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Why There's Rising Interest in Giving More Updates to Bondholders.

Investors and others would like to see more timely information about developments with municipal borrowers' finances. "Voluntary disclosure" can help, experts say.

When state and local governments borrow through the municipal bond market to pay for road construction, waterworks upgrades or other projects, they take on obligations to report information about their finances to investors until the debt is paid off.

But issuers often don't release annual financial statements they're required to disclose until well after their fiscal year ends, making it hard to get an up to date picture about what's happening with their finances. This gap between budget cycles and these disclosure filings can stretch six or even nine months and some investors and others think the delay is too long.

Beyond the annual financial reports, under Securities and Exchange Commission rules, borrowers also have to publicly file ongoing notices about certain events, like delinquent payments, unscheduled draws on debt service reserves, or credit ratings changes.

In recent years, there's been growing interest in what's known as "voluntary disclosure," where state and local governments proactively release information related to their finances and relevant for investors, even though they are under no obligation to do so.

"Voluntary disclosure is taking it a step further and truly is what it sounds like. It's voluntary," said David Erdman, Wisconsin's capital finance director, during a Government Finance Officers Association conference taking place online through next week.

Erdman pointed out that after a state or local government finishes issuing bonds and the proceeds are in-hand and construction is underway on a project, it can feel as though the deal is done. But until the bonds are paid off, that's not really the case.

While the bonds are still outstanding, investors might be looking to assess the value of the debt, or to sell it on the "secondary market." But infrequent financial disclosures by governments mean the official information they have to make decisions can be incomplete or scarce.

Erdman likens the situation here to someone trying to buy a used car, who can only find information about the vehicle that's a year or more old. "You wouldn't know what the current miles are, you wouldn't know if there's any recent accidents," he said.

"Same thing goes with a municipal bond," Erdman added, "more information needs to be out there and that's where voluntary information kicks in."

A good example of when disclosures to investors like this can make sense is the Covid-19 pandemic, which stirred historic uncertainty about state and local governments' finances, the expenses they were taking on to respond to the crisis, and how it was affecting revenues.

There are other situations as well. For instance, a cyberattack, or a natural disaster like a flood or hurricane, might be the kind of event that investors want more details about to have a better understanding of how it's affecting a bond issuer's finances.

GFOA points out that going beyond disclosure requirements can be a part of investor relations programs and is one measure that state and local bond issuers can take to promote efficiency in the municipal bond market and to improve how their debt sales are received.

"In today's municipal market there is a heightened focus on the quality and transparency of disclosure practices by issuers," GFOA notes.

Presenting information in context

Jacquelynne Jennings, a partner at the law firm Schiff Hardin LLP (emphasizing she was speaking for herself and not the company) said that the SEC has shown an interest in greater financial disclosures by municipal borrowers.

"They would like for municipalities to more mirror the corporate markets and provide information quarterly, which is not going to happen, but at least more frequently than annually," she said.

Erdman said he's concerned that if municipalities and others don't ramp up disclosure efforts, the SEC might push additional regulations on the muni market—possibly to a degree that some issuers might turn to bank loans rather than bonds to meet their capital needs.

That said, for governments that only sell bonds every few years, voluntary disclosures may not be worth the effort. "The state of Wisconsin is a large, frequent issuer and there's probably some investor relations benefit for us doing this," Erdman said.

But even for medium size issuers, who are issuing bonds on an annual basis, he added, providing voluntary information to the market on a regular basis can have benefits.

Also, voluntary disclosure doesn't have to just be for bad news. It can highlight notable developments that have to do with things like revenue growth or infusions of federal funds.

Another area where voluntary disclosure can make sense is around issues that have to do with environmental, social and governance, or ESG, criteria. GFOA describes these factors as areas that can affect a community's long-term sustainability. Examples include things like exposure to climate risks, demographic changes, or pension liabilities.

"ESG is all the rage right now in the market," said Timothy Ewell, chief assistant county administrator for Contra Costa County, California. "In California, wildfires are the thing now." He noted that a GFOA's committee is working to assemble best practices and templates that jurisdictions can use to disclose ESG information to the bond market.

Jennings discussed how if finance officials fall short sharing timely information with bond market participants, investors may look elsewhere to assess what's going on and that could mean turning to statements by politicians or press reports that don't give a full picture.

"A lot of times doing this voluntary disclosure is the best chance that you have," she said, "to present the facts in their proper context."

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JULY 15, 2021

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