

# **Bond Case Briefs**

*Municipal Finance Law Since 1971*

---

## **SEC Urges Municipal Issuers to Voluntarily Expand Disclosures: McGuireWoods**

For many years, the U.S. Securities and Exchange Commission (SEC) has advocated for increased transparency for municipal securities investors. Given the absence of a statutory scheme for municipal securities reporting, the SEC sought to protect investors through the regulation of broker-dealers, municipal securities dealers and municipal advisors; SEC interpretive guidance and industry guidelines; and enforcement of the antifraud provisions of the federal securities laws. Disclosure practices in municipal securities offerings, too, have largely developed in this way, with the SEC consistently advocating for greater and timelier disclosures of issuer and conduit borrower financial and operating information in the primary offering and continuing disclosure contexts.

The SEC has now reinforced its focus on enhanced municipal market disclosures in light of COVID-19 and the pandemic's potential effects on the financial status of state and local governments and special purpose entities. On May 4, 2020, SEC Chairman Jay Clayton and Office of Municipal Securities Director Rebecca Olsen released a public statement, "[The Importance of Disclosure for Our Municipal Markets](#)," requesting municipal issuers to provide robust, accurate and timely disclosures to market participants. In their statement, Chairman Clayton and Director Olsen stressed the importance of high-quality marketplace disclosures and requested "municipal issuers to provide investors with as much information about their current financial and operating condition as reasonably practicable."

They further observed that, in today's markets, the typical practice of providing historic information in the form of an annual filing or similar disclosure may be insufficient for investors to make informed assessments of the municipal issuer's current and expected future financial information. As a result, Chairman Clayton and Director Olsen encouraged municipal issuers voluntarily to provide investors with detailed current and forward-looking information regarding the impact of COVID-19 on their financial and operating conditions. Recognizing legitimate concerns of liability with respect to voluntary disclosure, including the provision of forward-looking financial information not historically provided by issuers, they expected that the SEC would not second-guess good faith attempts to provide appropriately framed current or forward-looking information. We believe this recognition should provide some comfort to issuers particularly as the SEC recently reminded them (and obligated persons) of the application of the anti-fraud provisions to public statements reasonably expected to reach investors and the trading markets. (For details, see a Feb. 7, 2020, OMS Staff Legal Bulletin, "[Application of Antifraud Provisions to Public Statements of Issuers and Obligated Persons](#).")

Other regulators likewise continue to evaluate the impact of COVID-19 on the markets and investors and provide guidance and relief to assist the industry in tackling the many new challenges brought about by the virus. Regulators at the same time have maintained a strong focus on identifying illicit activities that target the financial markets and prey on investor fears. (For details on regulators' previous efforts, see McGuireWoods' updates on [April 28](#), [April 21](#), [April 15](#), [April 6](#), [March 26](#) and [March 17](#).)

In announcing the formation of the North American Securities Administrators Association (NASAA) Enforcement Task Force (discussed below), Christopher W. Gerold, NASAA President and Chief of the New Jersey Bureau of Securities noted that “fraudsters are ramping up as a result of this crisis” and that state regulators will aim to “proactively identify COVID-19-related threats to investors, including but not limited to fraudulent offerings, investment frauds, and unregistered regulated activities, within the jurisdiction of NASAA member states and provinces, and to disrupt, discourage and deter those activities.”

These concerns are in line with messages from regulators as early as Feb. 4, 2020, when SEC issued its investor alert regarding COVID-19-related scams. On March 26, 2020, the Financial Industry Regulatory Authority (FINRA) issued a similar alert and, on March 30, 2020, NASAA issued an investor fraud alert. Finally, on May 4, 2020, the Financial Action Task Force — the international money laundering and terrorist financing watchdog — published a report highlighting fraud-related risks companies are facing in light of COVID-19, including the proliferation of investment scams, bank fraud targeting financial and account information, and cybercrime. The report advocated for increasing cooperation with regulators abroad and with the private sector.

## **U.S. SECURITIES AND EXCHANGE COMMISSION (SEC)**

### **Chairman Jay Clayton and Office of Municipal Securities Director Rebecca Olsen’s [Statement](#) on the Importance of Disclosure for Municipal Markets**

As described above, Chairman Clayton and Director Olsen are encouraging municipal issuers voluntarily to provide investors with as much current issuer- and security-specific information as practicable, as well as forward-looking investor-oriented disclosures discussing the anticipated effects of COVID-19 on their financial and operating conditions. As examples, they suggested the following kinds of disclosures that they believe would be helpful to investors:

- **Information Regarding the Impact of COVID-19 on Operations and Financial Condition.** Disclosures should reflect the issuer’s assessment of this state of affairs and outlook, and issuers should provide investors with information such as current operational and financial status including decreases in revenues and delays in collection of revenues; how their COVID-19 response has impacted their operational and financial condition, included unbudgeted costs; and anticipated changes in operational and financial condition as efforts to fight COVID-19 evolve.
- **Information Regarding Sources of Liquidity.** A description of cash on hand, access to reserves or other funds, access to liquidity facilities, and whether current liquidity is expected to be adequate to fund essential services and make timely debt service payments. If not otherwise disclosed, the issuer should describe the material terms of any liquidity facility the issuer has used or expects it may use.
- **Information Regarding Availability of Federal, State and Local Aid.** A description of available federal, state or local aid the issuer has sought or is planning to seek and the anticipated timing of such aid. If the issuer has obtained such aid, include information related to the nature, amount and other material terms of the aid if it materially affects or reasonably likely will materially affect its operational or financial condition.
- **Governmental Reports.** Municipal issuers should consider making available to investors reports prepared by municipal issuers for governance purposes that could provide insight into local, regional and sector-specific strategies to fight and recover from COVID-19. Chairman Clayton and Director Olsen stated that they did not expect the SEC to second-guess good faith attempts to provide the foregoing current and forward-looking disclosures. They believed that a municipal issuer’s approach to forward-looking statements should be informed by the judicially developed “bespeaks caution” doctrine (generally, that economic projections, estimates of future performance and similar forward-looking statements in a disclosure document are not actionable when

meaningful cautionary language elsewhere in the document adequately discloses the risks involved). Accompanying disclosures with meaningful cautionary language would help to reduce potential legal risks. However, they cautioned that it was extremely important to maintain confidentiality of information related to the financial impact of COVID-19 on municipal issuers, including, among other things, the pursuit of funding and support from governmental authorities and private parties, until that information is disclosed, and where it is disclosed, it should be disclosed broadly.

Finally, Chairman Clayton and Director Olsen encouraged financial professionals to discuss the importance of issuer-specific and security-specific disclosures with their investors who buy, sell and hold municipal securities, including in particular when providing recommendations and investment advice to Main Street investors.

Please refer to McGuireWoods' [April 17 legal alert](#) regarding the similar statement by Chairman Clayton and the SEC Division of Corporate Finance with respect to corporate issuers.

### **Updates to SEC Investment Management Staff FAQs**

On April 27, 2020, the Staff of the SEC Division of Investment Management updated its [COVID-19 Response FAQs](#). Among other things, the Staff addressed advisers that receive Paycheck Protection Program (PPP) Loans.

- The Staff said advisers should disclose to their clients the nature of assistance they received under the program if the circumstances leading the firm to seek a PPP loan or assistance “constitute material facts relating to your advisory relationship with clients.”
- The Staff specifically noted that inability of the adviser to pay its advisory employees’ salaries would be a material fact that must be disclosed.
- *Notably, this guidance from the SEC diverges somewhat from the stance FINRA has taken in its FAQs*, where FINRA has advised that, to the extent consistent with the terms of the PPP loan, forgiveness of the loan would be consistent with the loan’s original terms, and therefore would not constitute a “compromise with creditors” for purposes of Form U4 disclosure. (See April 15 update.)

### **FINANCIAL INDUSTRY REGULATORY AUTHORITY (FINRA)**

On April 28, 2020, FINRA released Episode 58 of its Unscripted Podcast, “[Market Structure & COVID-19: Handling Increased Volatility and Volumes](#).”

- In Episode 58, FINRA Executive Vice President of Market Regulation Tom Gira emphasized that the markets have generally held up very well during this period of extraordinary volatility. Gira provided a summary of the various market indicators during the COVID-19 pandemic and put them in historical context.
- First, circuit breakers had been utilized only once prior to the COVID-19 pandemic to temporarily halt trading on an exchange. Notably, between March 9 and 18 alone, the circuit breakers were employed four times.
- The CBOE VIX index (commonly known as the fear index) hit a record high of 83 on March 16. Additionally, the Limit Up/Limit Down has been triggered over one hundred times more than usual during the past several weeks, including a peak of 1,475 activated on March 18.
- Finally, short sale circuit breakers are activated on a stock-by-stock basis and when activated, short sales have to be executed in a stabilizing way. In the past, about 250 stocks were subject to the short sale breakers at any given time. But at various points throughout March, about 6,000 stocks were subject to it.

- Despite the extreme numbers for the market volatility moderators, FINRA is, overall, very pleased with how the markets have done and commended market intermediaries for their role in maintaining the markets.
- Given the increase in volume across markets and volatility generally, Gira indicated that FINRA will be actively prioritizing and escalating issues, as it wants to focus on issues that are creating more risk to the market and to investors.

## **STATE REGULATORS**

On April 28, 2020, NASAA [announced](#) the formation of the COVID-19 Enforcement Task Force, consisting of state and provincial securities regulators, to identify and stop potential threats to investors stemming from the COVID-19 pandemic. NASAA has identified as many as 200,000 coronavirus-related domains as of April 20, 2020, and the task force will be using online investigative techniques to identify additional websites, as well as social media posts that may be offering or promoting fraudulent offerings, investment frauds and unregistered regulated activities. Individual jurisdictions working as part of the task force will be responsible for taking regulatory action to address identified threats.

by E. Andrew Southerling, Cheryl L. Haas, Emily P. Gordy, Aline McCullough, Nicole S. Giffin, Joy D. Llaguno, Steven W. Peretz, Piper A. Waldron and Patrick A. Wallace

May 7 2020

**McGuireWoods LLP**