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Ballard Spahr: Industry Concerns Prompt SEC to Modify MCDC Initiative.

In response to concerns raised by industry participants, the Securities and Exchange Commission (SEC) has made some modifications to its Municipalities Continuing Disclosure Cooperation Initiative (MCDC Initiative). The SEC hopes the MCDC Initiative, announced on March 10, 2014, will encourage self-reporting by municipal securities issuers and underwriters of possible securities law violations arising from misstatements in offering documents about an issuer's prior compliance with its continuing disclosure obligations. A summary of the MCDC Initiative can be found here.

The SEC initially imposed a deadline of September 10, 2014, for all self-reporting under the MCDC Initiative. In view of the substantial burden of analyzing prior disclosures, numerous industry groups—including the Government Finance Officers Association, the Securities Industry and Financial Markets Association, Bond Dealers of America, and the National Association of Bond Lawyers—defense counsel, and U.S. Representative Steve Stivers, among others, raised concerns with the SEC, urging the agency to extend the deadline, limit the broad scope of the MCDC Initiative, and consider its unequal impact on smaller issuers, obligated persons, and underwriters.

Yesterday, the SEC responded in part by undertaking three key modifications. First, although the SEC publicly expressed reluctance to extend the MCDC Initiative deadline, issuers and obligated persons will now have until December 1, 2014 to self-report. The SEC declined to provide this extension to the prior deadline imposed upon underwriters to self-report.

Second, in an effort to encourage smaller underwriters to avail themselves of the MCDC Initiative, the SEC announced a tiered approach to civil penalties imposed on underwriters:

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

Finally, the SEC recognized the limitations in auditing continuing disclosure compliance prior to the Electronic Municipal Market Access (EMMA) system becoming the single, official repository for continuing disclosure information on July 1, 2009. The former Nationally Recognized Municipal Securities Information Repositories (NRMSIRs) system was a decentralized and unreliable source of continuing disclosure information. If the SEC identifies securities law violations after the MCDC Initiative self-reporting deadline, it stated that it will consider good faith efforts to discover violations that occurred pre-EMMA in determining whether to recommend an enforcement action or the type of relief sought if an enforcement action is undertaken.

The SEC's decision not to extend the deadline for underwriters will significantly impair the ability of underwriters and issuers or obligated persons to coordinate self-reporting, as underwriters will have to make their final materiality determinations far in advance of issuers and obligated persons. It is also unclear whether issuers and obligated persons will benefit from any cease and desist orders announced by the SEC against underwriters prior to their new self-reporting deadline. Such orders could provide guidance on the types of misstatements and omissions the SEC considers material under federal securities law. However, the SEC's first MCDC Initiative cease and desist order included only a cursory materiality analysis and was vague on the facts underlying the order. A summary can be found here.

To assist market participants in understanding how materiality is proven under federal securities law through market analysis, Ballard Spahr will host a brief webinar on August 7, 2014, at 12:00 p.m. ET, featuring economist Vinita Juneja, Ph.D. Register for the webinar here.

by John C. Grugan, Bradley D. Patterson, William C. Rhodes, Teri M. Guarnaccia, and Tesia N. Stanley

Ballard Spahr's Municipal Securities Regulation and Enforcement Group helps municipal market participants navigate a rapidly evolving regulatory, investigative, and enforcement environment, enabling them to anticipate and address compliance issues and respond effectively to investigations when necessary.

For more information, please contact John C. Grugan at 215.864.8226 or gruganj@ballardspahr.com, Bradley D. Patterson at 801.531.3033 or patterson@ballardspahr.com, William C. Rhodes at 215.864.8534 or rhodes@ballardspahr.com, Teri M. Guarnaccia at 410.528.5526 or guarnacciat@ballardspahr.com, or Tesia N. Stanley at 801.517.6825 or stanleyt@ballardspahr.com.