
SEC Weighs Providing Legal Guidance on Role of MAs in Bank Loans.

CHARLESTON, S.C. — The Securities and Exchange Commission's Office of Municipal Securities is weighing whether to provide legal interpretive guidance to help municipal advisors determine if they are acting as an adviser or broker-dealer when working with an issuer on a bank loan.

Rebecca Olsen, deputy director of OMS, told those attending the National Association of Municipal Advisors annual conference here that the role an MA plays in bank loans has raised legal issues because advisors, who owe fiduciary duties to their clients, and broker-dealers, who act as intermediaries, operate in different regulatory regimes. She said her office "could consider" providing the guidance, in close coordination with the SEC's division of trading and markets.

"We completely understand that the definition of municipal advisor contemplates advice with respect to structure, timing and terms of an offering of municipal securities that would typically require broker-dealer registration and that this is creating legal interpretive issues," Olsen said.

The issue, she said, is whether the bank loan should be considered a security and whether an advisor dealing with the bank loan is "acting only as an advisor in providing advice in the capacity of their advisory relationship with their client" or whether they are acting as a broker by entering into the business of effecting a transaction in the securities of others. The first question fits into an ongoing discussion best answered by the 1990 case Reves v. Ernst & Young. In that case, the court ruled that notes were presumably securities, but allowed for that presumption to be overcome if the notes bore a strong resemblance to another note that was not a security. The ruling said an instrument is a security if: it is motivated by investment or commercial purpose; it is traded for speculation and investments; the public views the transaction as a security; or it falls under other federal regulations which make applying the securities laws unnecessary.

If the test shows the instrument is not a security, the need to distinguish between MA and broker-dealer is moot because the Securities Exchange Act of 1934 rules for broker-dealers and the Municipal Securities Rulemaking Board rules only apply to municipal securities, Olsen said.

She said the issue of whether an individual is acting as an advisor or a broker-dealer is "more difficult" because "there is no bright line" and any answer requires "a very factually intensive analysis."

Olsen suggested the trading and markets division's guide on broker-dealer registration may help MAs determine whether they are acting as broker-dealers and participating in important parts of the securities transaction. Key parts of a securities transaction include: solicitation, execution of the transaction, conversations about the size of the transaction, and whether the MA handles the securities of others in connection with the securities transaction.

Bank loans also have raised other questions in the market, such as whether and how often an issuer should disclose them. They do not qualify as a material event under SEC Rule 15c2-12 on continuing disclosure, meaning any effort to disclose them requires an issuer to volunteer the information.

Allen Robertson, a managing partner at Robinson, Bradshaw & Hinson, said during a later panel that issuers' or obligated persons' decisions to disclose bank loans fall outside the scope of advice a lawyer advising them should give. Robertson, a former president of the National Association of Bond Lawyers, said NABL determined a lawyer's job is to make sure issuers and borrowers understand the risks and considerations behind any type of voluntary disclosure. Armed with that information, their clients can make an informed business judgment.

The three concerns a lawyer might raise, according to Robertson, are whether voluntarily disclosing the bank loan: opens the issuer up to a continual liability to provide general updates; means the issuer is committing itself to provide information about all future bank loans; or requires the issuer to make a disclosure any time the loan is amended. While he said there are likely ways to avoid each of those concerns while still disclosing, he said that legally there is no "black and white answer."

The two rating agency officials on the panel both advocated for disclosure whenever possible because it allows for a more complete picture of an issuer's ability to pay its debt.

"I will never tell you not to disclose a bank loan," said Tom Jacobs, senior vice president and manager of Moody's municipal supported products group. "The more transparent the market is, the happier we will be."

Loans are particularly worrisome when the banks have acceleration rights that allow them to seek immediate repayment if ratings or other indicators of an issuer's ability to repay the debt diminish, Jacobs said. When acceleration rights are written into a loan, bondholders without the rights become subordinate and have to wait behind the banks for payment.

Diane Brosen, managing director for Standard & Poor's corporate and government ratings, said that a few years ago, issuers questioned why rating agencies needed information about bank loans.

"We at Standard & Poor's felt like we had to go to the issuers and let them know how important this was to the market," Brosen said.

Many issuers now more readily supply bank loan information, but Brosen said there is still an issue, especially with smaller community banks that are harder to reach. She asked any MAs in the audience who are involved in bank loans with smaller banks to spread the message of the need for disclosure.

National Federation of Municipal Analysts industry and media liaison Bill Oliver mentioned NFMA's recent white paper urging issuers to disclose bank loans. He challenged the idea that issuers will always be able to access the capital market and that there is a good level of liquidity present regardless of their disclosure practices.

"The market does have a fragile side to it and I think disclosure and having a disclosure track record for your issuers is really important," Oliver told the audience. "This notion about disclosure being voluntary is outdated."

THE BOND BUYER

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OCT 9, 2015 10:31am ET