
MCDC's Appropriateness, Effect on Market Disclosure Debated.

CHICAGO – A regulatory official and market participants sparred over the merits of the Securities and Exchange Commission's voluntary continuing disclosure enforcement initiative during a panel here on Wednesday while acknowledging the need to improve municipal disclosure.

The industry roundtable at the National Federation of Municipal Analysts' annual conference was designed to address a variety of disclosure issues across the municipal market, such as the recent lack of bank loan disclosure, but quickly narrowed to a discussion of the changes in disclosure that have occurred as a result of the SEC's Municipalities Continuing Disclosure Cooperation initiative.

The MCDC initiative promised underwriters and issuers lenient settlements if they self-reported instances where issuers falsely said in offering documents that they were in compliance with their continuing disclosure agreements. Altogether, 72 underwriters representing 96% of the underwriting market by volume, paid $18 million to settle violations with the SEC under the initiative. The SEC has already started reaching out to issuers about settlements and has said it intends to pursue actions against those who didn't report under the program after it finishes settling with those who did.

Ben Watkins, Florida's director of bond finance who represented the Government Finance Officers Association on the panel, advocated for voluntary efforts among industry participants to solve disclosure challenges instead of a regulatory or enforcement solution like the one chosen by the SEC. The Securities Industry and Financial Markets Association has taken the lead in holding meetings for such discussions, which have also included market groups like GFOA, the NFMA, and the National Association of Bond Lawyers.

"My own personal point of view is [MCDC] was the most misguided, coercive, punitive approach to improving continuing disclosure that I have ever seen," Watkins said. "It was a monumental waste of resources."

Michael Decker, a managing director and co-head of municipal securities for SIFMA, said he couldn't think of "very much good to say about MCDC," going on to call it "a very frustrating experience from the industry's perspective."

"Maybe the most frustrating aspect of it was the enforcement people were addressing an issue where nobody lost money," he said. "Nobody lost a penny and still it cost issuers and underwriters many hundreds of millions of dollars."

Watkins said a study GFOA had conducted found that MCDC led to an average out-of-pocket cost for issuers of between $7,000 and $10,000.

But others on the panel, led by SEC Office of Municipal Securities head Jessica Kane, saw MCDC in a more positive light.

“From my perspective, the MCDC program was very successful. There was robust participation,” Kane said. “It especially heightened the focus of the market on continuing disclosure obligations.”

She added that the mandatory portions of the settlements that required underwriters to hire and retain independent compliance consultants are a “really great benefit.” She also emphasized that the initiative was a voluntary way to address past securities law violations and did not require anyone to participate.

Watkins said skeptically that Kane was calling it “voluntary and cooperative when the [SEC] says ‘if you don’t do it we’re going to come find you and throw you in jail.'”

All the participants, however skeptical, acknowledged that the industry is more focused on disclosure now than it was before MCDC.

Lisa Washburn, the NFMA’s chair and the panel moderator, said she and other analysts saw “a bunch of filings” come into the EMMA system after the initiative was announced. She also noted that MCDC helped spur SIFMA to organize the other industry groups to talk more about disclosure.

Decker said SIFMA has been pursuing changes both by itself and with the group since the industry groups first met in October. Most recently, SIFMA sent a white paper to the SEC outlining various changes it believes should be made to SEC Rule 15c2-12 on disclosure. Among other things, the paper asks the SEC to extend due diligence requirements to MAs that have worked with issuers on official statements, especially in competitive transactions, and improve the timeliness of issuers’ annual disclosures after the end of their fiscal years.

“We thought for five minutes about seeking statutory changes and asking Congress to give the SEC more authority to regulate issuer disclosure more directly, but that didn’t really seem politically feasible and I think the issuer community historically has been opposed to that for some pretty good reasons,” Decker said. “We did look at areas where short of regulation we think there could be some improvement.”

Others said the main problem with disclosure lies with an issuer’s staff, resources, and educational capabilities. Watkins said getting everyone educated about proper disclosure practices is “a monumental task” and added that while larger issuers usually have “robust” disclosure, many smaller issuers have trouble. One example cited by panelists was when an official for a small issuer may have multiple responsibilities beyond overseeing the issuer’s finances.

Bill Daly, NABL’s director of governmental affairs, agreed with Watkins and mentioned how he had recently heard about a client in a “plains state” that is both the finance director for a school district and the district’s bus driver.

The panelists offered several solutions to such problems, including having states take more responsibility for checking in with issuers about their continuing disclosure obligations. Louisiana already requires that auditors ask about compliance when they evaluate issuers. Most panelists also urged issuers to create and follow written policies and procedures to both keep consistency and prevent disclosure from deteriorating if an especially knowledgeable person leaves.

Washburn raised the issue of timeliness in disclosures, saying analysts have seen some issuers amend their continuing disclosure agreements to allow for more time to file after the end of the fiscal year. Watkins recommended the SEC try to address timeliness by creating a safe harbor for issuers to disclose unaudited interim information.

He said it is important to understand that governments are risk averse and if they violate securities laws after they pushed information out without waiting for an audit, they are not going to do it again and will take their time and delay disclosure to make sure everything is correct.

“Suffice it to say we don’t love that,” Washburn said.

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