the legislative solution would just change the nature of the litigation."

Bloomberg Markets

By William Shaw and Keshia Clukey

October 8, 2020, 3:00 AM PDT

More Unknowns to Come for Issuers, FIMSAC Members Say.

State and local governments will have to deal with many unknowns as 2020 wraps up, and figure out how to disclose pandemic concerns as conditions deteriorate for vulnerable credits, experts said at a Securities and Exchange Commission's Fixed Income Market Structure Advisory Committee meeting Monday.

FIMSAC met Monday to discuss various issues facing issuers.

Former SEC Chair and Commissioner Elisse Walter said FIMSAC needs to keep an eye on market structure to see if any changes need to be made to make the market function better, she told fellow members.

“We need to continue to have an eye on transparency and whether or not there are further routes that should be taken in mind, particularly with respect to pre-trade transparency to help investors in this market,” Walter said.

In regards to all types of fixed income, the committee needs to look at regulatory disparities between broker-dealers and alternative trading systems, Walter said. FIMSAC began taken those steps after approving a preliminary recommendation asking for a consistent definition of “electronic trading” and an industry standard for reporting “electronic trading volumes” on Monday.

The committee said there was no consistent standard for publicly reporting trading volumes across the 20 trading platforms currently trading corporate and municipal bonds. Volumes are reported inconsistently and make it harder for analysts to interpret, they said.

Some inconsistencies include reporting venue practices that don?t distinguish between trades that are fully electronic versus processed. Fully electronic trades are those in which all material interactions between the parties to the trade occur through the platform. Processed trades are trades where counterparties negotiate price and other terms away from the venue, but then submit the trade to a venue.

“I understand and support the desire for enhanced transparency,” SEC Chair Jay Clayton said in his written remarks. “Generally, markets and market participants benefit from accurate and consistent trading data, to find liquidity and make investment decisions. I appreciate the Committee’s attention to this important matter.”

This recommendation is related to an SEC concept release from last week. The SEC asked for comment on whether the current regulatory structure for alternative trading systems needs to be changed.

Major broker-dealer groups plan to comment on that release.

Meanwhile, Suzanne Shank, chair, chief executive officer and co-founder of Siebert Cisneros Shank & Co. LLC and member of the committee told members said she expects continued volatility as the year rounds out.

“We anticipate volatility to continue and to stall as municipal issuers really grapple with budgetary distress, which will hinge on news around vaccine developments and other stimulus package passages, if there is one with aid to state and local governments,” Shank said. “Of course, if there is any disruption surrounding the election results, we would expect that to contribute to volatility.”

Lawmakers have yet to pass another relief bill, and it is becoming less likely as election season nears. House Democrats approved a $2.2 trillion HEROES Act late last week without Republican support. It would include $436 billion in direct state and local aid.

Over the next few months, there will be a wider difference between the “haves and have-nots,” Shank said. Issuers with robust rainy day funds will be better positioned compared to challenged credits that hinge on hospitality, which will continue to struggle, she said.

Issuers are also grappling with how much to disclose because they are dealing with a lot of unknowns, Shank said.

The Municipal Securities Rulemaking Board tracks the number of COVID-19-related disclosures and publishes that data on a weekly basis.

To date, state and local government issuers have filed over 20,000 disclosures with the MSRB that reference the pandemic, said Mark Kim, FIMSAC member and MSRB CEO.

Many stakeholders have wondered in actuality how many issuers have submitted the disclosures.

Based on using the base CUSIP as a proxy, Kim said they found about 12,600 issuers had submitted disclosures that referenced COVID-19 to date. The muni market has over 50,000 municipal issuers total.

"If you take that universe of all the distinct CUSIP-6's that have traded in 2020, approximately 40% of those CUSIPs have a COVID-19 related disclosure associated with it," Kim told FIMSAC members.

CUSIP-6 identifies the bond issuer.

The Bond Dealers of America believe reasonable efforts to improve the clarity and transparency of trade reports are welcome, such as the recommendation approved Monday.

The American Securities Association said the recommendation will help more trading venues register and be under the SEC's supervision.

SEC commissioners also voiced their support to extend FIMSAC's term to March 2021 during the meeting Monday.

By Sarah Wynn

BY SOURCEMEDIA | MUNICIPAL | 10/05/20 03:37 PM EDT

Taxing Disclosures: Municipal Securities Issuers and COVID-19

As discussed in my earlier blog, "SEC Focus on Municipal Securities: Disclosure and Enforcement – The Peculiar Structure of the Municipal Securities Disclosure Regime," since 1994 issuers and, in the case of conduit issuers, obligated parties are required to enter into a Continuing Disclosure Agreement ("CDA") at the time of issuing municipal securities. Under a CDA, the issuer (or obligated person, or both) must post a Material Event Filing ("MEF") within ten business days of occurrence, and since 2008, that posting must be made on the Electronic Municipal Market Access ("EMMA"). Failure to comply with these requirements will lead to enforcement much like that which a public company would face under the Securities Exchange Act of 1934, as amended if the public company does not meet its disclosure obligations (such as press releases, filing Current Reports on Form 8-K, etc.) The particular challenge facing municipal securities issuers in the face of the COVID-19 pandemic is how to address in a timely manner and clear away the impacts of COVID-19 on the revenues of municipal securities issuers, as well as on the costs of governmental operations. Fortunately, municipal securities issuers have been given guidance in the form of recommended best practices developed by an industry group, the Disclosure Industry Working Group ("DIWG"), the "General Continuing Disclosure Considerations for Municipal Securities Issuers" (the "CDC"), which was published in August 2020.

Taxing Disclosures

The DIWG, which includes bond lawyers, issuer officials, municipal securities analysts, and municipal advisors, was founded in July 2019 under the leadership of the Government Finance Officers Association ("GFOA"). Founded in 1906, the GFOA is a trade association with over 20,000 members, who are finance officials in federal, state, provincial, and local governments in the United States and Canada. The DIWG was formed to seek improved and more timely disclosure due to the significant increase in scrutiny by the U.S. Securities and Exchange Commission ("SEC") of the quality and promptness of municipal disclosures. The GFOA had met with SEC Chair Jay Clayton and other commissioners in June 2019, following Chairman Clayton's call for the SEC Office of Municipal Securities to work with the Municipal Securities Rulemaking Board to improve municipal securities disclosure. One can readily conclude that forming the DIWG was and is a defensive move to try to forestall more frequent and aggressive enforcement actions. Nonetheless, the CDC does provide helpful reminders and guidance. This first product of the DIWG, said Emily Brock, Director of the GFOA's federal liaison center, is intended "…to improve disclosure without input from regulators." The DIWG had significant disagreements among its members as to what to put in any group document, but that situation was fundamentally changed by the pandemic. The DIWG has stated that: "We recognize that this is our problem and rather than a regulatory mandate, we thought it would be best … to work together and show the SEC and other parties… that we can work together and … {offer} solutions to address … timely disclosure."

One particular part of the CDC stresses the need for "good investor relations," which involves "… facilitating widespread and contemporaneous access to information" to ALL investors. This section was of critical importance to the National Federation of Municipal Analysts ("NFMA") and had to be in the document in order for the NFMA to support its issuance. A good part of the CDC is devoted to the need to recognize diligently the obligations inherent in a CDA, and to administer compliance with professionalism and care. This surely reflects concerns (raised by SEC comments and the formation of the DIWG itself) that too often municipal securities issuers do not devote adequate attention and/or resources to meeting those obligations, and do not adequately administer the disclosure regime applicable to them. For example, the CDC notes that the SEC has NOT relaxed the reporting requirements of issuers under their CDA's, both as to MEF's AND as to the annual filing requirement. As to the latter, the CDC emphasizes the need to know the date that the annual filing is due. The CDC also discusses at length the need for municipal securities issuers and obligated persons to consider voluntary disclosures relating to the impact of COVID-19, specifically making clear that revenue or budget projections should be official government estimates, and clearly marked as unaudited financial information. The CDC cites, in this regard, an SEC statement of May 4, 2020, which encourages municipal securities issuers and obligated persons to provide investors with forward-looking information regarding the impact of COVID-19. The SEC statement suggests that the issuer may want to add "…meaningful cautionary language…, "and notes that "good faith forward-looking information will not be second-guessed by the SEC."

Finally, the CDC reminds municipal securities issuers and obligated persons that NONE of the federal tax requirements related to the tax treatment of municipal securities have been suspended in the face of the pandemic. So issuers remain obligated to make federal arbitrage rebate and yield reduction payments. Issuers are also still subject to the private use regulation and must comply with other obligations related to tax-exempt bond issuances.

Municipal Securities Issuers and COVID-19

The CDC is helpful, BUT only if municipal securities issuers and obligated persons invest adequate time and resources in carrying out the steps it recommends. Neither the quality of municipal disclosure nor the quality of mercy need be strained IF issuers and their officials and advisors act promptly, in good faith, to keep investors informed – even in the face of a pandemic.

by Peter D. Hutcheon

Thursday, October 1, 2020

MSRB Municipal Securities Market COVID-19-Related Disclosure Summary.

Last Updated: Oct 05, 2020 for the Week Ending Oct 04, 2020

Read the MSRB Report.

A Technology Solution For Muni Bond Disclosure.

This article is the fifth of a six-part series on investor disclosure in the municipal bond market.

The previous article, *Muni Bond Market Disclosure: Thoughts From Standard-Setters And Stakeholders*, discussed how other stakeholders in the municipal bond market, such as the Governmental Accounting Standards Board and the National Federation of Municipal Analysts, have also contributed to creating a disclosure framework.

This article discusses how, just as the then-new technologies of a decade ago transformed disclosure in the municipal bond market, today's current technologies and data sciences portend further transformations. And, just as before, there are those that embrace them—and those that oppose them. History has shown that one thing is certain: technology keeps moving forward. Like it or not. Those that embrace it tend to succeed. Those that don't, fail.

Continue reading.

Forbes

by Barnet Sherman

Sep 30, 2020,11:19am EDT

Treasury's OIG Updates FAQs for Coronavirus Relief Fund Reporting Requirements.

On September 21, the Department of Treasury's Office of Inspector General (OIG) updated their Coronavirus Relief Fund (CRF) FAQs on reporting requirements.

The document swapped out guidance initially released on August 28, following complaints about the guidance by the OIG conflicting with guidance issued by the Treasury on August 10 regarding reporting payroll expenses for public health and public safety employees determined to have "substantially dedicated" their time in responding to the COVID-19 public health emergency.

The updated FAQs provide more flexibility to CRF prime recipients by implementing "administrative accommodations made in accordance to Treasury's FAQs."

View Updated Document.

Government Finance Officers of America

Disclosure Industry Working Group Encourages Timely Covid-19 Disclosures.

The Disclosure Industry Working Group reminds issuers that applicable filing deadlines have not been extended by either the U.S. Securities and Exchange Commission (SEC) or the Internal Revenue Service (IRS), and encourages all issuers to discuss COVID-19 disclosure with their entire financing team, including their bond and/or disclosure counsel. In its publication, General Continuing Disclosure Considerations for Municipal Securities Issuers, which includes those considerations related to COVID-19 financial matters, the working group provides guidance regarding the following topics:

- **Material Event Filings:** A Material Event Filing must be completed within 10 business days of the occurrence of a Material Event; notwithstanding the pandemic, the SEC has not relaxed these reporting requirements under SEC Rule 15c2-12 of the Securities Exchange Act.
- **Knowing Your Annual Disclosure Filing Dates:** Notwithstanding the pandemic, the SEC has not suspended the annual disclosure filing requirements under SEC Rule 15c2-12 of the Securities Exchange Act.
- **Annual Continuing Disclosure Filings:** If all or a portion of the annual continuing disclosure information is not available by the filing deadline, issuers (and obligated persons) must file a failure-to-file notice. The working group notes that it is important to include the reason(s) as to why any part of the submission is late.
- **Good Investor Relations:** With respect to information given to investors and rating agencies, issuers (and obligated persons) may want to consider disclosing the same information on their websites or via a filing on the Municipal Securities Rulemaking Board's Electronic Municipal Market Access (EMMA) system.
- **Determining Whether and/or When to Make Voluntary Disclosure Filings:** Issuers (and obligated persons) may be facing fiscal challenges due to the COVID-19 pandemic. Issuers (and obligated persons) should discuss the appropriateness, the contents and the context of voluntary disclosure of such fiscal challenges with their bond counsel and/or disclosure counsel.
- **Presenting COVID-19 Voluntary Disclosure Information:** As discussed in the SEC public statement on May 4, 2020, Chairman Jay Clayton and Rebecca Olsen, Director of the SEC's Office of Municipal Securities, encourage municipal issuers to provide investors with forward-looking information regarding the impact of COVID-19 on their financial and operating conditions.
- **EMMA Filings:** All filings on EMMA should be submitted for all relevant CUSIP numbers, and may be filed under multiple filing categories on the EMMA system.
- **Post-Issuance Compliance for Tax Law Purposes:** The IRS has not suspended the post-issuance responsibilities of issuers of municipal debt.

McCarter & English LLP – Sarah C. Smith

September 17 2020

BDA Washington Weekly – Muni Provisions Sidelined

For the past few weeks, it appeared that Congress was headed towards a government shutdown, in the middle of a pandemic, less than 6 weeks to a presidential election, with no deal in sight. This week, cooler heads prevailed, and disaster has been adverted-for now.

House Leadership, along with Trump Administration officials struck a short term deal mid-week and fast tracked the legislation through the House with a strong bipartisan vote. The bill is expected to pass the Senate next week. **Attached to the package is a years-long extension to the Surface Transportation reauthorization that does not include municipal bond provisions.**

Not to be forgotten is the death of Supreme Court Justice Ruth Bader Ginsburg, which will have direct impact on the Senate schedule, dampening the hopes of additional stimulus and aid to state and local governments. Though House Speaker Pelosi is attempting to revive talks with a narrow compromise bill, a long shot effort to pass legislation prior to the election.

This week, the BDA kicked off its new podcast series titled Bonding Time with an episode focused on muni happenings in Washington, DC. The podcast features Emily Brock of the GFOA Federal Liaison Center and the discussion focuses on issues such as stimulus, infrastructure and politics.

The inaugural Bonding Time podcast can be found here

Legislative Recap:

Congress Avoids Shutdown – Muni Provisions Sidelined

In the midst of a national health and economic crisis, Congress appeared poised to add gasoline to the fire by allowing government funding to lapse. This appears to have been avoided, at least in the near term, but in doing so Congress has dashed any hope that BDA priorities such as the restoration of advance refundings, expansion of PABs, or the raising of the BQ debt limit will happen in 2020.

As part of the negotiations, both House, Senate and administration officials agreed to extend the Surface Transportation Reauthorization through FY 2021 at current levels. This means that the House legislation that included many municipal market priorities are tabled likely through the remainder of 2020. There is still an outside chance for negotiations for a new stimulus deal, especially post elections in the lame duck session. However, at this time it is hard to see both Chambers and the White House coming together for a deal robust enough to include municipal bond provisions.

While a disappointing outcome, this is not an unexpected maneuver. The BDA continues to advocate for these provisions, along with our partners in the Public Finance Network, and believe that they are well positioned for consideration in 2021 regardless of outcome of the elections.

Dems Press Fed Chair to Expand MLF

In a marathon week of Congressional testimony for the Federal Reserve Chairman Jay Powell, the House Financial Services Committee pressed the Chair to expand the Municipal Liquidity Facility, noting that interest rates are still too high resulting little assistance to state and local governments with only two issuers accessing the program.

The Chair defended the program by stating, *"What that facility has accomplished is it opened up the private market so state and local governments are borrowing in record amounts at record low yields,"* avoiding the calls to lower the pricing of the securities.

This point of view was reiterated last week during a CARES Act oversight hearing in which Senator Pat Toomey (R-PA) called for the ending of the program with his rationale being that if only two issuers have used the program and the market is stabilized, thus it is unneeded.

The House also passed legislation this week that would require the Federal Reserve and the Treasury Department to expand the number of credit rating firms allowed to participate in Covid-19 financial market support programs.

The bill would intervene in the Fed and Treasury's bond-buying programs by forcing them to accept securities rated by any credit rating agency recognized by the SEC.

Since summer hearings on the issue, a bipartisan group of House lawmakers has continued to press the Fed and Treasury to expand the list of rating agencies beyond the three dominant ratings firms — Standard & Poor's, Moody's and Fitch. Under the bill, the Treasury and Fed would be able to exclude certain ratings if they're deemed unreliable or inaccurate for a particular asset class.

Fed Recap:

Fed Chair Calls on Congress to Provide Relief

Chairman Powell this week continued to urge Congress to take further actions to support the stalling U.S. Economy. While noting the CARES Act helped to vastly improve the national economic situation, he noted that the path ahead is uncertain as monies allotted in the legislation expires.

Powell has long been in favor of additional aide to state and local governments and further reiterated that position on the Hill this week. The Chairman also continue to praise Fed lending programs such as the Main Street Lending program and the MLF stating they help unlock liquidity and assisted the U.S economy in reversing the March loses.

Bond Dealers of America

September 25, 2020

Muni Bond Market Disclosure: Thoughts From Standard-Setters And Stakeholders

This article is the fourth of a six-part series on investor disclosure in the municipal bond market.

For decades, the issues surrounding disclosure in this $3.9 trillion market have vexed municipal bond borrowers and investors alike. Now, with both governments and nonprofits reeling from the adverse financial effects of Covid-19, municipal bond disclosure is back on the front burner. The public health crisis may prove the tipping point needed to finally resolve the market's disclosure issues.

The previous article, *Muni Bond Market: In Dogged Pursuit Of A Disclosure Framework*, covered the unflagging efforts of the Securities and Exchange Commission (SEC) and the Municipal Securities

Regulatory Board (MSRB) to sometimes guide and sometimes impose disclosure rules and standards in that market.

This article discusses how other market stakeholders and standard setters have shaped municipal bond disclosure—and continue to actively work to improve it.

Continue reading.

Forbes

by Barnet Sherman

Sep 25, 2020

Regulatory Spillover: Evidence from Classifying Municipal Bonds as High-Quality Liquid Assets

In the aftermath of the 2008-2009 financial crisis, the Basel Committee on Banking Supervision (BCBS) strengthened banks' liquidity regulation by requiring banks to maintain a minimum liquidity coverage ratio (LCR). This ratio is defined as high-quality liquid assets (HQLA) divided by estimated total net cash outflows during a 30-day stress period. Whether municipal bonds should be classified as HQLA in computing this ratio and the resulting economic consequences are subject to intense debate. Issuers of municipal bonds contend that municipal bonds should be classified as HQLA based upon their safety and liquidity profiles. In contrast, the U.S. banking regulators questioned both the liquidity of these bonds and the claim that municipalities would be affected and excluded municipal bonds from HQLA in the final rule issued in 2014. However, less than a year later, in an abrupt reversal, the Federal Reserve Board (FRB) unilaterally decided to include general obligation municipal bonds in the measurement of HQLA while continuing to exclude revenue municipal bonds. Exploiting this policy reversal, Jacob Ott of the University of Minnesota examines two potential spillover effects of the classification of general obligation municipal bonds as HQLA: (1) if there is a change in the yield spread of general obligation bonds relative to revenue bonds; and (2) if municipalities change their pattern of issuance of general obligation bonds relative to revenue bonds.

Ott finds that changing the measurements used in bank liquidity management can have spillover effects, specifically that classifying a general obligation municipal bond as a high-quality liquid asset in the regulatory accounting for the liquidity coverage ratio has a spillover effect by influencing municipal market pricing and behavior. In addition, the reduction in financing costs of general obligation bonds appears to influence municipalities' issuance decisions. This effect is magnified in the cross section of highly rated municipalities. Finally, Ott finds some indirect evidence for the proposed mechanism: a change in banks' investment behavior.

This paper contributes to several veins of literature, but also has important policy implications. The effects this paper discusses are the result of changing municipal bonds to Level 2B assets. Many different entities (e.g., banks, politicians, trade groups, etc.) have requested Level 2A treatment. It may be the case that the results of this paper would be strengthened in magnitude if this change was made. For example, municipalities could potentially be able to borrow at even lower rates under Level 2A treatment. The lack of Level 2A treatment may put U.S. domiciled municipalities at a disadvantage in maintaining and improving infrastructure relative to municipalities in other countries who do treat municipal bonds as Level 2A in their liquidity management regulations. However, it is important to note that this study does not examine if classifying general obligation bonds as high-quality liquid assets is an optimal decision for the purposes of liquidity management.

[Read the full paper here»]

The Brookings Institution

by Jacob Ott

September 21, 2020

[SEC Focus on Municipal Securities: Disclosure and Enforcement – The Peculiar Structure of the Municipal Securities Disclosure Regime]

When the two key Federal Securities Laws (the Securities Act of 1933 [the "33 Act"] and the Securities Exchange Act of 1934 [the "34 Act"]) were enacted, municipal securities (the bonds, notes, etc., issued by states, counties, municipalities, and municipal authorities) were exempt, both from the registration requirement of the 33 Act and from the oversight under the 34 Act of the professionals who underwrote and dealt in the purchase and sale of these securities. These exemptions resulted from policy (municipal securities were generally seen as more secure than those issued by corporations and other private sector entities) and political considerations. More individual investors sought to buy municipals by the early 1970s to reduce federal and state tax liabilities, at a time of ever-increasing inflation. This in turn led to an extraordinary proliferation of municipal security products. Then Congress passed the Securities Act Amendments of 1975, creating the Municipal Securities Rule Making Board ("MSRB") as a self-regulatory body subject to the oversight of the U.S. Securities and Exchange Commission ("SEC").

The Peculiar Structure of the Municipal Securities Disclosure Regime

In 1978, the MSRB adopted rules governing underwriting practices, urging "market participants" (i.e., broker/dealers, investment advisers, and the like) to comply with disclosure obligations consistent with those that the SEC required in connection with the registration and sale of securities under the 33 Act. It should be noted that, unlike the registration process (where the disclosure obligations fall on the issuer), in the case of municipal securities those obligations fall on market professionals. Disclosures concerning a municipal security (both as to the issuing entity and the terms of the security) are typically found in a Preliminary Official Statement ("POS"), followed at the time of issuance with an Official Statement ("OS"). The POS and OS are usually prepared by the underwriters in conjunction with the issuing entity and are expected to be reviewed by any broker/dealer involved in selling the security and by any investment adviser recommending the security. This somewhat "Rube Goldberg" disclosure structure reflects continuing political decisions to eschew direct federal regulation of municipal security issuers, including disclosure of material developments following issuance.

In 1989, the SEC adopted Rule 15c2-12 under the 34 Act, which requires an underwriter of municipal securities to obtain a written agreement from the issuer requiring the issuer (and any related obligor, as in the case of conduit issuers), to deliver an OS within seven days of issuance. Under the Rule, underwriters are also required to review the POS and the OS for the adequacy and completeness of the disclosures. In 1994 the SEC amended Rule 15c2-12 to also require the underwriter to obtain a written agreement (a Continuing Disclosure Agreement ["CDA"]) from an issuer of a municipal security, under which the issuer (and any related obligor) commits to provide annual updates on the issuer's financial condition. In addition, both the Rule and the CDA require the issuer to file "timely reporting of material events" affecting the issuer (or any related obligor). Originally both the OS and disclosures under the CDA were filed with designated depositories. In 2002 the MSRB required that these filings be done electronically. In 2008, the MSRB launched the Electronic Municipal Market Access ("EMMA") website. All OS's and CDA disclosures are now filed on EMMA. Any market professional dealing in municipal securities is required to review those filings prior to effecting transactions.

Increasing SEC Enforcement Activity

In January 1996, the SEC brought an enforcement action against the principal officials of Orange County, California (ironically including its Treasurer, Robert Citron, whose last name is the French word for "lemon") for massive misstatements and omissions in disclosure documents covering 11 bond offerings from July 1, 1993, to September 28, 1994, which raised over $2.1 billion. In addition to material errors about the tax treatment of some of the offerings and continuing failures to disclose the deteriorating financial condition of the county, there was a failure to disclose that the county tried to greatly increase revenues by attempting to hedge payment obligations on the bonds with "earnings" on short-term reverse repurchase agreements. When interest rates went against the county's "bets," the County experienced such great financial losses that it was forced to file bankruptcy under Chapter 9 of the Federal Bankruptcy Act. The county filed on December 9, 1994, and made its final payment under the court-approved reorganization plan on July 1, 2017.

In 2010, the SEC brought its first-ever enforcement action against a state – New Jersey. The SEC asserted that the POS's and OS's used for the offer and sale of over $26 billion of bonds in 79 separate bond offerings from August 2001 through April 2007 contained material misrepresentations and omissions about the underfunding of New Jersey's two largest pension plans (one for teachers, the other for State employees). There had been no payment default on any of the bonds (a situation that continues to date). New Jersey consented to a settlement in which it accepted a cease and desist order; it was not subjected to a civil penalty. Illinois suffered a similar fate in 2013 for failing to adequately disclose pension shortfalls in connection with the sale of over $2.2 billion in bonds from 2005 to early 2009.

Beginning in 2014, the SEC undertook an initiative to identify material misstatements and omissions in municipal security offering documents from 2011 on. As a result, the SEC found that 71 issuers (and in some cases, related obligated persons) had inadequate POS's and OS's relating to new securities issuances. In some cases, they also found that the issuers had not met their obligations under the CDA's related to those or previously outstanding issuances. All 71 issuers eventually settled with the SEC and accepted cease and desist orders. On September 14, 2016, the City of Miami and its former budget director were found liable for securities fraud in connection with the sale of $153.5 million of bonds. The offering documents failed to disclose that the value of the city's reserves were materially overstated (by illegally transferring capital funds to the city's General Fund), resulting in significantly higher ratings from bond rating agencies. Both the city and the former budget director were permanently enjoined from engaging in securities fraud. The city settled the case by paying $1 million; the former budget director, whom the court found did not personally profit from the fraud, was ordered to pay $15,000.

In April of 2016, the SEC charged the town of Ramapo, New York, along with the town supervisor (who doubled as president of the municipality's Development Corporation ["RLDC"]), an assistant town attorney (who doubled as executive director of the RLDC), two other municipal officials, and the RLDC with securities fraud in connection with 16 bond offerings from 2010 to 2015, which raised over $300 million. The primary basis of the material misstatements in the offering documents was the failure to disclose the impact of the expenditure of over $58 million to construct a minor-league baseball park for the town's Ramapo Boulders – presciently-named, as this became the proverbial "millstone" around the necks of the defendants. The United States Attorney brought parallel criminal proceedings against the town supervisor and the assistant town attorney. In October 2018, the town and the RLDC consented in the SEC lawsuit to injunctions; the town supervisor paid a $327,000 civil penalty; the two other municipal officials paid civil penalties of $25,00 and $10,000 respectively; and all four were collaterally barred from serving as officials of a municipal entity. The two other officials were able to apply for release from the bar after a term of years. The assistant town attorney pled guilty in the criminal action, was fined $10,000, sentenced to 18 months supervised release, and disbarred. The town supervisor was convicted by a jury on 20 counts and sentenced to serve 30 months in prison and pay a fine of $75,000.

In November 2017, the SEC brought a lawsuit against the Town of Oyster Bay ["TOBAY"] (a part of Nassau County, Long Island, New York, where the author of this blog grew up; TOBAY has a dedicated portion of Jones Beach set aside for TOBAY residents), and the town supervisor for failing to disclose in 26 offerings from August 2010 to December 2015 that the town had guaranteed four private loans totaling over $20 million to a restauranteur in connection with his operating restaurants and concession stands on town property (theoretically at TOBAY Beach). TOBAY was permanently enjoined. The town supervisor was acquitted in a criminal prosecution for official corruption; the resolution of the SEC's civil lawsuit against him was not reported.

The SEC Provides an "Education" in Disclosure Obligations

In March 2019, the SEC brought a civil lawsuit against the former controller of the College of New Rochelle, a non-profit college located in Westchester County, just north of New York City. The college was under financial duress due to declining enrollment and deteriorating collection of pledged donations. The controller created false financial records and failed to pay payroll taxes so that the college's financial statements for 2015 had overstated net assets by almost $34 million. He also certified those statements. What he failed to do was file timely disclosures under the CDA relating to an outstanding 1999 bond issue. Due to its self-reporting of the matter and exemplary cooperation, as well as its difficult financial condition, the college was not charged and no penalty was sought. The controller, who was also charged in a parallel criminal action for securities fraud, pled guilty in the criminal case and reached a partial settlement with the SEC that permanently enjoined him from future misconduct, with civil penalties to be determined by the court. Six months later the SEC brought suit in federal court in California against the former chief business officer and the superintendent of schools of a school district in connection with falsified disclosures relating to the 2016 offering of $100 million of the district's general obligation bonds. The district's independent auditor had repeatedly sought to investigate allegations of fraud and internal control issues. The district refused to pay the fees for that investigation, and instead terminated the auditor. The chief business officer used the prior year's clean audit as part of the 2016 offering documents and provided "deceptive updates" to the attorneys who worked on the disclosures for those 2016 documents. The district and the superintendent agreed to settle with the commission, consenting to the entrance of cease and desist orders. The superintendent, who signed the OS, was also ordered to pay a $10,000 civil penalty. The case against the former chief business officer seeks injunctive and collateral bars, as well as financial penalties, for his active misconduct.

This year brought an expanded scope of "educational" opportunities in the charter school context. First, in April 2020, the SEC charged the then chief executive officer AND the then director of finance of the Tri-Valley Learning Corporation, which operates two charter schools in Northern California, with misleading investors who purchased $25.54 million in bonds in a May 2015 offering.

The two individuals helped prepare and signed the POS and the OS, which failed to disclose serious cash flow problems, inability to service payments on the bonds, delinquency on payables, non-payment of a term loan over one year overdue, and that the school had fully drawn on its bank line of credit. The same two signed demonstrably false certifications that the POS and OS contained no material misrepresentations or omissions. The individual defendants agreed, in a settlement with the commission, to be permanently enjoined from securities law violations and from participating in future municipal securities offerings, and in addition, to pay a civil penalty of $20,000 and $15,000 respectively. Most recently on September 14, 2020, the SEC charged a state-funded nonprofit charter school in Arizona and its former president with misleading investors in a $7.6 million offering in April 2016. The charter school was experiencing significant operating losses and was "staying afloat" by making repeated unauthorized withdrawals from two reserve accounts to cover "routine" operating expenses, pay other debts, and transfer money to affiliated entities. The offering documents did not disclose this but instead contained profit and expense projections showing profitability in fiscal 2017 and a clear ability to repay the debt. Both the charter school and its former president agreed to settle with the commission, becoming subject to an injunction against future violations of the Federal Securities Laws. In addition, the individual defendant agreed not to be involved in any future issue of a municipal security.

Closing Observations

It seems quite clear that persons acting in the municipal securities markets, including public officials and local educators, are not all well-informed. "Educational" lessons from the SEC can prove costly and destructive of both careers and reputations, let alone possible exposure to criminal prosecution. The design, functioning, and assessments of municipal securities markets are necessarily critical to achieving both fairness and liquidity when raising private capital for public purposes. It behooves financial professionals and others to learn the disclosure rules, and even more importantly, to strive for clarity, completeness, and compliance.

The National Law Review

by Peter D. Hutcheon

September 22, 2020

Peter D. Hutcheon practices primarily in the areas of business governance, commercial transactions, securities, banking, and finance.

Peter counsels management of public and private companies and banking institutions on governance matters. He also has particular expertise with respect to indemnification and insurance issues affecting directors and officers. Peter has represented parties in major public-private partnership financings. He also represents clients seeking investment capital from private placements, venture capital, and private…

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SEC Charges Former Jefferies Registered Representative for Improper Retail Orders in Municipal Bond Offerings.

September 22, 2020 – The Securities and Exchange Commission today filed settled charges against Eliseo Sampayo, a former registered representative at Jefferies LLC, for his improper conduct involving the submission of retail orders in new issue municipal bond offerings.

According to the SEC's order, between October 2016 and August 2017, Sampayo, of Larchmont, New York, improperly placed retail orders for new issue municipal bonds on behalf of a registered broker-dealer that was attempting to buy bonds for its inventory. Municipal issuers typically require underwriters to give retail investor orders the highest priority when allocating new issue bonds, particularly retail investors within the municipal issuer's jurisdiction. The order finds that Sampayo improperly submitted the orders as retail customer orders when he knew or should have known that these did not qualify for retail priority. In addition, the order finds that Sampayo submitted inaccurate zip codes with some of these improper retail orders, which created the appearance that the orders were on behalf of an individual residing in the issuer's jurisdiction when, in fact, they were not, and had the effect of giving the orders priority that should have been reserved for retail customers.

On September 3, 2019, the SEC filed settled charges against the trader who submitted these orders to Sampayo, see Administrative Summary 34-86848.

The SEC's order finds that Sampayo willfully violated the disclosure and fair dealing provisions of Rules G-11(k) and G-17 of the Municipal Securities Rulemaking Board, and imposes a 6-month industry suspension and penny stock bar and a $20,000 civil penalty. Sampayo consented to the order without admitting or denying the SEC's findings.

The SEC's investigation was conducted by the Division of Enforcement's Public Finance Abuse Unit, including Joseph Chimienti, Laura Cunningham, Warren Greth, and Cori Shepherd, with assistance from Deputy Unit Chief Mark Zehner. The investigation was supervised by Ivonia K. Slade.

File No. 3-20047

MSRB Summary Report.

Read this week's COVID-19 summary report, aggregating municipal market disclosures that cite the pandemic.

Muni Bond Market In Dogged Pursuit Of A Framework.

This article is the third of a six-part series on investor disclosure in the municipal bond market.

This piece discusses how both Securities and Exchange Commission (SEC) and the Municipal Securities Rulemaking Board (MSRB) continue to doggedly pursue disclosure improvements in the municipal bond market. Restricted by legislation from accomplishing that by regulating municipal bond borrowers directly, they have wisely applied the substantial powers they have to regulate market participants in order to enforce better disclosure from municipal borrowers. They have also *encouraged what should be disclosed and the framework for that disclosure. But is there a constitutional solution that makes all this legal maneuvering moot?*

In Dogged Pursuit

Limited by the Securities Act of 1933, Securities Exchange Act of 1934 and its founding legislation, the Securities Exchange Act 15B, the MSRB found its ability to compel municipal bond issuers to disclose hobbled.

But it could sure compel the underwriters and broker dealers selling and trading the bonds of those issuers. Having bulked up in 1994 with the adoption of [further amendments to the Rule](), the MSRB flexed its regulatory muscle to "deter fraud and manipulation" in the market. Disclosure was a big part of that deterrence strategy; municipal bond underwriters were compelled to get written disclosure agreements, in compliance with MSRB guidelines, from their bond issuer clients. If broker/dealers wanted to engage in the underwriting and secondary market trading of their primary market bond issues, they were required to get a continuing disclosure statement from an issuer.

No disclosure? No underwriting, no trading.

As the municipal bond market grew (in 1994, there were roughly $1.5 trillion in outstanding bonds compared to nearly $4 trillion today), the rule continued to be amended and expanded. Additionally, new technology was integrated into the solution. The MSRB created "Electronic Municipal Market Access" (EMMA) as the official source for municipal securities data and disclosure documents with mandatory filing requirements. Currently, there are [16 material event disclosures]() codified in the rule, requiring an issuer to post if one (or any) occur.

Constitutional Sidebar

Richard Ciccarone, president of Merritt Research Services (an Investortools Company) and a long-time municipal bond market veteran, offers a different perspective on the legal limitations oft cited in regard to disclosure. Ciccerone has not only given this subject considerable thought, but he dedicated a large part of his career to it. Back in 1986—well before the internet, "'big data," the MSRB, and EMMA—he was tapped to build out a municipal research database and software package that ultimately led to the creation of the Merritt System. Today, Merritt Research Services arguably offers subscribers the longest standardized time-series of municipal financial information in the world, with financial information (including annual audits) on over 12,000 municipal bond credit obligors reporting entities.

Ciccarone contends that the Tower Amendment arguments overlook a constitutional issue, specifically the Commerce Clause. Congress has the power to regulate commerce "among the several states." The sale of a municipal bond—a debt security—across state lines constitutes commerce. Congress (or its agents and assigns—i.e. regulators) can therefore step in to impose rules and regulations on those securities. Issues of sovereignty may apply to any number of things but regulating the disclosure of securities in financial markets is not one of them, in Ciccarone's view. After all, municipal securities dealers fall under the regulation of the Securities Exchange Act 15B specifically because they engage in "interstate commerce to effect any transaction [inducing] the purchase or sale of any municipal security." If the purchase and sale of the goose's eggs can be regulated, why not the goose?

In any legal matter, there is always going to be counterargument. According to some legal-eagles, the reason the Commerce Clause argument doesn't apply to municipal bonds is two-fold. They object, in the first place, to the Goose's Eggs analogy on the grounds that the issuer isn't engaging in interstate commerce; rather, the underwriter is. The issuer's bonds might be sold and distributed across state lines by others, but the issuers themselves aren't doing that. It's a thread-thin line perhaps, but it is a line nonetheless. They also object to the matter of the matter of the sovereignty issue as set forth under Article 10 of the US Constitution. Issuers of municipal bonds are public entities, municipal securities dealers are private entities. This is a crucial regulatory distinction: the feds can regulate private companies, but they cannot impose regulations, at least in this regard, on states.

If there is a legal conflict between the Constitution's Commerce Clause, Article 10, and the Securities Acts of 1933 and 1934, it can only be resolved by one body: the Supreme Court. Currently, there are no cases regarding this matter on the Court's docket.

Encouraging a Disclosure Framework

While the SEC and MSRB might not be able to establish a disclosure framework for the municipal bond market by direct fiat, they actively use their bully pulpit and big stick oversight powers to offer disclosure guidelines to the market and its borrowers. Recently, they took advantage of both.

The SEC and MSRB released a public statement on May 4, 2020, *The Importance of Disclosure for our Municipal Markets*, in which it offered quite explicit guidance to "encourage" issuers on what and how to disclose. (Note the word "encourage" is applied no less than thirteen times in the SEC's May 4 statement. Seven of those specifically refer specifically to municipal issuers, the first one in the introductory paragraph.)

This statement is consistent with the long-standing position on disclosure by these regulators. "Investor access to accurate, timely, and comprehensive information about municipal issuers and their securities has long been a focus of the SEC," stated Rebecca Olsen, the Director of the Commission's Office of Municipal Securities. She continued, "[SEC] Chairman Clayton and I thought it was important to highlight this focus in light of the potentially significant effects of COVID-19 on the finances and operations of many municipal issuers."

Explicit Language

For example, the release explicitly encourages borrowers to provide investors with forward-looking statements during this time, including five very clearly detailed bullet points explaining the why and the how. To those timid souls fretting about potential liability—there are no "safe harbor" rules on the governmental side preventing potential legal action for forward looking statements—the SEC promises that such good-faith, forward-looking disclosure would not be "second guessed".

The regulators didn't stop there. The statement goes on to offer four very specific "examples of information" that might be disclosed, such as Federal, State and Local Aid and Sources of Liquidity. It goes even further. For a "helpful guide" to frame municipal disclosure practices and procedures, it points to Regulation Fair Disclosure (65 FR 51716). Reg FD codifies best practices for corporate issuers. Interpret that as you will, but it sure sounds something like 'if the corporate market can do it, the municipal bond market can too.'

The statement also points to the many reports for "other governance purposes" municipal issuers routinely prepare and release. This provides critical information not only to internal and external government administrators, but to investors as well.

Important point: Reading through all this, one cannot help but notice that the vast majority of this guidance and encouragement outlined here apply regardless of the state of public health. These are just good disclosure practices, regardless of Covid-19. The SEC and MSRB have set out some very clear “best practices.”

These may not be regulations, but the SEC is speaking loudly and has a big stick to back up its statements. It is entirely possible that what is “‘encouraged” now could eventually appear as must-haves in disclosure agreements. Borrowers are encouraged to listen.

Read the first two articles of this series:

Covid-19: The Tipping Point For Municipal Disclosure?

Municipal Bond Market Disclosure: Through The Legal Looking Glass

Next in the six-part series: The SEC and MSRB aren’t the only one’s setting out disclosure standards in the municipal bond market. Investors, borrowers, bond counsel and broker/dealers all have their very distinct—and sometimes opposing—views.

Forbes

by Barnet Sherman

Sep 21, 2020

Charter School Defrauds Bond Holders.

Municipal bonds are sold to fund a variety of local projects. One of the sales features is the local interest. Another can be the tax free income. Thee bonds can thus be a very attractive investment. Critical to the investment is the ability to repay. The necessary information is supposed to be provided to potential investors in the offering documents. If those documents do not have the proper information, as in the Commission’s most recent municipal bond case, investors can suffer significant losses. *SEC v. Park View School, Inc.*, Civil Action No. 3:20-cv-08237 (D. Ariz. Filed September 14, 2020).

Park View School, defendant, is an Arizona nonprofit corporation based in Prescott Valley, Arizona. It operates two charter schools that receive funding from the state of Arizona. That funding is paid in monthly installments beginning in July, the start of the fiscal year. The payments are based on reported school enrollment. The schools submit a budget of anticipated expenses to the Arizona State Board for Charter Schools at the beginning of the year. The firm’s operations and finances were managed by Debra K. Slagle, also a defendant.

This action is based on two offerings, the first in 2011 and the second in 2016. In 2011 Park View was a conduit borrower for a $6.625 million by Pima Industrial Development Authority. The bonds were issued subject to an indenture agreement that governed disbursement of the bond proceeds and repayment of the bond investors. The 2011 Indenture provided that the trustee deposit almost $250,000 of the bond proceeds into an Operating Reserve Fund to protect investors. The bonds were to build the school facilities.

Monthly deposits were required to be made to cover the operating expenses under the terms of the 2011 bond offering to an Operating Reserve Fund. Ms. Slagle, however, made 12 requested over a four-year period, beginning in May 2012, to withdraw funds. While she certified that each request was permissible, that claims were incorrect.

The school was unable to replenish the withdrawals despite efforts by Ms. Slagle to aid the project. By January 2016 Park View was essentially out of cash and owed $400,000. Ms. Slagle made four requests totaling $31,900 from the Operating Reserve Fund and a total of $46,000 from the Repair and Replacement Fund. Each request certified that it was for unbudgeted expenses or repair and replacement costs. In fact, most of the funds were used to cover payroll and to pay other operating expenses.

In 2916 Ms. Slagle decided to seek another bond offering to repay the 2011 bonds and other debt. The Official Statement for the offering was posted on the Municipal Securities Rulemaking Board's Electronic Municipal Market Access system in April 2016.

The statement was based on a feasibility study for the next two years that contained projects showing Park View as profitable. The projections contained material errors, understating, for example, the operating expenses for 2016 by 20%. Key to the projections was an expense reduction program. The statement and projections were created by Ms. Slagle.

The offering materials did not disclose the operating difficulties of Park View. While the projections were based on an expense reduction program, it had not in fact been adopted or implemented. Without that program Park View's on-going financial difficulties would preclude meeting the projections in the offering materials.

No debt reduction was ever adopted. By early the next year Park View defaulted. It was April 2017, one year after the offering. The complaint alleges violations of each subsection of Securities Act Section 17(a) and Exchange Act Section 10(b). The action is pending.

SEC Actions – T. Gorman

September 15 2020

Roosevelt & Cross Settles Bond-Flipping Case; CEO Resigns.

Roosevelt & Cross agreed to pay about $1 million as part of a settlement with the Securities and Exchange Commission over charges that the broker-dealer and its chief executive officer improperly allocated municipal bonds meant for retail buyers to professional investors looking to make a quick profit.

The SEC found that Roosevelt & Cross helped so-called "flippers" by circumventing order periods designated for individual investors between March 2014 and May 2017. The flippers would then resell the bonds to other broker-dealers for a profit. Roosevelt & Cross did not deny or admit the SEC's charges.

Chief Executive Officer Thomas Vigorito resigned on Sept. 11, said Matthew Campolettano, the firm's chief compliance officer.

The SEC's order said that Roosevelt & Cross placed such orders for two firms, RMR Asset Management Company and Core Performance Management, LLC –also known as Dockside Asset Management — over 100 times and often during retail order periods.

“In almost all instances where bonds were allocated, Roosevelt’s registered representatives submitted inaccurate zip codes which corresponded to the state of the issuer and did not correspond to where Dockside and RMR were located,” the order said.

The SEC filed enforcement actions against RMR and Core and their associates in 2018.

Campolettano, the compliance officer, said in an emailed statement that the broker-dealer “is among the firms that interacted with flippers and failed to detect the flippers’ fraudulent misrepresentations.”

“These dealing with the flippers involved a very small part of the firm’s total business and took place between three and six years ago,” he said. “Roosevelt & Cross fully cooperated with the SEC in its investigation and took prompt remedial actions.”

The SEC also settled with Vigorito and William W. Welsh, a salesperson. Both representatives consented to cease-and-desist order findings but did not admit or deny the SEC’s allegations. The SEC’s order says that Vigorito had served as the company’s chief executive officer since 2017.

The SEC order against Vigorito said he would also engage in a practice known as “parking,” in which he would arrange for a bond flipper to buy a new issue deal underwritten by Roosevelt with the understanding that the flipper would sell the bonds back to Roosevelt at a higher price.

Roosevelt & Cross is ranked the 28th largest underwriter of long-term municipal-bond debt so far in 2020, according to data compiled by Bloomberg. The firm specializes in smaller bond deals sold by towns and school districts in New York, New Jersey and Connecticut.

Monday’s announcement is the latest enforcement action by the SEC involving muni-bond flippers, an enforcement effort that’s spanned years. In July, UBS Group AG agreed to pay more than $10 million to resolve charges that it helped such buyers.

Bloomberg Markets

By Amanda Albright

September 14, 2020, 10:45 AM PDT Updated on September 14, 2020, 12:25 PM PDT

— With assistance by Danielle Moran

GASB Opens Search for Director of Research and Technical Activities.

Norwalk, CT, September 10, 2020 — The Governmental Accounting Standards Board (GASB) today announced that it has opened a formal search for the next GASB director of research and technical activities.

David R. Bean, the GASB’s current director of research and technical activities, plans to retire on March 31, 2021 after more than 30 years with the organization.

The director in this role is the leader of the GASB staff and principal advisor to the GASB chair and Board. This position has a critical leadership function in the overall management of projects on the GASB’s technical and research agendas, GASB project-related communications, and interaction and engagement with stakeholders.

Reporting to the GASB chair, the director leads and manages the GASB's 25 staff members on all technical accounting projects and ensures that detailed project plans, priorities, and timetables are consistent with the Board's goals and priorities. In addition, the director represents the GASB as a spokesman on technical issues at a variety of speaking engagements, serves as a primary liaison with key stakeholder groups, and develops the GASB budget.

The ideal candidate should be a demonstrated leader and critical thinker, have a passion for the GASB mission, a dedication to service, and extensive technical knowledge of state and local government accounting and financial reporting. The successful candidate will have a minimum of 15-20 years senior-level experience at a public accounting firm, government, university, or comparable organization.

A full job description and list of requirements can be found on the Financial Accounting Foundation (FAF) website. Interested candidates must apply by October 30, 2020.

SEC Charges Charter School Operator With Fraudulent Municipal Bond Offering.

SEC Charges Charter School Operator, Debra Kay Slagle, and its Former President With Fraudulent Municipal Bond Offering

Washington DC (STL.News) The Securities and Exchange Commission today charged Park View School, Inc., a state-funded, nonprofit charter school operator based in Prescott Valley, Arizona, and its former President, Debra Kay Slagle, with misleading investors in an April 2016 municipal bond offering.

According to the SEC's complaint, Park View and Slagle made false and misleading statements about Park View's financial condition. As alleged, in the years and months leading up to the bond offering, Park View experienced significant operating losses and repeatedly made unauthorized withdrawals from two reserve accounts to cover routine operating expenses, to pay other debts, and to transfer money to affiliated entities. Park View allegedly provided investors an offering document that included misleading statements about profit and expense projections and showed that Park View would be profitable in the upcoming fiscal year and able to repay the bondholders. According to the complaint, investors purchased $7.6 million in bonds in the April 2016 offering. Although the bonds were nominally offered by the Industrial Development Authority of the County of Pima, Arizona, Park View, as conduit borrower, received the bond proceeds and was responsible for repaying them. Park View allegedly defaulted one year later by reducing the interest payments that it made on the bonds.

"Issuers and conduit borrowers of municipal bonds must provide investors with an accurate picture of their financial condition, and any financial projections they provide to investors must have a reasonable basis," said LeeAnn G. Gaunt, Chief of the Division of Enforcement's Public Finance Abuse Unit. "The SEC will continue to vigorously pursue those who deceive investors, as we allege Slagle and Park View did."

The SEC's complaint, filed in U.S. District Court for the District of Arizona, charges Slagle and Park View with violating antifraud provisions of the federal securities laws. Without admitting or denying the allegations in the complaint, Slagle and Park View agreed to settle with the SEC and to be enjoined from future violations of the charged securities laws. Slagle further agreed to pay a

$30,000 penalty and to be enjoined from participating in future municipal securities offerings. The settlements are subject to court approval.

For further information about the SEC's enforcement actions involving fraud charges in connection with bond issuances by or on behalf of schools and colleges, see SEC v. Batchelor (N.D. Cal. April 27, 2020), SEC v. Rojas (C.D. Cal. September 19, 2019), and SEC v. Borge (S.D.N.Y. March 28, 2019). The SEC has also brought a number of recent enforcement actions against municipal advisors who provide services to school district issuers.

The SEC's investigation was conducted by Steven Varholik and Creighton Papier of the Enforcement Division's Public Finance Abuse Unit and John Yun of the San Francisco Regional Office, with assistance from Deputy Unit Chief Mark Zehner and Erin Smith of the Division of Economic and Risk Analysis. The investigation was supervised by Jason H. Lee.

STL.News

09/14/2020

SEC Charges Charter School Operator and its Former President With Fraudulent Municipal Bond Offering.

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NFMA At-Large Board Elections.

Each fall, the National Federation of Municipal Analysts Board accepts applications for three At-Large Board seats. The term for these seats is two years, commencing January 1, 2021. All regular members in good standing are eligible to submit an application. The election will take place in late October. While traditionally, participation on the Board would entail three in-person meetings per year (along with a few virtual meetings), the current pandemic has curtailed in-person meetings until later in 2021.

Questions about serving on the Board may be addressed to Lisa Good at lgood@nfma.org.

To submit an application, click here or go to the Member Home page (after logging in).

Applications are due by October 1.

MSRB Event-Based Continuing Disclosures.

Event-based continuing disclosures that cite COVID-19 continue their downward trajectory.

Read this week's disclosure summary report.

SEC Identifies LIBOR Preparedness as an Examination Priority.

On 18 June 2020 the Securities Exchange Commission's (SEC's) Office of Compliance Inspections and Examinations (OCIE) announced the details of an examination initiative specifically focused on London Interbank Offered Rate (LIBOR) preparedness.(1)

The OCIE has previously identified LIBOR preparedness of registrants (eg, SEC-registered investment advisers, broker-dealers, investment companies, municipal advisers, transfer agents and clearing agencies) as a key examination priority for 2020, but the latest announcement offers specific insights into what information examiners will be seeking from registrants.(2)

Background

The expected cessation of LIBOR after 2021 is expected to significantly impact financial markets and present a multitude of financial, legal, operational, conduct and reputation risks for certain market participants. Preparing for the transition away from LIBOR to alternative rates is viewed as essential by a number of regulators, including the SEC. The OCIE will be conducting examinations to facilitate an orderly transition.

Examination process

According to the OCIE's release, examiners will review whether and how a registrant has evaluated the potential impact of the LIBOR transition on the organisation's:

- business activities;
- operations;
- services; and
- customers, clients and/or investors (collectively, investors).

Examiners will review the plans that registrants have developed and steps they have taken to prepare for the LIBOR discontinuation, including with respect to operational readiness and disclosures. The OCIE has also identified the types of information and document that may be sought in these examinations, including:

- information regarding any individuals or groups (eg, internal committees, working groups or transition teams) assigned responsibility to oversee or manage the effects of the LIBOR transition on the registrant, including information regarding the frequency of any meetings on this topic and whether minutes are kept;
- the identity of any third parties the registrant has used or plans to use to assess the impact of the LIBOR transition on the firm or its investors;
- documentation or descriptions of any analysis performed to identify contracts or obligations held and/or issued by the registrant or its investors that may be affected by the LIBOR transition and any remediation plans thereof;
- information regarding any investors whose fee structure (eg, performance-based fees) or performance reporting (eg, use of LIBOR-linked benchmark) could potentially be affected by the LIBOR transition;
- any written assessments, strategic plans (including remediation plans, as applicable), roadmaps or timelines prepared by or for the registrant regarding preparation for the LIBOR transition, including the consideration of alternative reference rates;
- materials referencing the LIBOR transition provided to the registrant's board of directors, any committee thereof, any board member, the board or board member(s) of any investors, or the board, legislative body or member(s) thereof of any municipal entity or obligated person client, if applicable, or equivalent governing bodies or offices, if the registrant is not organised as a corporation;
- information regarding any third-party vendors the registrant uses that may be impacted by the LIBOR transition, including the services provided (eg, back office) and how the vendor may be impacted; and
- any implemented or planned changes to compliance procedures, controls or surveillance systems designed to monitor for LIBOR-linked instruments or contracts recommended or sold to clients.

What registrants should be doing now

The list of information that will be sought by SEC examiners is not exclusive and should underscore the urgency of having both experienced counsel on LIBOR matters and a well-designed transition roadmap. Ideally, firms should not wait until an exam is scheduled or a request for information is received to start preparing. Further, as a matter of best practice, firms should begin collecting information that would be responsive to the areas identified by the OCIE.

Endnotes

(1) See SEC, "Examination Initiative: LIBOR Transition Preparedness" (18 June 2020).

(2) See SEC, "Examination Priorities for Fiscal Year 2020" (7 January 2020).

Shearman & Sterling LLP – Donna M Parisi, Geoffrey B Goldman, Azam H Aziz, Jennifer Oosterbaan

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NABL: Disclosure Industry Working Group Publishes Paper on Timely Disclosures

The Disclosure Industry Working Group has released a paper entitled, General Continuing Disclosure Considerations for Municipal Securities Issuers. The considerations were developed to provide guidance to issuers on timely disclosure. The ongoing COVID-19 pandemic and its impact on all municipal governments and their respective economies highlights a need for accurate, timely, and responsive municipal disclosure.

The paper contains eight considerations including:

- Material Event Filings
- Know Your Annual Disclosure Filing Dates
- Making Annual Continuing Disclosure Filings
- Good Investor Relations
- Determining Whether and/or When to Make Voluntary Disclosure Filings
- Presenting COVID-19 Voluntary Disclosure Information
- EMMA Filings
- Post-Issuance Compliance for Tax Law Purposes

While the considerations contained in the paper are general in nature, different issuers of different credits may need to take into account other specific considerations while addressing disclosure both generally and during the COVID-19 pandemic. Further, while the recommendations are actions that municipal issuers should consider, all issuers are encouraged to discuss COVID-19 disclosure with their entire financing team, including with their bond or disclosure counsel.

The organizations who signed onto the paper include:

- Bond Dealers of America (BDA)
- Government Finance Officers Association (GFOA)
- National Association of Bond Lawyers (NABL)
- National Association of Municipal Advisors (NAMA)
- National Association of State Auditors, Comptrollers and Treasurers (NASACT)
- National Association of State Treasurers (NAST)
- National Association of Health and Educational Facilities Finance Authorities (NAHEFFA)
- National Federation of Municipal Analysts (NFMA)

You can find the paper here.

MSRB Disclosure Summary Report.

Rating change disclosures citing COVID-19 hit their highest weekly count since early May.

Read the MSRB's new disclosure summary report.

MSRB Weekly COVID-19-Related Continuing Disclosures.

Weekly COVID-19-related continuing disclosures hit their second-highest weekly figure, driven in large part by 356 new quarterly and monthly financial information disclosures.

Read this week's disclosure summary report.

FAF Reappoints Robert Scott and Alan Skelton to Leadership Roles on the Governmental Accounting Standards Advisory Council.

Norwalk, CT—August 18, 2020 — The Board of Trustees of the Financial Accounting Foundation (FAF) today announced the reappointment of Robert Scott and Alan Skelton as chair and vice chair, respectively, of the Governmental Accounting Standards Advisory Council (GASAC). The reappointments are for a one-year term beginning on January 1, 2021.

The GASAC is responsible for advising the Governmental Accounting Standards Board (GASB) on technical issues, project priorities, and other matters that affect standard setting for accounting and financial reporting by state and local governments. Members of the GASAC represent a cross-section of the GASB's state and local government stakeholders, including users, preparers, and auditors of financial information. GASAC members are selected for their professional expertise and the depth and breadth of experience they bring to the Council.

The GASB is the independent, private-sector organization that sets accounting standards for state and local governments in the United States. The FAF oversees the activities of the GASB and its sister accounting standard setter, the Financial Accounting Standards Board (FASB).

"We are very pleased that Robert and Alan have agreed to continue their strong leadership of the GASAC for another year," said Kathleen Casey, chair of the FAF Board of Trustees. "They combine strategic insight with on-the-ground perspective about accounting issues facing state and local governments, and they have proven to be capable leaders and advisors to the GASB."

Mr. Scott has been the Director of Finance and Administration for the city of Brookfield, Wisconsin since 1999. Prior to joining the city of Brookfield, he served in similar financial management positions for Milwaukee Area Technical College and the cities of Franklin and Cedarburg, Wisconsin. Before entering the public sector, he was employed as an audit manager with the accounting firm of Deloitte & Touche. He joined the GASAC in 2011 as a representative of the Government Finance Officers Association and has served as chair since 2015.

Mr. Skelton serves as the State Accounting Officer for the state of Georgia and was initially appointed to the position by Governor Nathan Deal in July 2012. He was reappointed by Governor Brian Kemp in January 2019. He provides accounting leadership for the state of Georgia, which includes oversight of statewide financial reporting, issuing accounting policy and interpretation of GAAP standards, and the implementation of business process improvements. Before his current appointment, he was Deputy State Accounting Officer for three years and had more than a decade of experience in public accounting roles.

SIFMA Seeks to Vacate Muni Advisor BD Exemption: Cadwalader

SIFMA filed suit seeking to vacate a recently adopted SEC temporary exemption for municipal advisors from broker-dealer registration. The exemption (which was previously covered here) permits municipal advisors to make limited solicitations to certain banks and similar entities to invest in "direct placements" of municipal issuers without being subjected to broker-dealer registration.

SIFMA stated that existing market data do not support the purported need for the exemption, which harms investors and other market competitors by "eliminating investor protections and critical reporting requirements." SIFMA President and CEO Kenneth Bentsen Jr. asserted that "through the [exemption], the SEC allows municipal advisors to engage in broker-dealer activity without the attendant legal and regulatory requirements that apply when a broker-dealer is engaged."

The SIFMA petition – filed for review in the D.C. Circuit Court of Appeals – has yet to be made public.

Cadwalader Wickersham & Taft LLP – Nihal S. Patel

August 19 2020

LIBOR Transition: Business Loans SOFR Summer Wrap Up - McGuireWoods

It's been a busy summer in the land of LIBOR transition preparation. As part of the ARRC's ongoing efforts to prepare the cash product markets for the transition to SOFR and away from LIBOR as a benchmark interest rate, it posted ten separate releases between Memorial Day and August 7, 2020, in addition to hosting six "SOFR Summer Series" panel discussions on various SOFR topics (which were recorded and can be accessed here). This blogpost focuses on aspects of the ARRC's releases relating to business loans.

Read on for more details, but here are a few major takeaways: (1) don't expect any COVID related delays in the LIBOR sunset schedule – work on implementing hardwired LIBOR fallback language this fall and plan stop using LIBOR by mid-2021; (2) the ARRC now recommends simple SOFR in arrears as the best available fallback rate alternative for most business loans (at least until a term SOFR in advance market develops); and (3) feedback from the business loan market reflects a preference for following ISDA's lead on LIBOR to SOFR transition issues whenever practicable to facilitate consistency between swaps and business loans (e.g., spread adjustments and certain conventions).

ARRC Best Practices for Completing Transition from LIBOR

On May 27, 2020, the ARRC released its "Best Practices for Completing Transition From LIBOR," which set the table for its later releases over the summer. The key recommendations for business loans:

- To the extent not already utilized, all new business loans should include ARRC-recommended (or substantially similar) ***hardwired*** USD LIBOR fallback language (rather than relying on the "amendment approach" which has been more widely accepted to date) as soon as possible, but in no event later than September 30, 2020.
- Third-party technology and operations vendors relevant to business loans (including those with booking, trading, valuation, settlement, and accounting systems used for loans) should complete all necessary enhancements to support SOFR (including but not limited to simple, compounding in arrears, and term SOFR) by September 30, 2020.
- No business loans using USD LIBOR and maturing after 2021 should be originated after June 30, 2021.
- For business loans specifying that one or more parties will select a replacement rate for USD LIBOR at their discretion, the determining parties should disclose to relevant parties the replacement rate and any related spread adjustment methodology that they anticipate selecting to relevant parties at least 6 months prior to the date that a replacement rate would become effective.

The release also set forth recommendations for Floating Rate Notes, Consumer Loans, Securitizations and Derivatives. Click through above and check in with this blog for further detail on the ARRC's best practices recommendations for those products.

SOFR Spread Adjustments Revisited

In a June 30 release, the ARRC elaborated on its prior recommendation for a spread adjustment methodology in cash products, based on market participant feedback from its supplemental consultation on spread adjustment methodology. Recall that the ARRC had initially recommended a spread adjustment methodology based on a historical median over a five-year lookback period calculating the difference between USD LIBOR and SOFR, which matches the methodology recommended by the International Swaps and Derivatives Association (ISDA) for derivatives, with a 1-year transition period to this methodology for consumer products.
<https://www.liborblog.com/2020/04/arrc-announce-
-recommendation-of-a-spread-adjustment-methodology-for-cash-products/>.

After soliciting and receiving additional market feedback on the interaction of this methodology with ISDA's methodology and timing, the ARRC clarified in a June 30 release that:

- for cash products (other than consumer products), the ARRC would recommend that the value of USD LIBOR spread adjustment match the value of ISDA's spread adjustment spread adjustments (rather than merely using the same adjustment methodology to calculate a different spread adjustment for each potential fallback rate), while reserving on treatment for consumer products; and
- for all cash products, in the event of a pre-cessation trigger, the ARRC's recommended 5-year historical median spread adjustments will be determined at the same time as the ISDA's spread adjustments (which will be at the time of any announcement that LIBOR will or has ceased or will or has become no longer representative).

In short, the ARRC continues to respond to feedback from market participants that cash products should be closely aligned with the swaps and derivatives market in the transition from LIBOR to SOFR.

Updated Hardwired Fallback Language: This Time We Mean It

The ARRC also released updated recommended "Hardwired" fallback language for syndicated loans on June 30. Recall that in April 2019, the ARRC released both "Amendment" fallback language (adopting a streamlined but flexible amendment process to incorporate a to-be-determined substitute benchmark rate for LIBOR) and "Hardwired" fallback language (contemplating Compounded SOFR in Advance as the default substitute benchmark rate) for syndicated loans. The syndicated loan market responded by almost uniform adoption of some version (in some cases modified) of the "Amendment" language, with little uptake of the "Hardwired" approach.

In an effort to help foster adoption of a "Hardwired" approach beginning in Q4 2020 as recommended in its May 2020 "Best Practices" release, the June 30 ARRC release modifies its recommended "Hardwired" amendment language to account for market feedback and easier market adoption. "To the extent market participants continue to enter into LIBOR-based contracts, the ARRC recommends and endorses the fallback language and related guidance herein and believes the cash markets will benefit by adopting a more consistent, transparent and resilient approach to contractual fallback arrangements for new LIBOR products." It is a lengthy release containing both updated form contract language and an explanatory guide. A few highlights:

- *Available Tenors:* Refines the references to and transition between LIBOR tenors (forward looking periods (e.g., 30/60/90 days) of locked rates) and potential SOFR tenors (periods of interest accrual and interest payment periods).
- *Benchmark Replacement Triggers:* Clarifies that the "No Longer Representative" prong of the benchmark replacement trigger will only be triggered when "all Available Tenors" of LIBOR are deemed unrepresentative of market conditions. This will prevent an unintended early benchmark transition trigger if only certain LIBOR tenors become unreliable (e.g., as we approach the formal LIBOR cessation date, longer LIBOR tenors may become unrepresentative while shorter LIBOR tenors remain viable), allowing administrative agents to "turn off" those LIBOR tenors that are deemed no longer representative.
- *Benchmark Replacement Waterfall*: Changes the "waterfall" of benchmark replacement rates (originally drafted as (1) forward looking term SOFR (plus a spread adjustment) (which does not currently exist and may not exist), then (2) compounded SOFR (either in advance or in arrears) (plus a spread adjustment), then (3) as selected by the Administrative Agent and Borrower (plus a spread adjustment)) ***by replacing*** compounded SOFR in arrears (step 2) with daily simple SOFR. The ARRC rationale for the change: the use of compounded SOFR in advance does not match the needs of business loans to accommodate frequent unscheduled balance changes (e.g., prepayments), and although compounded SOFR in arrears better matches the ISDA calculation convention, daily simple SOFR can be more easily implemented on bank systems now and historically only varies from compounded SOFR in arrears values by a few basis points. The ARRC release contains detailed explanations on when market participants might prefer to use daily compounded SOFR in arrears or compounded SOFR in advance, so it should be reviewed for further detail on the differences in these calculations.
- *Spread Adjustments:* Implements the revised ARRC approach to spread adjustments released on June 30 and summarized above, and defaults to available ISDA spread adjustments if ARRC approved spread adjustments are not available.

The revised language contains other modifications and should be reviewed in detail with the guidance that follows it in the June 30 release.

Down to Details: SOFR "In Arrears" Conventions for Syndicated Business Loans

In the June 30 ARRC release updating the "Hardwired" fallback language, the definition of "Daily Simple SOFR" provides that the administrative agent shall establish conventions for that rate in accordance with ARRC recommended conventions. On July 22, the ARRC released its initial guidance on conventions for "in arrears" structures (Daily Simple SOFR and Daily Compounded SOFR). To remind, these rate structures allow for interest accruals to be calculated daily, but they are not set in advance and not fixed during each interest period (both of which are true for forward-looking term LIBOR rates). The recommended ARRC conventions for "In Arrears" rate structures described in the July 22 release address both new loans that are originated using SOFR and legacy loans that "fall back" from LIBOR to SOFR upon LIBOR cessation or LIBOR being declared to be unrepresentative. The ARRC emphasized in its release that these convention recommendations are voluntary and may not be applicable to all segments of the business loan markets. Some highlights:

- *Compounding:* The release compares simple interest and compound interest, and describes different calculation approaches for compounding in arrears.
- *Lookback / Lockout / Payment Delay:* The release recommends using the business day "lookback" approach with no observation shift for SOFR loans. A five day "lookback" convention (different days can be selected by market participants) for a June 1 loan with a 30 day interest period, for example, would apply the May 25 SOFR rate to the June 1 balance, and so on throughout the interest period, so that by June 23, the administrative agent will know the daily rates through the end of the 30 day interest period. This would enable the administrative agent to determine the rate of interest for the interest period before the period ends and the payment is due, so that the administrative agent has time to invoice the borrower and the borrower has time to pay the interest on time. The ARRC rejected an observation shift for compounded SOFR in arrears (which would weight the rate by the daycount weight of the "lookback" day in the compounding formula) for creating unnecessary complexity relative to the benefit gained in reduced hedging basis relative to a standard SOFR OIS contract.
- *Holiday and Weekend Conventions:* For Compound Interest, interest would be compounded on business days, and the preceding business day's rate would be applied over weekends or holidays, weighted by the number of calendar days until the next business day. For Simple Interest, the preceding business day's rate would be applied over weekends or holidays, weighted by the number of calendar days until the next business day. For payment dates, the release recommends a convention similar to that applicable to LIBOR today: if a SOFR loan is repaid to a UK lending office on a US Business Day that is not a UK Business Day, it would remain in the swift/clearing account of the UK lending office until the following UK Business Day when the lending office processes the payment. A borrowing notice for a USD borrowing sent to a UK Bank on any day other than a UK Business Day would be processed on the next succeeding UK Business Day.
- *Daycount:* actual / 360 (standard for US money markets).
- *Modified Following Business Day Convention*: payments dates that fall on a non-Business Day would be adjusted to the next succeeding business day, unless that business day falls in the next succeeding calendar month, in which case the interest payment date would be the preceding business day.
- *Rounding: interest-rate calculations rounded (not truncated) to 5 decimal points;* dollar amounts rounded to 2 decimal points (for example in an invoice or ledger reports), but recommends that calculations not be rounded internally.
- *Floors:* interest rate floors would be calculated daily and not at the end of an interest period because loans accrue interest daily and loan funds strike a daily net asset value based on this daily accrued interest.

  Distribution of Interest: Daily accrued interest calculated on each lender's share of principal that day, which is same convention currently used for LIBOR loans.

- *SOFR Index:* The release points out that the ARRC published SOFR Index is less useful for business loans than other cash products, such as floating rate notes, due to (1) use of an observation shift (as noted above, not recommended for business loans), (2) the possibility of frequent intra-period prepayments for business loans and (3) the possibility for interest rate floors in business loans, which are not compatible with the SOFR Index.
- *Compensation for Losses:* The release recognizes that typical "breakage" language found in LIBOR based loan agreements may not be applicable to Daily Simple SOFR or Daily Compounded SOFR, but that market participants may wish to include language that compensates lenders for funding losses due to intra-period prepayments.

Wrapping up the SOFR Summer with the SOFR Starter Kit

The ARRC wrapped up its busy "SOFR Summer" with the release of its "SOFR Starter Kit" on August 7. This release links to three factsheets covering (1) the History and Background of USD LIBOR, the ARRC and SOFR, (2) Key Facts about SOFR and (3) SOFR Next Steps. These convenient fact sheets consolidate current best practices and timelines for transitioning from LIBOR to SOFR, and link through to more detailed materials previously published by the ARRC and maintained on its website.

By Donald A. Ensing, Susan Rodriguez, Jennifer J. Kafcas & Barlow T. Mann on August 21, 2020

ARRC Updates Recommended Best Practices in Anticipation of ISDA's IBOR Fallback Protocol: McGuireWoods

On August 19, 2020, the ARRC updated its recommended Best Practices for the LIBOR transition in anticipation of the imminent publication of ISDA's IBOR Fallback Protocol (the "Protocol") (which we discussed in our earlier blog post, available here).

These updates follow the July 22, 2020 letter from ISDA (the "Letter") (available here), in which ISDA confirmed that market participants will be able to sign up to the Protocol "in escrow". This will consist of a two-week pre-publication period in which firms can sign up in order to adhere to the Protocol as promptly as possible. It is expected that this escrow period will begin soon, though no hard date has yet been set.

In light of the Letter, the ARRC's Best Practices have been updated to include a specific recommendation to "[d]ealers and other firms with significant derivatives exposures" to sign up to the Protocol during the escrow period to promote adoption as quickly as possible. The Best Practices have also been updated to recommend that other market participants adhere to the Protocol "within the 3 to 4 month period after it is published and before the amendments to embed the fallbacks in legacy transactions take effect."

As such, it is important that market participants, especially those with significant derivatives exposures, consider adhering to the Protocol "in escrow" in order to navigate the transition of their legacy derivatives as smoothly and efficiently as possible. Please contact any of the authors of this article or your regular McGuireWoods contact if you have questions about, or would like assistance with, the LIBOR transition.

By Jennifer J. Kafcas, Donald A. Ensing, Susan Rodriguez, Lauren J. Blaber & Harry Poland on August 24, 2020

MSRB COVID-19 Rating Change Disclosure Report.

COVID-19-related rating change disclosures continue to rise, now at their highest point in almost three months.

Read the MSRB's new disclosure summary report.

SIFMA Files Suit Seeking to Vacate SEC's Temporary Conditional Exemption for Municipal Advisors.

Washington, D.C., August 14, 2020 – SIFMA today filed a suit seeking to vacate the Securities and Exchange Commission's Order Granting a Temporary Conditional Exemption from the Broker Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934 for Certain Activities of Registered Municipal Advisors (TCE). The TCE permits registered municipal advisors to solicit banks, their wholly-owned subsidiaries that are engaged in commercial lending and financing activities, and credit unions in connection with direct placements of securities issued by their municipal issuer clients, without registering as broker-dealers.

The Commission described the TCE as a measure needed to provide relief to small issuers in light of the Covid-19 pandemic. Generally speaking, SIFMA applauds the SEC's and other regulators' ongoing efforts to proactively respond to pandemic-related interference with normal market operations. In this case, however, the purported need for the TCE is not supported by existing market data and creates a host of negative consequences for not only other market competitors but also issuers and investors alike.

"The TCE creates an uneven playing field that exclusively benefits municipal advisors at the expense of more regulated broker-dealers, and ultimately we believe at the expense of issuers and market transparency," said Kenneth E. Bentsen, Jr., president and CEO of SIFMA. "The SEC in effect suspended SEC regulatory requirements for one type of business entity, at the expense of another. Further, we believe the SEC failed to follow the proper procedure by taking such sweeping action absent a formal rulemaking with notice and comment, along with a genuine cost benefit analysis."

The SEC has suggested for some time that it would consider taking this type of action and SIFMA has repeatedly argued that the Commission must go through a formal rulemaking process involving notice and comment and rigorous cost benefit analysis, where SIFMA believes the proposal would fail. Instead, the Commission chose to assert its exemptive powers to cure a perceived emergency in the small-issue municipal market, which is not supported by existing market data. The Commission's claim is not supported by the facts, and even if it were, such circumstances would not justify eliminating substantive issuer and investor protections.

The Commission's action has a detrimental impact on investors and the municipal market by eliminating investor protections and critical reporting requirements. In addition, there is no evidence the TCE creates cost savings for municipal issuers by lowering fees or by creating additional market liquidity. The only parties benefiting from the TCE are municipal advisors who are now incentivized to advise clients to engage in transactions that fit within the parameters of the

TCE. As a result, the investor protections and stringent reporting requirements under MSRB rules and Exchange Act Rule 15c2-12 that apply when a broker-dealer is involved do not apply to municipal advisors under the TCE. The resulting lack of transparency could have broad and detrimental effects on issuers, investors and the municipal markets.

The SEC did not adequately justify why it is "consistent with the public interest and protection of investors" for municipal advisors to engage in broker-dealer activity pursuant to the terms of the TCE without the protections afforded to investors when a registered broker-dealer is engaged.

"Through the TCE, the SEC allows municipal advisors to engage in broker-dealer activity without the attendant legal and regulatory requirements that apply when a broker-dealer is engaged. Broker-dealer transaction reporting requirements provide critical market data and transparency to the municipal securities market. These reporting requirements, along with other significant compliance obligations, are completely lacking when a municipal advisor acts pursuant to the TCE. There is also a risk of harm to issuers, as the TCE undermines the duty owed them by advisors, and the SEC has not provided any empirical evidence that issuers would benefit from the TCE as compared to the public market or direct placements solicited by broker-dealers," said Mr. Bentsen.

GASB Offers Grants for Research on Severe Financial Stress.

Read the Request for Research.

[08/12/20]

MSRB to Implement Strengthened Board Governance and Announces FY 2021 Board Leadership.

Washington, DC – The Municipal Securities Rulemaking Board (MSRB) announced today that enhancements to its governance structure would take effect for the fiscal year beginning October 1, 2020. The MSRB initially proposed the strengthened governance standards in a filing to the Securities and Exchange Commission (SEC) in June after a lengthy comment process. The new rules tighten the standards for selecting members and reduce the size of the Board of Directors that oversees the self-regulatory organization (SRO) responsible for safeguarding a fair and efficient municipal securities market. The SEC approved the standards on Wednesday, August 5.

In its approval order, the SEC noted it had carefully considered the proposed rule change, the comment letters received and the MSRB's letter in response to comments.

Bob Brown, MSRB Board member and Chair of the Board's Governance Review Special Committee said: "The rules approved by the SEC remove even the appearance of a conflict of interest for public members of the MSRB Board. We also begin a two-year process to scale down the size of the Board following its expansion a decade ago."

Amended MSRB Rules A-3 and A-6 tighten the eligibility requirement for public board members by requiring separation from a regulated entity of at least five years. The amended rules also reduce the size of the 21-member Board, initially moving to 17 members in Fiscal Year 2021 before ultimately shrinking to 15 members in FY 2022. The Board had expanded to 21 members in response to the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 as a way to provide additional flexibility in balancing public and regulated membership and to broaden the range of Board-member perspectives during the development of the core municipal advisor regulatory framework.

As part of its transition to a smaller board size, the Board approved extending the terms of two current Board members whose terms were about to expire. Julia Cooper, Director of Finance, City of San Jose, will remain on the MSRB Board as a public member representing issuers. Ed Sisk, current Board Chair and Managing Director, Head of Public Finance at BofA Securities, will remain on the Board as a regulated member. The 17-member transitional Board will therefore include two issuer representatives among its nine public members. Also, as required by statute, the Board will continue to be as closely divided in number as possible between public and regulated representatives.

In addition to extending their terms, the Board re-elected Sisk to serve as Chair and elected Cooper to serve as Vice Chair in FY 2021.

"We are fortunate to have Ed's experienced leadership at the helm of the Board especially at this time of unprecedented strain on market participants stemming from the pandemic and during the integration of a new CEO into the MSRB team," said Brown. "As we demonstrated when we amended our original transition plan, the Board believes this is a critical time to have effective issuer representation on the Board. With Julia and our FY 2020 Vice Chair Manju Ganeriwala both continuing on the Board in FY 2021, the MSRB will have the benefit of local and state issuer representation next year."

The Board formed the Governance Review Special Committee in September 2019 to begin a comprehensive review of the MSRB's governance practices. In January 2020, the Board solicited public comment on a number of proposed changes to MSRB Rules A-3 and A-6. The comment period occurred during the early stages of the pandemic, and in response to requests from stakeholders, the Board extended the original 60-day comment period to 90 days to ensure all interested persons had sufficient time to prepare comments. After reviewing the comments received, the MSRB then filed a revised proposal for SEC approval, where additional comments were received and considered.

Read the MSRB's approval notice.

Date: August 6, 2020

Contact: Leah Szarek, Interim Chief External Relations Officer
202-838-1500
lszarek@msrb.org

Financial Accounting Foundation Board of Trustees Notice of Meeting.

Read the Notice.

[08/03/20]

FINRA Issues Guidance to Help Firms Prepare for LIBOR Transition: McGuireWoods

On August 5, 2020, FINRA issued a regulatory notice outlining steps for broker-dealers to prepare for the pending transition away from LIBOR. The notice reminds firms to "evaluate their exposure to LIBOR" and "review their preparedness to manage LIBOR's phase-out." While the notice expressly disclaims any agency view of "specific effective practices," it provides questions for firms to consider and a general description of best practices, which derive from responses to a survey undertaken by FINRA of a cross-section of member firms.

The survey found that, while large broker-dealers, especially those affiliated with large bank holding companies, had implemented extensive programs to prepare for the LIBOR transition, many other FINRA members had implemented only limited efforts. To help these firms prepare, FINRA shared practices relating to the following categories of preparedness:

- Governance Framework: Not surprisingly, as with any large-scale change event affecting the industry, FINRA found that many firms have prepared for the transition by implementing governance frameworks to manage the LIBOR phase-out. These firms will assign organizational responsibility for preparing for and managing the transition and developing "comprehensive phase-out plans," including identifying process changes, setting timelines, and tracking progress.
- **Financial Risk:** FINRA also found that firms are evaluating their financial risk by identifying their inventory of products and contracts maturing or rolling over after the phase-out to estimate the exposure of the firm and its customers.
- **Operational Risk:** FINRA found that firms are evaluating their operational risk by identifying "business processes, business units, information systems and vendors that would be impacted by the phase-out" and by testing the firm's market, credit, and liquidity models with appropriate new reference rate(s).
- **Alternative Reference Rates:** FINRA found that firms have "reviewed and identified options" for alternative reference rates to replace LIBOR, including by participating in, or following the work of, industry organizations.
- **Legal Risk:** FINRA found that firms are reviewing their exposure to legal risk by identifying all existing contracts impacted by the phase-out and reviewing or developing fallback language. In some cases, this may include renegotiating contracts to account for the transition and replacement with alternative rates.
- **Staff Training and Customer Education:** Finally, FINRA found that firms have prepared by providing education and guidance to their staff, customers, and counterparties, including by developing "centralized" resources and guidance for staff and by "providing disclosures on firm websites and customer communications" about the phase-out's impact on the firm's customers and its products.

We can expect more information from FINRA between now and leading up to the transition deadline. As FINRA stated in its 2020 Risk Monitoring and Examination Priorities Letter, in highlighting their continued efforts to "explore new ways to expand our dialogue with firms about risks and trends facing the industry," it intends to engage with firms outside the examination program in order to understand how firms are preparing for the LIBOR transition. FINRA has used this approach to understand other issues with significant impact on the industry and shared its findings in the form of notices and reports to assist other firms in meeting the challenges. Additionally, the 2020 Letter emphasized FINRA's intent to assess the transition impact on customers, in addition to assessing risk and exposure to LIBOR-linked products.

FINRA's notice follows the June 18, 2020, SEC Risk Alert announcing that its Office of Compliance

Inspections & Examinations ("OCIE") had identified registrant preparedness for the LIBOR transition as an examination priority for fiscal year 2020. OCIE stated that it "intends to engage with registrants through examinations to assess their preparations for the expected discontinuation of LIBOR and the transition to an alternative reference rate." These examinations will review, among other items, exposure of firms and their investors to LIBOR-linked contracts, "operational readiness" to manage the transition, and firms' disclosures and representations to investors regarding their "efforts to address LIBOR discontinuation and the adoption of alternative reference rates."

The SEC also highlighted the LIBOR transition in its [2020 examination priorities alert](). OCIE noted that the examination staff, along with other SEC Divisions and Offices, would engage with firms to assess the impact the transition would have on risk and compliance challenges. OCIE also highlighted that they would pay particular attention to disclosure issues "regarding [firms'] readiness, particularly in relation to the transition's effects on investors." OCIE concluded by encouraging "each registrant to evaluate its organization's and clients' exposure to LIBOR, not just in the context of fallback language in contracts, but its use in benchmarks and indices; accounting systems; risk models; and client reporting, among other areas. Insufficient preparation could cause harm to retail investors and significant legal and compliance, economic and operational risks for registrants."

These communications highlight the extensive attention given by the federal government and financial regulators to ensuring industry's proactive preparedness for the LIBOR transition and its consequences. We can expect to see further alerts from both regulators throughout the rest of 2020 and in 2021 as they share what they have learned from their engagement with the industry about what has worked and not worked for firms in preparing for the end of reliance on the LIBOR standard.

By Emily Gordy, Bryan M. Weynand & Edward M. Nogay on August 10, 2020

McGuireWoods LLP

Brace for More SEC Muni Advisor Antifraud Actions.

SEC hasn't taken enforcement action against a municipal advisor in over a year, but that situation could change very soon.

As we approach the 10-year anniversary of Dodd-Frank's municipal advisor antifraud and registration provisions, which takes place on Oct. 1, several trends are converging that may put municipal advisors in the SEC's crosshairs.

Historically, the SEC's enforcement actions against issuers of municipal bonds often look very similar to the actions brought against issuers of other securities.

So, for example, a few years ago, the New York and New Jersey Port Authority paid $400,000 to settle SEC claims the Port Authority violated the antifraud provisions of the federal securities laws in connection with a $2.3 billion bond offering.

The Port Authority admitted failing to disclose to investors known material risks surrounding the potential lack of legal authority to fund the projects described in the bond offering documents. This and dozens of other, similar SEC cases are fairly routine stuff as against securities issuers.

However, in 2010 the Dodd-Frank Wall Street Reform and Consumer Protection Act contained a municipal advisor antifraud provision that for the first time specifically applied to the many advisors who assist municipal entities with bond offerings, reinvestment of bond proceeds, and structuring and pricing of related products.

It took the SEC six years after Dodd-Frank became effective before it used its new tool to bring an enforcement action for the first time against a municipal advisor.

‘Opening of Floodgates’

The SEC’s first case applying the municipal advisor antifraud provision involved a small, California-based advisor to several school districts who allegedly shared confidential information with financial professionals being considered by the school districts for certain advisory contracts. The advisory firm paid a small fine to settle the matter.

But the floodgates opened: since that first 2016 case, the SEC has brought several more enforcement actions against municipal advisors. Until the middle of 2019.

In June of last year, the SEC brought an action against a municipal advisor for breaching its fiduciary duties to its client: a small public library district in Illinois.

According to the SEC, the advisor (among other things) “did not provide the Library District with the information and advice needed to determine whether the price of the bonds was fair and reasonable . . . and the mispricing of the bonds will cause the Library District to pay more than $500,000 in additional interest over the life of the bonds.”

The municipal advisor paid a $50,000 penalty to settle.

But the SEC hasn’t brought any enforcement actions against a municipal advisor in over a year. Current volatile market conditions and the unprecedented precarious fiscal posture of many municipalities create a unique set of risks that may cause the SEC to end its drought.

Coronavirus Climate

News reports in the spring painted a dire picture of the impact COVID-19 would have on municipal bond issuers: “Delinquencies in the municipal market — already on the rise as counties and cities get squeezed by the coronavirus crisis — are likely to worsen amid soaring unemployment, rising alarm about stressed municipalities, and Federal conflict about aid,” according to a Barron’s report in April.

More recent reports note that the Federal Reserve’s $500 billion Municipal Liquidity Facility — open to states and cities and counties that meet population thresholds — have calmed the municipal bond markets. Ironically, even municipalities that qualify aren’t using the federal backstop in large numbers because bond issuance is way up.

“In all, about $201.5 billion in municipal bonds were issued during the first half of the year, up from $173.3 billion during the first half of 2019,” according to the Fed.

Against this backdrop, the SEC put out a public statement in May with an explicit (and verbose) headline: “The Effects of COVID-19 Have Raised Uncertainties Regarding Financial Status of State and Local Governments and Special Purpose Entities; Municipal Securities Issuer are Encouraged to Provide Updated Financial and Other Disclosures; Financial Professionals are Encouraged to Discuss These Matters with Main Street Investors.”

The SEC emphasized the types of information that it views as critical to municipal bond investors:

- The impact of COVID-19 on operations and financial condition;
- Sources of liquidity availability of federal, state and local aid; and
- Reports prepared for other governmental purposes.

The municipal bond market is booming; the risks faced by that market are enormous and unprecedented; the SEC is hyper-focused on ensuring that retail muni-investors receive adequate disclosures; and municipalities will rely in no small part on financial advisors to successfully navigate this high wire.

Expect the SEC to spend the next several years forensically pouring over the events of the next several months to find its next case against a municipal advisor.

ThinkAdvisor

By Nicolas Morgan | August 07, 2020 at 09:31 AM

SEC Publishes OCIE Risk Alert on LIBOR Transition Preparedness Examination Initiative: Dechert

The Securities and Exchange Commission's Office of Compliance Inspections and Examinations issued a National Exam Program Risk Alert on June 18, 2020 (Risk Alert),1 which introduces an examination initiative on the upcoming discontinuation of, and transition from, LIBOR2 to alternative risk-free reference rates (widely referred to as RFRs) (LIBOR Transition). The Risk Alert states that the examination initiative (LIBOR Exams), which has commenced recently, is intended to allow OCIE to assess the preparedness of SEC-registered investment advisers, broker-dealers, investment companies, municipal advisors, transfer agents and clearing agencies (collectively, Registrants) that may be impacted by the LIBOR Transition. The Risk Alert includes a sample list of documents that may be requested in a LIBOR Exam and is intended to assist Registrants with their preparations.

This Dechert OnPoint provides general background regarding LIBOR and the LIBOR Transition, describes key points for Registrants impacted by the LIBOR Transition or who are the recipients of a related examination request, and offers next steps that Registrants can consider in their LIBOR Transition preparations. Dechert has tracked developments related to LIBOR and the LIBOR Transition – for further information, please refer to Preparing for the Replacement of LIBOR.

Background on LIBOR

On any given day, LIBOR is calculated across seven tenors for each of five currencies (USD, GBP, CHF, EUR and JPY). LIBOR is intended to be a measure, for each currency and tenor, of the average rate at which leading internationally active banks are willing to borrow wholesale, unsecured funds in the London interbank market.3 LIBOR and other interbank offered rates (IBORs) are global, long-standing and extensively used benchmarks or reference rates (reference rates) for determining interest rates in contracts related to financial transactions, adjustable-rate financial products and derivatives.4

In July 2017, Andrew Bailey, then-Chief Executive of the UK Financial Conduct Authority (FCA), announced that the FCA would no longer persuade or compel LIBOR panel banks to continue to make LIBOR data submissions after 2021.[5] As a result, it is currently expected that around January 1, 2022, LIBOR will cease publication or will no longer be sufficiently robust or reliable to be representative of its underlying market.[6] It follows that LIBOR (and most other IBORs) then will cease to be effective reference rates for financial transactions and other contractual arrangements.

Following Mr. Bailey's 2017 announcement, working groups began to plan in earnest for the eventual unavailability of LIBOR and other IBORs throughout the world. Each of these working groups aimed to identify and recommend alternative RFRs denominated in the relevant local currency. Since reference rates serve a critical commercial function, any alternative to LIBOR will need to be commercially similar in a variety of respects in order to assure consistent adoption by the financial community.[7] It is expected that the majority of LIBOR (and other IBOR) replacements will be derived from RFRs developed by these working groups.

In the United States, the Federal Reserve Board and the Federal Reserve Bank of New York convened the Alternative Reference Rates Committee (ARRC), a working group of private-sector representatives and financial regulators, to recommend an alternative reference rate to USD LIBOR. The ARRC recommended the Secured Overnight Financing Rate (SOFR)[8] as its preferred alternative reference rate. Launched in April 2018, SOFR is based on the cost of overnight loans, using repurchase agreements secured by U.S. government securities (which represents a larger section of transactions than is used to derive the Fed Funds rate). However, at this time, SOFR is not widely used as a reference rate. As LIBOR may become unavailable to be used in contracts in 2022, the timeline for the transition to using SOFR as the reference rate for USD LIBOR will be highly compressed. The ARRC and similar working groups are continuing their work on LIBOR replacement solutions.

Practically, transitioning to a new reference rate is not a flip-of-the-switch event, and the current timeline only emphasizes the need for a transition plan. Given the widespread use of LIBOR as a reference rate in common commercial arrangements, the LIBOR Transition no doubt will have a significant and broad-reaching impact on many Registrants (including their business activities, operations and service provider relationships). Based upon a Registrant's business model, the Registrant will need to implement LIBOR Transition solutions (such as those recommended by the ARRC or other similar working groups) in a manner appropriate to its businesses and operations.

In light of the commercial importance of LIBOR and other IBORs, coverage in the financial press has been widespread, and issues related to LIBOR and its expected discontinuation are high on regulatory agendas worldwide.[9] Financial services regulators – including the staffs of OCIE and various other SEC divisions and offices – have repeatedly emphasized the importance of Registrants' careful and considered preparation for the LIBOR Transition.[10] In addition, the LIBOR Transition is listed as one of OCIE's 2020 examination priority "risk themes" that would be used to "tailor its risk-based program" this year.[11] Consistent with those messages, the Risk Alert further emphasizes the importance of Registrants' preparations, and provides OCIE's views regarding the preparations required for a Registrant to effect an orderly transition away from LIBOR.

Risk Alert

The Risk Alert describes the "scope and content" for a series of risk-based examinations (often referred to as "sweep exams") that will focus on Registrants' preparedness for the LIBOR Transition.[12] The Risk Alert further emphasizes the theme of preparedness and provides some insight into what OCIE staff may view as steps Registrants could take in anticipation of the LIBOR Transition. The Risk Alert states OCIE's view that "[p]reparation for the transition away from LIBOR is essential for minimizing any potential adverse effects associated with LIBOR discontinuation" and that the “risks associated with this discontinuation and transition will be exacerbated if the work necessary to effect an orderly transition to an alternative reference rate is not completed in a timely manner.” As such, OCIE staff stresses that the LIBOR Exams are intended to “help promote and facilitate an orderly discontinuation … and transition.”

Examinations

Consistent with the above themes, the Risk Alert states that LIBOR Exams will assess (among other matters) “whether and how the registrant has evaluated the potential impact of the LIBOR transition on the organization’s: (i) business activities; (ii) operations; (iii) services; and (iv) customers, clients, and/or investors” (collectively, investors). By way of example, the Risk Alert states that OCIE will seek to review the Registrant’s preparation, plans and actions related to the LIBOR Transition, which could include an evaluation of:

- *Exposure to LIBOR and mitigation efforts.* OCIE will seek to understand and evaluate, to the extent relevant, the exposure of the Registrant and its investors to contracts that use LIBOR as a reference rate beyond the expected LIBOR Transition date, “including any fallback language incorporated into these contracts”;
- *Operational readiness for LIBOR Transition.* OCIE will review and evaluate enhancements or modifications the Registrant has made to its “systems, controls, processes, and risk or valuation models” in connection with the LIBOR Transition to a new reference rate;
- *Investor communications relating to the LIBOR Transition.* OCIE will examine the Registrant’s “disclosures, representations, and/or reporting to investors regarding its efforts to address LIBOR discontinuation and the adoption of alternative reference rates”;
- *Potential conflicts of interest.* OCIE will seek to understand and evaluate the Registrant’s identification and mitigation of “any potential conflicts of interest” related to the LIBOR Transition; and
- *Efforts to replace LIBOR.* OCIE will examine the Registrant’s actions taken to transition to an “appropriate alternative reference rate.”***Sample Document Request List***

The Risk Alert states that the sample document request list included in the Risk Alert is intended to “empower compliance professionals” to assess and assist with Registrants’ preparedness for the LIBOR Transition. While this list is a “resource” for Registrants to consult, it is not “all-inclusive” or “specifically indicative of the validation and testing” OCIE could perform. Thus, an actual document request list received by a Registrant is likely to vary based on the facts and circumstances. The Risk Alert also references the OCIE staff’s potential “review [of] certain information onsite.”

The types of documents set forth in the document request list can be broadly categorized as pertaining to:

- *Organizational structure and management.* This consists of information identifying aspects of a Registrant that might be impacted by the LIBOR Transition, as well as the personnel responsible for assessing, overseeing and managing LIBOR Transition efforts, including any third parties, and documentary evidence of the same (e.g., meeting minutes).
- *Assessment and management of LIBOR exposure.* This is documentation identifying: (i) potentially affected contracts or obligations of the Registrant or its investors, performance composites or advertisements, LIBOR-based models (e.g., risk, valuation), and investors (e.g., fee structures, performance reporting); (ii) the related underlying documents; and (iii) information regarding dependence on third-party service providers and the potential impact on their services. This also includes strategic plans or timelines for remediation, and any risk matrices “that reference” the LIBOR Transition.
- *Disclosures to stakeholders.* This includes information provided to governing bodies and filed with

the SEC.13

- *Guidance provided by the Registrant to its employees or supervised persons regarding recommendations or advice to investors, issuers or clients.* This includes: recommendations to investors regarding "LIBOR-linked instruments or contracts that extend past the current expected discontinuation date, reviews of portfolios containing such instruments, or the underwriting of new instruments referencing LIBOR"; advice to issuers as to "new LIBOR-linked instruments"; and advice to clients regarding outstanding contracts or obligations that replace LIBOR with an appropriate reference rate.
- *Modifications to operations or compliance programs made or anticipated.* This includes planned or implemented changes to various systems (e.g., "accounting, investor reporting, risk, valuation or trading") and "compliance procedures, controls, or surveillance systems."***Resources to Aid Registrants with the LIBOR Transition***

The Risk Alert encourages continued engagement by: suggesting that Registrants' personnel keep up-to-date on developments related to the LIBOR Transition via the AARC website; and inviting "the public to share information about the potential impact" of the LIBOR Transition via LIBOR@sec.gov.

Implications for U.S. and Non-U.S. Registrants

While the Risk Alert is the statement of one office of one regulator regarding how to prepare for the LIBOR Transition, its message should resonate across all market participants and jurisdictions. The message is consistent with statements from other regulators internationally: the issue of LIBOR Transition is not going away, and it is now time for Registrants and other market participants to focus on preparations for the LIBOR Transition. The Risk Alert is a signal that Registrants and other market participants are expected to be preparing for the transition from LIBOR and other IBORs. As indicated by the document request list, Registrants can begin by evaluating the potential impact of the LIBOR Transition on their businesses and operations, with a view toward implementing solutions that are appropriate in light of their exposure to LIBOR or other IBORs.

Regardless of a Registrant's state of preparation, the Risk Alert can prove valuable in helping Registrants better understand OCIE's view as to the type of preparations that could best effectuate an orderly transition. Registrants at the beginning stages of preparedness can use the Risk Alert to assess the scale and scope of the Registrant's current exposure to LIBOR, as well as a road map for managing an orderly LIBOR Transition. Registrants that are further down the road might view the Risk Alert as a checklist to assess their own progress. The Risk Alert (in particular, the sample document request list) also could be instructive to Registrants and other market participants in determining key documents that might be useful in identifying and managing any emerging risks across their businesses, and engaging and sharing information with various stakeholders about those risks and the Registrant's efforts to manage and/or mitigate them.

Dechert LLP – Philip T. Hinkle, Michael L. Sherman, Jonathan D. Gaynor, Ashley N. Rodriguez and Karen Stretch

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Dechert's Financial Services and Finance and Real Estate practice groups have significant experience and are available to assist firms on a collaborative basis to address concerns related to the LIBOR Transition, including guiding a Registrant through any SEC examinations.

Footnotes

1) Examination Initiative: LIBOR Transition Preparedness, National Exam Program Risk Alert, U.S.

SEC Office of Compliance Inspections and Examinations (June 18, 2020). The Risk Alert indicates that it “has no legal force or effect: it does not alter or amend applicable law, and it creates no new or additional obligations for any person.”

2) LIBOR also is referred to as ICE LIBOR and formerly as the London Interbank Offered Rate.

3) The methodologies used to determine LIBOR for a particular currency and tenor are based on submissions made by panel banks to the LIBOR benchmark administrator, ICE Benchmark Administration Limited (IBA), each London business day. The methodologies and panel banks per currency and tenor used are listed on IBA’s webpage. As a UK-based benchmark administrator, IBA is regulated by the UK’s Financial Conduct Authority.

4) Libor: Entering the Endgame, Andrew Bailey, Governor of the Bank of England (July, 13, 2020) (including an indication that LIBOR rates directly impact the cash flows and values of an estimated $400 trillion of financial products globally).

5) The Future of LIBOR, Andrew Bailey, then-Chief Executive of the FCA (July, 27 2017).

6) Panel banks have agreed to continue submitting the relevant data through 2021. However, absent an active market for unsecured term lending to banks, the FCA has determined not to compel banks to provide this information after 2021. The limitations of LIBOR as a reference rate have been widely reported, and the July 2020 speech by Andrew Bailey (footnote 4 supra) includes a discussion of this topic.
More generally, and historically, regulatory investigations in Europe and the United States following the 2007-2008 financial crisis revealed that for some years, both preceding and during the financial crisis, the volume of transactions in the interbank markets of the relevant currencies had decreased significantly. It was determined that the panel banks that contribute to the production of LIBOR were relying on their expert judgment, rather than observable market rates, for some of their submissions, and in many cases were manipulating their submissions to the benchmark administrator and, thus, manipulating LIBOR for certain tenors and currencies.

7) RFRs generally measure market rates for secured overnight borrowing. RFRs do not purport to capture the sort of counterparty credit risk or term component that may be represented in unsecured term borrowing rates, like LIBOR or other IBORs; thus, a spread adjustment would be needed for an RFR to serve as a commercially practical replacement reference rate for LIBOR or other IBORs.

8) SOFR and the SOFR Averages are published by the Federal Reserve Bank of New York.

9) For example, regulatory investigations in Europe and the United States following the 2007-2008 global financial crisis revealed that for some years, both preceding and during the financial crisis, the volume of transactions in the interbank markets of the relevant currencies had decreased significantly. It was determined that the panel banks that contribute to the production of LIBOR were relying on their expert judgment, rather than observable market rates, for some of their submissions, and in some cases were seen as manipulating their submissions to the benchmark administrator (and, thus, manipulating LIBOR for certain tenors and currencies).

10) For example, see SEC Public Statement, Staff Statement on LIBOR Transition (July 12, 2019); for further information, please refer to Dechert OnPoint, SEC Staff Issues Statement on LIBOR Transition; Practical Considerations for Investment Companies, Investment Advisers and Other Financial Institutions in Proactively Addressing LIBOR Cessation and Transition.

11) 2020 Examination Priorities, U.S. Office of Compliance Inspections and Examinations (Jan. 7, 2020) ("The risk-based approach, both in selecting registrants as examination candidates and in scoping risk areas to examine, provides OCIE with greater flexibility to cover emerging and exigent risks to investors and the marketplace as they arise. For example, as our registrants and other market participants transition away from LIBOR as a widely used reference rate in a number of financial instruments to an alternative reference rate, OCIE will be reviewing firms' preparations and disclosures regarding their readiness, particularly in relation to the transition's effects on investors. Some registrants have already begun this effort and OCIE encourages each registrant to evaluate its organization's and clients' exposure to LIBOR, not just in the context of fallback language in contracts, but its use in benchmarks and indices; accounting systems; risk models; and client reporting, among other areas. Insufficient preparation could cause harm to retail investors and significant legal and compliance, economic and operational risks for registrants"). For further information, please refer to Dechert OnPoint, OCIE Releases 2020 Examination Priorities.

12) Typically, the federal securities laws subject Registrants (and those required to be registered) to examination by the SEC. The SEC views examinations as a front-line means to protect investors and ensure compliance with the federal securities laws. Sweep examinations are focused on identified risks, and these examinations tend not to be as broad as routine examinations of Registrants.

13) The sample document request list indicates that the relevant period for filings with the SEC is from January 2019 to present.

LIBOR Summer Update: Regulatory Scrutiny Heats Up on Transition Preparedness - Sherman & Sterling

With fewer than 18 months until the expected cessation of the London Interbank Offered Rate (LIBOR), regulators have developed a keen interest on how financial institutions are preparing to transition from what has been called the "world's most important number." In recent weeks, a number of U.S. and global regulators have issued statements on the need for financial institutions to make actionable progress. On July 13, 2020, John C. Williams, President of the Federal Reserve Bank of New York, said "the importance of transitioning from LIBOR is so great that despite the effects of the COVID-19 pandemic, the overall timeline remains the same."[1] Notably, the transition was the focus of his first speech since the advent of the pandemic on a topic other than economic and monetary policy. Emphasizing the need for the market to "work together to ensure we are all ready for January 1, 2022," Mr. Williams stressed that "[i]t doesn't matter whether you're a large global bank or a local company with a handful of employees, you need to be prepared to manage your institution's transition away from LIBOR."

In this memorandum, we summarize some of the more recent statements by regulatory authorities on the LIBOR transition.

Global Regulatory Bodies Urge Action

The LIBOR transition has been called an "essential task" by the Financial Stability Board (FSB), and one that is directly related to global financial stability.[2] With the transition having been identified as a G20 priority, the FSB has joined the Basel Committee on Banking Supervision in issuing a report that identifies several remaining supervisory and other challenges to the transition, based on surveys taken by the FSB, the Basel Committee and the International Association of Insurance Supervisors.[3]

Among other findings, the report noted:

- Authorities are expecting financial institutions to make “significant progress” in 2020.
- From a microprudential perspective, the key concerns related to the LIBOR transition are in terms of operational risks; legal risks; prudential risks; conduct, litigation and reputational risks; hedging risks; and accounting risks.
- From a system-wide perspective, the uncertainty about the future of LIBOR as we get closer to the end of 2021 could increase macroprudential risks from heightened volatility or disorderly markets, as users are unable, unaware or unwilling to move to the new benchmarks.
- Challenges relating to contract amendments and the lack of term rates for risk-free rates (RFRs) are widely cited as the main obstacles to a successful transition for financial institutions.
- Lack of liquidity in new RFR products and the uncertainty of when sufficient liquidity will be achieved make it difficult to motivate market participants to shift to RFRs.
- For derivative contracts, financial institutions are awaiting the finalization of the ISDA fallback language and largely plan to adopt the ISDA protocol for the alternative reference rates. For cash products, authorities in many jurisdictions have raised concerns about the complexity of incorporating robust/standardized fallbacks into legacy contracts that do not have them, and the required operational readiness to facilitate their use.
- Authorities are concerned about the differing supervisory expectations for transition across jurisdictions, especially on legal and conduct risks. The varying transition timelines for different products is complicating the monitoring. There is a lack of clarity regarding the readiness of external systems used by financial institutions and others. Supervisors also have limited insight into, and communication with, the non-regulated clients of regulated financial institutions.
- Authorities have identified number of available tools of increasing supervisory intensity to speed up transition in case the increased monitoring and scrutiny do not prove sufficient. In the first stage these would include meetings with banks’ senior management, board of directors and the issuance of non-binding best practices. More intensive measures may include on-site inspections and requests to improve operational capabilities (e.g., risk-mitigation plans, requirements to increase resources aimed at supporting transition). In exceptional circumstances, some jurisdictions pointed to the use of capital charges and restrictions on specific product offerings, and finally administrative sanctions or other legal actions.

US Banking and Consumer Regulators Ramping Up LIBOR Transition Focus

On July 1, 2020, the Federal Financial Institutions Examination Council (FFIEC) issued a statement highlighting the financial, legal, operational and consumer protection risks that financial institutions will need to address as they prepare to transition away from LIBOR.[4] The discontinuation of LIBOR will affect nearly every financial institution, though larger institutions and those engaged materially in capital markets activities will face a more substantial impact.

The FFIEC’s statement does not constitute new guidance, nor it is a regulation, but it suggests an increasing emphasis within the bank examiner community that the LIBOR transition needs to be properly planned for and prioritized.

According to the FFIEC’s statement, institutions should first identify risks in their own on- and off-balance sheet assets and contracts that reference LIBOR, including derivatives, commercial and retail loans, investment securities and securitizations. Potential risks include:

- operational difficulty quantifying the exposure;
- financial, valuation and model risk related to reference rate transition;
- inadequate risk-management processes and controls to support the transition;
- consumer protection-related risks;

- limited ability of third-party service providers to support operation changes; and
- potential litigation and reputational risk arising from reference rate transition.

Following an identification of key risks and dependencies, institutions should quantify their LIBOR exposure. Generally, exposure is measured as the size of any activity and the number of counterparties or consumers with financial contracts that reference LIBOR across all products. This quantification should also include an assessment of the viability of existing contract fallback language. For contracts with inadequate fallback language, institutions need to develop a remediation strategy. To limit additional exposure, institutions should also discontinue the origination or purchase of LIBOR-indexed instruments.[5] For derivatives exposures, the FFIEC recommends that financial institutions and their clients eventually adhere to the International Swaps and Derivatives Association’s protocol upon its release.

In planning for the transition, institutions should consider the various legal, operational and other risks associated with various consumer financial products that reference LIBOR. Any replacement rate not already included in fallback language may impact consumers, increase reputation risk and result in legal exposure to institutions and the financial industry. Transition plans should, among other things, identify affected consumer loan contracts, highlight necessary risk mitigation efforts and address development of clear and timely consumer disclosures regarding changes in terms.

Relationships with third-party service providers is another key aspect of sound transition planning. When addressing third-party service providers that use LIBOR to provide valuation/pricing, modeling, accounting or other services, institutions should evaluate the preparedness and transition planning of those providers and consider whether they will be able to accommodate an alternative reference rate.

Significantly, the FFIEC has indicated that “the supervisory focus on evaluating institutions’ preparedness for LIBOR’s discontinuation will increase during 2020 and 2021, particularly for institutions with significant LIBOR exposure or less-developed transition processes.” Looking ahead, supervisory staff will ask institutions about their exposures to LIBOR-indexed instruments and details on their specific plans to transition away from LIBOR during regularly scheduled examinations and monitoring activities. In particular, the FFIEC identified the following areas as points for discussion with supervisory staff:

- identification and quantification of LIBOR exposure across product categories and lines of business;
- risk assessment of LIBOR exposures, which may include scenario testing, legal review and other analysis;
- transition plans with milestones and key completion dates addressing areas such as:
- strategies to inventory, analyze and assess risk posed by existing contracts;
- strategies to identify replacement rates, modify spreads and revise existing contracts, as necessary;
- strategies to address third-party risk management;
- potential impact to the institution’s customers;
- communication plans for engaging with customers and other stakeholders; and
- plans to identify, monitor and resolve system and other operational constraints;
- management’s assessment of revisions that may be necessary to update the institution’s policies, processes and internal control systems;
- responsibility for LIBOR transition oversight (to a committee, team or officer); and
- progress reporting to a supervised institution’s board of directors and senior management on the LIBOR transition plan.

While there is a recognition that the supervisory focus itself will depend on the size and complexity of each institution's LIBOR exposures, examiners expect "[a]ll institutions" to have transition plans and risk management processes in place.

SEC Eyes LIBOR Preparedness of Registrants

On June 18, 2020, the Securities Exchange Commission's (SEC) Office of Compliance Inspections and Examinations announced the details of an examination initiative specifically focused on the LIBOR preparedness of firms on the "buyside" of LIBOR-based products: SEC-registered investment advisers, broker-dealers, investment companies, municipal advisors, transfer agents and clearing agencies.[6] The announcement was accompanied by a sample document request that included items ranging from the assessments and plans undertaken to date, the identity of third parties that have been engaged to assist with the transition and materials referencing the LIBOR transition that have been provided to a registrant's board of directors. We have summarized the SEC's release in our memorandum of July 20, 2020.

Next Steps

Financial institutions of all kinds need to take recent statements by regulators seriously. Indeed, many financial institutions have already designed transition-related infrastructure and formulated plans. But having plans is not the same as actually executing them. There needs to be a full understanding of how to properly mitigate the various legal and other risks that arise from such tasks as executing contract amendments, communicating with customers and counterparties and responding to inquiries from regulators.

Footnotes

[1] John C. Williams, President and Chief Executive Officer, Federal Reserve Bank of New York, "537 Days: Time Is Still Ticking" (July 13, 2020).
[2] FSB, "FSB Statement on the Impact of COVID-19 on Global Benchmark Reform" (July 1, 2020).
[3] FSB and the Basel Committee on Banking Supervision, "Supervisory Issues Associated with Benchmark Transition: Report to the G20" (July 9, 2020).
[4] FFIEC, "Joint Statement on Managing the LIBOR Transition" (July 1, 2020). The FFIEC is composed of the principals of the following: the Federal Reserve Board, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, the State Liaison Committee and the Consumer Financial Protection Bureau. Various agencies with representatives on the FFIEC have made separate statements indicating that the LIBOR transition is a key supervisory priority for 2020 and 2021.
[5] The U.S. Alternative Reference Rates Committee (ARRC) has recently issued a set of "recommended best practices," which contained specific timelines for a variety of products. According to the ARRC, USD LIBOR should not be used in new transactions, with timing varying on the particular product: for floating rate notes, by December 31, 2020; for business loans, by June 30, 2021; for mortgages, by September 30, 2021; for securitizations other than CLOs, by June 30, 2021, and for CLOs by September 31, 2021; and for derivatives, by June 30, 2021. See "ARRC Recommended Best Practices for Completing the Transition from LIBOR" (May 27, 2020).
[6] SEC, "Examination Initiative: LIBOR Transition Preparedness" (June 18, 2020).

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July 23 2020

MSRB Board Prioritizes Investing in Technology and Reducing Compliance Burdens.

Washington, DC – The Board of Directors of the Municipal Securities Rulemaking Board (MSRB) convened virtually on July 29–30, 2020 for its final quarterly meeting of Fiscal Year 2020. The Board adopted an operating budget of $41.5 million for FY 2021 and approved designating $10 million of reserves for a multi-year strategic investment to modernize its market transparency systems to leverage the power of the cloud.

"We are poised to seize the potential of cloud-based technologies to begin delivering new market transparency tools and functionality to the market," said Ron Dieckman, Chair of the Board's Technology Committee. "We are tremendously excited to continue working with our Market Transparency Advisory Group to test out several promising prototypes in our new EMMA Labs platform."

The MSRB is developing EMMA Labs as an innovation hub where market stakeholders can collaborate on active prototypes and share feedback on preliminary concepts that could eventually make their way to the Electronic Municipal Market Access (EMMA®) website.

The MSRB will publish its budget detailing its operating expenses and technology investment when the fiscal year begins October 1, 2020. The Board also will announce the results of its elections for FY 2021 chair and vice chair in the coming weeks.

The MSRB could begin the fiscal year with a smaller Board under a proposal before the Securities and Exchange Commission (SEC) for approval. The MSRB's governance proposal also enhances the independence standard for public members of the Board and establishes a six-year lifetime service limit.

At its meeting the Board also discussed several major initiatives aimed at reducing compliance costs and burdens for regulated entities. Finally, the Board discussed its search for a new Chief Executive Officer and senior staff promotions.

Reducing Compliance Burdens

As part of its retrospective rule review, the Board discussed supervision requirements for dealers under MSRB Rule G-27 and approved a staff-led effort to conduct a comprehensive review of the historical body of interpretive guidance in the MSRB Rule Book. The review of guidance aims to identify opportunities to clarify, amend or delete guidance to help ensure it continues to achieve the intended purposes and takes into account the current state of the municipal securities market. The Board noted that input from stakeholders would be essential throughout this multi-year project.

"In our 45 years as the market's regulator, we have produced a vast library of interpretive guidance," said Gail Marshall, the MSRB's Chief Compliance Officer. "We believe this initiative will be an impactful way to support compliance and reduce unnecessary costs and burdens for regulated entities while balancing our regulatory obligation to protect investors and issuers."

The Board continued its discussion of the practice of pennying in the municipal securities auction process and directed staff to remain coordinated with the Financial Industry Regulatory Authority (FINRA).

The Board also discussed its efforts to advance regulated entities' understanding of MSRB rules through MuniEdPro®, a free online learning service featuring courses on core MSRB regulatory obligations and their application in practical scenarios.

Corporate Leadership

The MSRB announced today that it is promoting Jacob Lesser to Deputy General Counsel to lead the team responsible for governance and corporate legal matters. Lesser joined the MSRB as an associate general counsel and has played a critical role in the development of the Board's proposed enhancements to its governance rules. The MSRB also named Gail Marshall Interim Chief Regulatory Officer and Chief Compliance Officer, a role in which she will continue to lead the MSRB's market regulation activities, including rulemaking, enforcement coordination and professional qualifications. The MSRB is naming Leah Szarek Interim Chief External Relations Officer in recognition of her leadership of the MSRB's corporate communications and stakeholder engagement initiatives, as well as new responsibility for government relations.

"The Board is consistently impressed with the dedication and commitment of the staff, particularly as our market continues to feel the effects of the pandemic," said Board Vice Chair Manju Ganeriwala. "We are tremendously grateful for these individuals and the entire senior leadership team, whose experience and thoughtfulness help to advance our important mission."

The Board's CEO Search Special Committee is continuing its work to identify a new CEO. MSRB Chief Financial Officer Nanette Lawson has led the organization as interim CEO since October 1, 2019. Hear Lawson and other MSRB leaders speak about the MSRB's strategic initiatives and proactive response to the pandemic in a recent MSRB Podcast.

Bill Fitzgerald, Chair of the Board's CEO Search Special Committee, said, "Few decisions are more important for a Board than selecting the executive to lead and inspire the organization into the future. The pandemic has certainly changed the way our Board is going about its search process, but we remain optimistic that we will identify our candidate in the near future."

Date: July 31, 2020

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The SEC and DOJ Sign Historic Memorandum of Understanding to Enhance Competition in Securities Markets: BakerHostetler

On June 22, 2020, the Securities and Exchange Commission ("SEC") and Antitrust Division of the Department of Justice ("DOJ") Antitrust Division announced that they have signed an interagency Memorandum of Understanding ("MOU") to "foster competition and communication between the agencies" in an effort to enhance competition in the securities industry.[1] This is the first MOU between the DOJ's Antitrust Division and the SEC.

While the two enforcement agencies have worked together in the past, Assistant Attorney General Makan Delrahim stated that the MOU "institutionalizes a strong working relationship between" the agencies, which he expects will result in "robust, comprehensive analyses" regarding competition and securities law concerns.[2] According to Delrahim, this in turn could result in "healthier markets yielding enhanced consumer benefits."[3] SEC Chairman Jay Clayton also noted the MOU's goal of “greater collaboration and cooperation” between the agencies and the desire to ensure efficiency and competitiveness in U.S. markets.[4]

Competition in the Securities Markets

The presence of competition in the securities markets benefits customers on many levels, including competition on price, quality, service, and innovation.[5] Delrahim noted that firms that fear losing their market position are more likely to engage in these activities, thereby benefitting customers.[6] For example, firms may invest more in research and development to introduce new products or services to meet customer needs, seek out ways to streamline production processes, enhance the quality of their offerings, and pursue ways to make their products and services desirable.[7]

The SEC has consequently listened to concerns from market participants on where competition may be absent or diminished and has engaged in reviews of these concerns and the underlying industries to determine whether competition is lacking. This has led to various rule-making actions by the SEC, including the Market Data Proposal,[8] which is designed to update the national market system (“NMS”) for the “collection, consolidation, and dissemination of information with respect to quotations for and transactions in [NMS] stocks.”[9] The proposal also seeks to introduce competitive forces NMS for the first time. According to the SEC, the introduction of competition could allow all market participants — including investors — to access and benefit from the expanded content of NMS market data.[10] The Antitrust Division lauded the Market Data Proposal in its public comments, noting that it seeks to lower barriers to market entry, which improves quality of and access to inputs, such as information — a classic way to enhance competition.[11] This is a signal that the SEC is seeking to revisit and revise older regulations in an effort to enhance competition in the U.S. markets.

The Antitrust Division also commented on the procompetitive effects of the SEC’s Proxy Rules Proposal,[12] which, according to the SEC, is designed to “help ensure that proxy voting advice used by investors and others who vote on investors’ behalf is accurate, transparent, and materially complete.”[13] Delrahim noted that the proposed rule is also designed to update regulations to better fit the current landscape and lead to healthier competition.[14] In other words, while certain of the details of the markets have changed, competition remains wholly relevant.[15]

Increased Coordination Could Lead to Increased Investigations

Adopting the approach of continuously reviewing rules and regulations for their applicability and relevance in today’s markets, the SEC and the Antitrust Division entered into the MOU — the first of its kind — to establish regular communication between the agencies to allow for information sharing. Specifically, the MOU is targeted at facilitating communication and cooperation between the agencies, by establishing a framework for the SEC and the Antitrust Division to continue discussions and review regulatory matters that affect competition in the securities industry.[16] This includes provisions to establish periodic meetings among the agencies’ officials.[17] Additionally, the MOU provides for the exchange of information and expertise the agencies may believe relevant to their oversight and enforcement responsibilities, as consistent with legal and confidentiality restrictions.

Delrahim noted that the Division has taken on several complex criminal investigations in the financial services industry, including recent investigations into foreign currency exchange, interest rate benchmarks, and municipal bonds. For example, the agencies worked closely on an investigation of anticompetitive activity in the municipal bond investments market, which resulted in the conviction of one financial services firm and 17 individuals, and in restitution, penalties, and disgorgement related to four other financial institutions under non-prosecution agreements.[18] With help from the SEC, among others, the financial services firm agreed to pay restitution to victims of the anticompetitive conduct and to cooperate with the Antitrust Division regarding ongoing investigations into anticompetitive conduct in the municipal bonds industry. This could mean that the MOU serves as further justification for referrals between agencies that may result in criminal prosecution.

Is noteworthy that shortly after Delrahim's remarks, The Wall Street Journal suggested that the MOU may lead to antitrust scrutiny of fees charged by exchanges for information, including market data.[19] Chairman Clayton has previously noted that the SEC has an obligation under the Securities Exchange Act of 1934 "to suspend exchanges' fee filings unless it is established that the fee is reasonable on another basis, such as a reasonable cost basis,"[20] although, Section 11A of the 34 Act never uses the term "cost basis." Rather the law states that market data must be disseminated by securities information processors and securities exchanges on "fair and reasonable terms" and make that data available on terms that are not "unreasonably discriminatory." The government takes the position that the burden is on the exchange to demonstrate competitive forces or an alternative basis for finding the fee reasonable, while exchanges may well disagree. Exchanges argue that markets functioned well through the highest periods of volatility during the pandemic crisis and continue to do so. Further, they argue that significant changes to well-functioning market infrastructure, particularly during a pandemic, could introduce untold operational and technical risks, confusion and the likelihood for an unfriendly investor experience. Market structure reform raises highly complex, competitive and regulatory issues. This MOU could potentially result in litigation by and against the SEC or enforcement actions. In recent testimony before the Subcommittee on Investor Protection. Entrepreneurship and Capital Markets, SEC Chairman Clayton noted that the signing of the MOU with the Justice Department does not "imply that we are investigating anybody together."[21] When asked about potential anticompetitive behavior that may have been contemplated, Chairman Clayton informed the Subcommittee that they do not comment on investigations but rather the MOU "formalizes that powerful relationship that we have across our respective agencies."[22]

Conclusion
Although specific detail has not yet been provided on how the MOU will be put into effect, a number of circumstances now seem more likely:

- **Rule Changes:** The Antitrust Division and the SEC will likely continue to evaluate rules and regulations they deem outdated due to technological advances in the marketplace. There are, however, challenges in achieving this goal. Specifically, markets and data move quickly, which means that the agencies will need to move quickly to monitor industry developments and their effects, particularly in an effort to understand when intervention is appropriate and required.[23]
- **Parallel Investigations:** The agencies will share information on a more frequent basis, which may in turn lead to a greater number of investigations that could very well be done in parallel by both agencies. However, given confidentiality considerations as laid out in the MOU, it will be interesting to see how, if at all, the cooperation contemplated in the MOU will successfully interact with the Antitrust Division's Leniency Program and/or the SEC's whistleblower and cooperation program.

[1] U.S. Sec. & Exch. Comm'n., Press Release, Rel. No. 2020-140, "Securities and Exchange Commission and Justice Department's Antitrust Division Sign Historic Memorandum of Understanding" (June 22, 2020), available at https://www.sec.gov/news/press-release/2020-140; U.S. Dep't. of Justice, Justice News, "Justice Department's Antitrust Division And The Securities And Exchange Commission Sign Historic Memorandum of Understanding" (June 22, 2020), available at https://www.justice.gov/opa/pr/justice-department-s-antitrust-division-and-securities-and--xchange-commission-sign-historic. The MOU is available at https://www.sec.gov/files/ATR-SEC%20MOU-06-22-2020.pdf.

[2] Id.
[3] Id.
[4] Id.
[5] U.S. Dep't. of Justice, Justice News, "Changes in Latitudes, Changes in Attitudes: Enforcement Cooperation in Financial Markets (June 22, 2020), available at https://www.justice.gov/opa/speech/changes-latitudes-chang-s-attitudes-enforcement-cooperation-financial-markets ("Delrahim Speech").
[6] Id.
[7] Id.
[8] 17 CFR Parts 240, 242, and 249; Rel. No. 34-88216.
[9] Id. at p. 1.
[10] U.S. Sec. & Exch. Comm'n., Press Release, Rel. No 2020-34, "SEC Proposes to Modernize Key Market Infrastructure Responsible for Collecting, Consolidating, and Disseminating Securities Market Data" (Feb. 14, 2020), available at https://www.sec.gov/news/press-release/2020-34.
[11] Supra note 5.
[12] 17 CFR Part 240, Rel. No. 34-87457.
[13] U.S. Sec. & Exch. Comm'n., Press Release, Rel. No. 2019-231, "SEC Proposes Rule Amendments to Improve Accuracy and Transparency of Proxy Voting Advice" (Nov. 5, 2019), available at https://www.sec.gov/news/press-release/2019-231.
[14] Delrahim Speech.
[15] Id.
[16] Id.
[17] Id.
[18] Delrahim Speech; see also U.S. Dep't. of Justice, Justice News, "GE Funding Capital Market Services Inc. Admits to Anticompetitive Conduct by Former Traders in the Municipal Bond Investments Market and Agrees to Pay $70 Million to Federal and State Agencies" (Dec. 23, 2011), available at https://www.justice.gov/opa/pr/ge-funding-capital-market-services-inc--dmits-anticompetitive-conduct-former-traders.
[19] Dave Michaels and Alexander Osipovich, The Wall Street Journal, "SEC, Justice Department to Scrutinize Exchanges' Market-Data Business" (June 22, 2020), available at https://www.wsj.com/articles/sec-justice-department-to-scrutinize-exch-nges-market-data-business-11592864481.
[20] U.S. Sec. & Exch. Comm'n., Speech, "Modernizing U.S. Equity Market Structure" (June 22, 2020), available at https://www.sec.gov/news/speech/clayton-redfearn-modernizing-us-eq-ity-market-structure-2020-06-22.
[21] See "Hybrid Hearing – Capital Markets and Emergency Lending in the COVID-19 Era," June 25, 2020, before the Subcommittee on Investor Protection. Entrepreneurship and Capital Markets, Committee on Financial Services, U.S. House of Representatives, available at: http://archives-financialservices.house.gov/media/pdf/072601rb.pdf.
[22] Id.
[23] Delrahim Speech.

BakerHostetler

July 15, 2020

NABL Submits Letter to IRS and Treasury.

On July 22, 2020, NABL submitted a letter to the Treasury and IRS to inform the development of their 2020-2021 Priority Guidance Plan.

Topics include: recommendations to provide cash flow relief to issuers and borrowers from economic difficulties caused by COVID-19, recommendations to provide better access to capital markets for issuers and borrowers to deal with the economic difficulties caused by COVID-19, and additional requests for further guidance.

Find the full letter here.

MSRB Compliance Corner Newsletter.

Read about the MSRB's resources on 529 plans, recent enforcement actions and more in the latest Compliance Corner newsletter.

NFMA Cybersecurity White Paper.

The National Federation of Municipal Analysts released a draft White Paper on Best Practices in Cybersecurity Risk Disclosure for State & Local Governments in Municipal Offerings. The paper is in the comment period until September 20, 2020.

To read the paper, click here.

GASB Adds Resources to Emergency Toolbox Addressing Issues Arising from COVID-19 Pandemic.

Norwalk, CT, July 20, 2020 — During the development of the recently issued Technical Bulletin 2020-1, *Accounting and Financial Reporting Issues Related to the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) and Coronavirus Diseases*, several issues were raised that were not specifically addressed in the Technical Bulletin, but for which current authoritative standards provide guidance.

To assist stakeholders with those issues, the GASB has updated its Emergency Toolbox, which addresses accounting and financial reporting issues that may arise during the ongoing COVID-19 pandemic.

The following issues have been added:

- Disclosures related to outflows of resources incurred in response to COVID-19
- Donated inventory
- Nonexchange financial guarantee disclosures
- Subsequent contravention of eligibility requirements
- Classification of transactions not specifically addressed in Category A or Category B authoritative literature as either operating or nonoperating revenues and expenses
- Extension of property tax due dates
- Subsequent events disclosures for legislation enacted after the end of the reporting period.

The GASB provides a number of additional stakeholder resources that may be useful during this period on its website at www.gasb.org/COVID19.

GASB Requests Input on Proposals to Improve Key Components of Government Financial Reports.

Norwalk, CT, July 24, 2020 — The Governmental Accounting Standards Board (GASB) today issued for public feedback a proposed Statement that is designed to improve to key components of the blueprint for state and local government annual financial reports.

- The Exposure Draft, *Financial Reporting Model Improvements*, proposes improvements that are designed to:Enhance the effectiveness of financial reports in providing information essential for making decisions and assessing a government's accountability, and
- Address certain application issues.

The Exposure Draft includes proposals that would establish or modify existing accounting and financial reporting requirements related to:

- Application of the short-term financial resources measurement focus and accrual basis of accounting in governmental funds (replacing the existing current financial resources measurement focus and modified accrual basis of accounting)
- Management's discussion and analysis
- Presentation of governmental fund financial statements
- Presentation of the proprietary fund statement of revenues, expenses, and changes in fund net position
- Unusual or infrequent items
- Budgetary comparison information.

The changes in the proposed Statement would improve financial reporting in a variety of ways. For example, the proposed short-term financial resources measurement focus and accrual basis of accounting would improve the consistency of the information in governmental fund financial statements. The proposed changes to the presentation of governmental fund financial statements would (1) make the short-term nature of their information more evident and understandable and (2) more clearly differentiate them from the long-term perspective of the government-wide financial statements.

Stakeholders are asked to review the proposals and provide input on the document by February 26, 2021. A series of public hearings and user forums on the Exposure Draft tentatively have been scheduled for March and April 2021 to further enable stakeholders to share their views with the Board. More information about commenting on the Exposure Draft and participating in the public hearings and users forums can be found in the document.

BDA Sends Comments to SEC on Proposed Changes to MSRB Rules A-3 and A-6 on Board Composition and Governance.

BDA this morning filed a comment letter with the SEC on proposed changes to MSRB Rules A-3 and A-6 on board composition and governance. The proposal before the SEC is available here.

BDA's comment letter is available here.

Senator Kennedy's MSRB reform bill is available here.

The proposed changes will, when approved by the SEC, impose these changes:

- Reduce the size of the MSRB board from 21 to 15, with a transitional 17-member board in 2021, with the new board being comprised of eight independent members and seven industry representatives
- Specify that at least two of the seven industry representatives must be from non-dealer Municipal Advisor firms; and
- Specify that independent board members, if they previously worked for regulated companies, must be away from the industry for five years to qualify for a board position as opposed to the current two, among other changes.

In our letter to the SEC, we state that BDA opposes "the MSRB's Proposal and we urge the Commission to reject the initiative." On the issue of independent directors, we state that "five years away from the industry and the market is too long for a Board member to be effective." On the issue of a minimum of two directors being MAs, we state "we call on the MSRB to set the ratio of board seats between dealers and MAs based on each constituency's relative financial contribution to the organization, subject to statutory requirements."

It is likely that the SEC will approve the MSRB's proposal without amendment. It is also likely that the MSRB's motivation for this change is to forestall action by Senator John Kennedy (R-LA) on his broader MSRB reform legislation.

Please call or write if you have any questions.

Bond Dealers of America

July 15, 2020

Libor Showed its Weakness in Coronavirus Market Crisis.

The deadline for the phaseout of Libor at the end of 2021 will not be delayed and despite the effects of the COVID-19 pandemic, progress is being made on the switch to alternative reference rates.

That was the message of New York Federal Reserve officials in two webcast presentations Monday and Wednesday.

New York Federal Reserve President John Williams said Monday in a joint presentation with Bank of England Governor Andrew Bailey that the transition away from Libor "continues to be of paramount importance."

"The clock is still ticking," Williams said. "It's critical that regulators and institutions continue to work together to ensure they're all ready for January 1, 2022."

The No. 1 priority, according to Williams, "is to stop writing Libor contracts."

The London Interbank Offered Rate is a widely used benchmark for short-term interest rates based on data contributed by participating banks. It was tarnished by rate-rigging scandals.

Market participants who continue to use Libor are driven by nostalgia because it’s not a robust reference rate, Williams said.

Bailey highlighted that weakness by discussing the recent market crisis that occurred as worldwide awareness grew of the impact of the pandemic.

The week of March 16 when central bank rates were at historically low levels, “over half of the 35 published Libor rates across all currencies contain no transaction-based submissions at all,” said Bailey. Simultaneously, Bailey said, “Libor rates, and therefore costs with borrowers, spiked upwards.”

In contrast, the Secured Overnight Financing Rate (SOFR), which is being promoted as an alternative to Libor in the United States, held its volumes and weathered the crisis.

David Bowman, senior associate director of the Federal Reserve, said during Wednesday’s presentations that the SOFR market now accounts for over $1 trillion of transactions daily.

“It is produced in a transparent and direct manner,” said Bowman. “It is based on observable transactions, not dependent on estimates like Libor or derived from some model.”

The SOFR, which the Federal Reserve Bank of New York publishes on its website each weekday, represents the rate in the repo market the previous day. It is published in the morning and finalized at 2:30 p.m. Eastern time.

The New York Fed also publishes 30-day, 90-day and 100-day compound averages of SOFR.

The SOFR index, also published by the New York Fed, can be used to calculate a customized compound average over any period the user chooses.

“People forget that the reason that we have to go through this transition is because of the way the financial system structured itself,” said Bowman. “It put far too much weight on a rate that was far too weak. And now we’re dealing with the consequences.”

John Gerli, chief capital markets officer of the Federal Home Loan Bank’s Office of Finance, said his experience with SOFR so far has provided him encouragement that the investor base may be broader than it was with Libor.

“Some of them have said that it’s a good substitute for repo, and it’s a cash and highly liquid marketplace,” Gerli said. “So I think from our perspective, at least in two years out [from the phaseout] the investor base here, may be broader.”

By Brian Tumulty

BY SOURCEMEDIA | ECONOMIC | 07/15/20 03:35 PM EDT

[LIBOR Summer Update: Regulatory Scrutiny Heats Up on Transition Preparedness - Sherman & Sterling]

With fewer than 18 months until the expected cessation of the London Interbank Offered Rate (LIBOR), regulators have developed a keen interest on how financial institutions are preparing to transition from what has been called the "world's most important number." In recent weeks, a number of U.S. and global regulators have issued statements on the need for financial institutions to make actionable progress. On July 13, 2020, John C. Williams, President of the Federal Reserve Bank of New York, said "the importance of transitioning from LIBOR is so great that despite the effects of the COVID-19 pandemic, the overall timeline remains the same."[1] Notably, the transition was the focus of his first speech since the advent of the pandemic on a topic other than economic and monetary policy. Emphasizing the need for the market to "work together to ensure we are all ready for January 1, 2022," Mr. Williams stressed that "[i]t doesn't matter whether you're a large global bank or a local company with a handful of employees, you need to be prepared to manage your institution's transition away from LIBOR."

In this memorandum, we summarize some of the more recent statements by regulatory authorities on the LIBOR transition.

Global Regulatory Bodies Urge Action

The LIBOR transition has been called an "essential task" by the Financial Stability Board (FSB), and one that is directly related to global financial stability.[2] With the transition having been identified as a G20 priority, the FSB has joined the Basel Committee on Banking Supervision in issuing a report that identifies several remaining supervisory and other challenges to the transition, based on surveys taken by the FSB, the Basel Committee and the International Association of Insurance Supervisors.[3]

Among other findings, the report noted:

- Authorities are expecting financial institutions to make "significant progress" in 2020.
- From a microprudential perspective, the key concerns related to the LIBOR transition are in terms of operational risks; legal risks; prudential risks; conduct, litigation and reputational risks; hedging risks; and accounting risks.
- From a system-wide perspective, the uncertainty about the future of LIBOR as we get closer to the end of 2021 could increase macroprudential risks from heightened volatility or disorderly markets, as users are unable, unaware or unwilling to move to the new benchmarks.
- Challenges relating to contract amendments and the lack of term rates for risk-free rates (RFRs) are widely cited as the main obstacles to a successful transition for financial institutions.
- Lack of liquidity in new RFR products and the uncertainty of when sufficient liquidity will be achieved make it difficult to motivate market participants to shift to RFRs.
- For derivative contracts, financial institutions are awaiting the finalization of the ISDA fallback language and largely plan to adopt the ISDA protocol for the alternative reference rates. For cash products, authorities in many jurisdictions have raised concerns about the complexity of incorporating robust/standardized fallbacks into legacy contracts that do not have them, and the required operational readiness to facilitate their use.
- Authorities are concerned about the differing supervisory expectations for transition across jurisdictions, especially on legal and conduct risks. The varying transition timelines for different products is complicating the monitoring. There is a lack of clarity regarding the readiness of external systems used by financial institutions and others. Supervisors also have limited insight into, and communication with, the non-regulated clients of regulated financial institutions.

- Authorities have identified number of available tools of increasing supervisory intensity to speed up transition in case the increased monitoring and scrutiny do not prove sufficient. In the first stage these would include meetings with banks' senior management, board of directors and the issuance of non-binding best practices. More intensive measures may include on-site inspections and requests to improve operational capabilities (e.g., risk-mitigation plans, requirements to increase resources aimed at supporting transition). In exceptional circumstances, some jurisdictions pointed to the use of capital charges and restrictions on specific product offerings, and finally administrative sanctions or other legal actions.

US Banking and Consumer Regulators Ramping Up LIBOR Transition Focus

On July 1, 2020, the Federal Financial Institutions Examination Council (FFIEC) issued a statement highlighting the financial, legal, operational and consumer protection risks that financial institutions will need to address as they prepare to transition away from LIBOR.[4] The discontinuation of LIBOR will affect nearly every financial institution, though larger institutions and those engaged materially in capital markets activities will face a more substantial impact.

The FFIEC's statement does not constitute new guidance, nor it is a regulation, but it suggests an increasing emphasis within the bank examiner community that the LIBOR transition needs to be properly planned for and prioritized.

According to the FFIEC's statement, institutions should first identify risks in their own on- and off-balance sheet assets and contracts that reference LIBOR, including derivatives, commercial and retail loans, investment securities and securitizations. Potential risks include:

- operational difficulty quantifying the exposure;
- financial, valuation and model risk related to reference rate transition;
- inadequate risk-management processes and controls to support the transition;
- consumer protection-related risks;
- limited ability of third-party service providers to support operation changes; and
- potential litigation and reputational risk arising from reference rate transition.

Following an identification of key risks and dependencies, institutions should quantify their LIBOR exposure. Generally, exposure is measured as the size of any activity and the number of counterparties or consumers with financial contracts that reference LIBOR across all products. This quantification should also include an assessment of the viability of existing contract fallback language. For contracts with inadequate fallback language, institutions need to develop a remediation strategy. To limit additional exposure, institutions should also discontinue the origination or purchase of LIBOR-indexed instruments.[5] For derivatives exposures, the FFIEC recommends that financial institutions and their clients eventually adhere to the International Swaps and Derivatives Association's protocol upon its release.

In planning for the transition, institutions should consider the various legal, operational and other risks associated with various consumer financial products that reference LIBOR. Any replacement rate not already included in fallback language may impact consumers, increase reputation risk and result in legal exposure to institutions and the financial industry. Transition plans should, among other things, identify affected consumer loan contracts, highlight necessary risk mitigation efforts and address development of clear and timely consumer disclosures regarding changes in terms.

Relationships with third-party service providers is another key aspect of sound transition planning. When addressing third-party service providers that use LIBOR to provide valuation/pricing, modeling, accounting or other services, institutions should evaluate the preparedness and transition planning of those providers and consider whether they will be able to accommodate an alternative reference rate.

Significantly, the FFIEC has indicated that "the supervisory focus on evaluating institutions' preparedness for LIBOR's discontinuation will increase during 2020 and 2021, particularly for institutions with significant LIBOR exposure or less-developed transition processes." Looking ahead, supervisory staff will ask institutions about their exposures to LIBOR-indexed instruments and details on their specific plans to transition away from LIBOR during regularly scheduled examinations and monitoring activities. In particular, the FFIEC identified the following areas as points for discussion with supervisory staff:

- identification and quantification of LIBOR exposure across product categories and lines of business;
- risk assessment of LIBOR exposures, which may include scenario testing, legal review and other analysis;
- transition plans with milestones and key completion dates addressing areas such as:- strategies to inventory, analyze and assess risk posed by existing contracts;
  – strategies to identify replacement rates, modify spreads and revise existing contracts, as necessary;
  – strategies to address third-party risk management;
  – potential impact to the institution's customers;
  – communication plans for engaging with customers and other stakeholders; and
  – plans to identify, monitor and resolve system and other operational constraints;
- management's assessment of revisions that may be necessary to update the institution's policies, processes and internal control systems;
- responsibility for LIBOR transition oversight (to a committee, team or officer); and
- progress reporting to a supervised institution's board of directors and senior management on the LIBOR transition plan.

While there is a recognition that the supervisory focus itself will depend on the size and complexity of each institution's LIBOR exposures, examiners expect "[a]ll institutions" to have transition plans and risk management processes in place.

SEC Eyes LIBOR Preparedness of Registrants

On June 18, 2020, the Securities Exchange Commission's (SEC) Office of Compliance Inspections and Examinations announced the details of an examination initiative specifically focused on the LIBOR preparedness of firms on the "buyside" of LIBOR-based products: SEC-registered investment advisers, broker-dealers, investment companies, municipal advisors, transfer agents and clearing agencies.[6] The announcement was accompanied by a sample document request that included items ranging from the assessments and plans undertaken to date, the identity of third parties that have been engaged to assist with the transition and materials referencing the LIBOR transition that have been provided to a registrant's board of directors. We have summarized the SEC's release in our memorandum of July 20, 2020.

Next Steps

Financial institutions of all kinds need to take recent statements by regulators seriously. Indeed, many financial institutions have already designed transition-related infrastructure and formulated plans. But having plans is not the same as actually executing them. There needs to be a full understanding of how to properly mitigate the various legal and other risks that arise from such tasks as executing contract amendments, communicating with customers and counterparties and responding to inquiries from regulators.

Shearman & Sterling LLP – Mark Chorazak, Patrick Clancy , Reena Agrawal Sahni, Lona Nallengara, Donna Parisi and Geoffrey B. Goldman

July 23 2020
