



August 8, 2011

Commissioner Elisse B. Walter  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Room 10200  
Washington, DC 20549

Re: Municipal Securities Rulemaking Board's Recommendations for Update of 1994  
Interpretive Guidance

Dear Commissioner Walter:

The Municipal Securities Rulemaking Board ("MSRB" or "Board") understands that the Securities and Exchange Commission ("SEC" or "Commission") is in the process of updating its 1994 Interpretive Release on Municipal Securities Disclosure Obligations (the "1994 Interpretive Release").<sup>1</sup> The Board appreciates the invitation to provide input on this important topic.<sup>2</sup> The first part of our letter provides recommendations on actions the Commission might take to improve both primary market disclosure and continuing disclosure in the secondary market. The second part of our letter describes efforts undertaken by the MSRB to address many of the issues raised by the 1994 Interpretive Release, as well as additional ways in which the MSRB might contribute over the next few years to improving the quality, timeliness and content of disclosure.

I. Recommended Commission Action

A. Amendment of Rule 15c2-12 to Require Official Statements for Primary Offerings of VRDOs

Notwithstanding the significant changes made to Rule 15c2-12 in 2010 (the "2010 Release"),<sup>3</sup> underwriters are not yet required to contract with an issuer to obtain an official

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<sup>1</sup> Release No. 33-7049 (March 9, 1994).

<sup>2</sup> The MSRB submitted comments on the 1994 Interpretive Release on August 3, 1994 (*see* letter to Jonathan G. Katz from David C. Clapp, then Chair of the MSRB).

<sup>3</sup> Release No. 34-62184A (May 26, 2010).

statement for most primary offerings of variable rate demand obligations (“VRDOs” or “demand securities”) because of the exemption from the official statement requirement found in Rule 15c2-12(d)(5). The MSRB recommends that the Commission eliminate the exemption for VRDOs from the official statement requirements of Rule 15c2-12(b) (1) - (4). Official statements would then be required for all primary offerings of VRDOs. As described below, the MSRB requests that, along with elimination of the VRDO exemption, the Commission provide additional clarity on what types of VRDO remarketings are primary offerings.

Other than uncertainty about what types of remarketings might be primary offerings and trigger the requirement for an underwriter to review an official statement, the MSRB does not know of any justification to treat VRDOs differently from fixed rate municipal securities. We support the Commission’s recent amendments to Rule 15c2-12, which apply the continuing disclosure requirements of Rule 15c2-12 to demand securities, and respectfully suggest that the same considerations that were cited by the Commission when it decided to amend Rule 15c2-12 in 2010 to require continuing disclosure with respect to VRDOs also support the amendment we propose.<sup>4</sup> The amendment the MSRB supports is also necessary to level the playing field by eliminating inconsistent behavior in the market caused by injudicious reliance by some on the VRDO official statement exemption, which we believe has the potential to cause harm to those investors that purchase VRDOs without the benefit of a disclosure document. We do not believe that the requirement to produce an official statement will disrupt the municipal marketplace since, at this point in the evolution of this product, most issuers appreciate the benefit of disclosure and prepare and distribute official statements for primary offerings of VRDOs. Furthermore, requiring underwriters to review official statements for VRDOs will encourage consistency in the content of such official statements and give more meaning to the Commission’s 2010 elimination of the VRDO exemption from continuing disclosure.

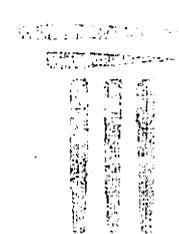
B. Additional Guidance on Primary Offerings of VRDOs

The MSRB recommends that, together with the elimination of the VRDO official statement exemption described above, the Commission provide additional guidance on when remarketings of VRDOs are primary offerings.<sup>5</sup> MSRB staff frequently receives questions from dealers (often acting as remarketing agents) on whether particular remarketings are primary offerings. The callers are seeking to determine whether, in the case where a disclosure document has been prepared, they should post it to the section of the MSRB’s Electronic Municipal Market Access (EMMA) system reserved for disclosure for primary offerings pursuant to MSRB Rule

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<sup>4</sup> “As the size, volatility, and complexity of the VRDO market and the number of investors have grown, so have the risks associated with less complete disclosure.” 2010 Release; Federal Register Vol. 75, No. 111 (Thursday, June 10, 2010) at page 33102.

<sup>5</sup> See examples provided in Rule 15c2-12(f) (7).





liquidity facility might not be available to pay debt service (including bankruptcy and other default) without providing disclosure on the financial ability of the underlying obligor to pay debt service in that event.

D. Key Disclosures

The MSRB supports a renewed emphasis on certain key disclosures. Among the disclosures that the Board considers key are: (i) risks, (ii) conflicts of interest of various transaction participants, and (iii) standardization of certain disclosures.

1. Risks Disclosure

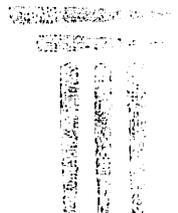
The MSRB shares the Commission's view that the terms and risks of securities must be clearly disclosed. In addition to our recommendations described under the heading "Disclosure Related to the Underlying Obligor," the Board recommends that the Commission consider elaborating on the importance of disclosure of risk factors in many primary offerings, although the Board recognizes that not all financings require a risk factors section. In particular, the Commission might address the merits of disclosure of market risks, credit and liquidity risks, legal risks (including those posed by the lack of disclosure of so-called "most favored nations" clauses, in the case of VRDOs), risk mitigation strategies, and the various risks associated with new products. We suggest that this disclosure is most prominent and readily accessible to investors (particularly retail investors) if it is found in a discrete section of the official statement called "Risk Factors," rather than being scattered throughout the official statement. The MSRB believes that the placement of this disclosure is particularly important for lower-rated and non-rated securities.

2. Conflicts Disclosure

The MSRB believes that enforcement actions over the last several years have highlighted the need for more guidance from the Commission on disclosures of conflicts, particularly concerning disclosures of payments made and received by transaction participants, including those made by third parties, such as GIC brokers and swap providers, that might give rise to conflicts of interests. Shedding light on the conflicts experienced by many transaction participants, which diminish investor confidence in the municipal marketplace, will hopefully discourage transaction participants from engaging in such conflicts or persuade them to act in a manner that safeguards against the potential adverse consequences of such conflicts.

3. Standardization of Certain Disclosures

Many investors have told the MSRB that one of the factors that significantly impedes their ability to compare bond issues for possible investment is the lack of standardized and detailed disclosure of the use of bond proceeds and other sources of funds. They have also expressed the desire for standardization of disclosure concerning the name of the issuer, the



name of any other obligor, the source of payment of debt service, and the sector (e.g., hospital, public power).<sup>7</sup>

E. Amendment of Rule 15c2-12 to Promote Compliance with Certain Continuing Disclosure Agreement Undertakings

Rule 15c2-12 has played a transformative role in facilitating the delivery by issuers and other obligated persons of continuing disclosure documents in the secondary market. EMMA has become the primary source for free access to these materials and the benefits accrue to all municipal market participants, including retail investors. A Continuing Disclosure Agreement (“CDA”) has become a standard closing document and the specifics of the undertakings are made known to prospective investors in the primary market, as well as investors that buy and sell in the secondary market, either because the undertakings are summarized in an official statement or, because a form of CDA is included in an appendix to the official statement. In addition to the issuer’s commitment to deliver the material event notices as prescribed in Rule 15c2-12, CDAs define the type of financial information that will be made available to investors via EMMA on an annual basis and, if not included in the annual financial information, require the submission to EMMA of audited financial statements, as well. The entity making the undertaking also indicates the due date for the delivery of such financial information to EMMA.

Many issuers and obligated persons have complied (or substantially complied) with the CDA undertakings that were disclosed in the official statement, particularly if they access the municipal securities market frequently. However, for those that have not, there is no easy means by which to enforce compliance short of a suit for specific performance and there seem to be no significant regulatory repercussions for non-compliance. Rule 15c2-12 does not impose penalties for non-compliance and therefore there is limited accountability for those issuers or obligated persons that do not furnish the information. Some callers to the MSRB have expressed frustration with the apparent unwillingness of some issuers or obligated persons to post audited financial statements within a reasonable time after the due date has elapsed or to acknowledge responsibility to do so. Other callers who are themselves bondholders are dismayed at the prospect that the MSRB has no authority to seek redress on their behalf even if they are third-party beneficiaries under the express provisions of the related CDA.<sup>8</sup> The Board recommends that the Commission consider issuing more interpretive guidance in this area and amending Rule 15c2-12, as necessary to impose consequences for non-compliance with continuing disclosure undertakings.

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<sup>7</sup> Such standardization should also address the concern expressed by some issuers that the repayment obligations of borrowers in certain conduit deals may not be adequately distinguished from the limited liability of governmental issuers.

<sup>8</sup> Rule 15c2-12(b) (5) (i) requires that the undertaking be “in a written agreement or contract for the benefit of holders of such securities.”



The Board understands that in some cases, non-compliance may result from circumstances beyond the control of the issuer or obligated person such as a natural disaster or other difficulty that has significantly compromised the ability to access all documents required to produce audited financial statements. It is equally plausible that in other cases non-compliance may result from a conscious decision to suppress unfavorable financial results. Any solution proffered should balance the legitimate needs and real world concerns of issuers and obligated persons with the needs of the investors that require financial information so they can make informed investment decisions.

In the case of issuers and obligated persons that exhibit a disregard for their CDA undertakings, we suggest that the Commission require much more robust disclosures in their official statements about their previous breaches of their CDAs. Of course, as is currently the case, underwriters should be required to have formed a reasonable belief that such issuers and obligated persons will, in fact, satisfy their CDA undertakings in the future in order to be able to underwrite their municipal securities. Underwriters could benefit from the Commission's guidance as to what steps an issuer might be required to take in order for the underwriter to establish such a reasonable belief. For example, the Commission might provide that establishing such a reasonable belief would appear difficult absent some real evidence of intent to comply (e.g., the adoption of policies and procedures concerning required submissions and retention of a dissemination agent that is charged with reminding issuers and obligated persons of their required filings).

Another possible way to emphasize the importance of compliance with CDA undertakings would be to require that CDAs include enforceable remedial steps to ensure that future disclosures are made appropriately, such as the adoption of specific procedures, granting investors direct enforcement rights (for damages as well as specific performance), engagement of professionals to assist in compliance obligations,<sup>9</sup> or other concrete and demonstrable actions designed to encourage compliance without initiation of a law suit.

## II. MSRB Disclosure Achievements and Initiatives

The MSRB has taken major steps to address many of the concerns raised by the Commission in the 1994 Interpretive Release. Our disclosure achievements and initiatives are summarized below.

### A. Conflicts of Interest and Other Relationships or Practices

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<sup>9</sup> Some may conclude that it would be advisable to contract with the indenture trustee, a designated dissemination agent or financial advisor to assist them in fulfilling these responsibilities in a timely fashion.



In the 1994 Interpretive Release, the Commission said that primary market disclosure could be improved by disclosure of financial and business relationships, arrangements, including political contributions, or practices. It said that failure to disclose material information concerning such relationships, arrangements or practices might render misleading those statements in the official statement that relate to use of proceeds, underwriters' compensation, and other expenses of the offering.

The MSRB has adopted major rules that promote the disclosure of conflicts, most importantly Rule G-37 (on political contributions and prohibitions on municipal securities business). Rule G-37 was adopted by the MSRB in 1994 due to concerns about the opportunity for abuses and the problems associated with political contributions by dealers in connection with the award of municipal securities business, known as "pay to play." Since its adoption, Rule G-37 has played a major role in eliminating potential conflicts of interest for issuers, or at the very least the appearance of a conflict, when dealers made contributions to officials responsible for, or capable of influencing the outcome of, the award of municipal securities business and then were awarded business by issuers associated with such officials. Dealers are required to make quarterly filings to the MSRB that list non-*de minimis* contributions, as well as municipal securities business engaged in during that quarter. Those disclosures are publicly available on the MSRB's website. The MSRB has recently proposed Rule G-42 (on political contributions and prohibitions on municipal advisory business and certain solicitations), which would extend similar pay to play rules to municipal advisors.<sup>10</sup>

Recent amendments to Rule G-23 prohibit dealers from serving as both financial advisor to an issuer and underwriter on the same issue of municipal securities. A companion interpretive notice requires dealers that act as underwriters to provide written disclosures to issuers about the arm's-length nature of their relationship with the issuer and requires them to state that they have financial and other interests that differ from those of the issuer.<sup>11</sup>

Other MSRB rules require dealers to disclose conflicts to investors. For example, Rule G-32 requires the disclosure to investors that the underwriter is being compensated by the issuer and the amount of such compensation. MSRB Rule G-22 requires that a dealer that has a control relationship with respect to an issue of municipal securities (*e.g.*, an official of an investment bank that is underwriting an issue and also controls the board of the issuer) must disclose that relationship to investors.

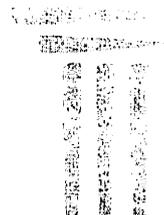
The MSRB has also proposed Rule G-36 (on fiduciary duty of municipal advisors), as well as a companion interpretive notice.<sup>12</sup> Proposed Rule G-36 would require all municipal advisors (those that are dealers and those that are not) to disclose any conflicts that might impair

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<sup>10</sup> See MSRB Notice 2011-04 (January 14, 2011).

<sup>11</sup> See MSRB Notice 2011-29 (May 31, 2011).

<sup>12</sup> See MSRB Notice 2011-14 (February 14, 2011).





MSRB has required underwriters to report for display on EMMA information about whether the issuer or obligated person has undertaken to provide continuing disclosure documents under Rule 15c2-12, the identity of any obligated persons other than the issuer, and the dates by which issuers or obligated persons have agreed to provide annual financial and operating data.

In 2009, the MSRB implemented its Short-term Obligation Rate Transparency (“SHORT”) System, which provides for market-wide collection of current interest rates and key information for municipal Auction Rate Securities (ARS) and VRDOs. On May 16, 2011, the MSRB increased the information collected by the SHORT System by adding information about orders submitted to an ARS auction, additional data for VRDOs, including information about current holders, and added documents detailing ARS auction procedures as well as liquidity facilities for VRDOs (such as letter of credit agreements, standby bond purchase agreements, and any documents establishing an obligation to provide a liquidity facility). All information and documents collected by the SHORT System are available, for free, on the EMMA web site.

E. Delivery of Official Statements

The MSRB’s Rule G-32 provides for free public access to all official statements. Underwriters must provide information to their customers during the primary offering disclosure period showing them how to find the official statement on EMMA for the bonds they have purchased. Since this requirement took effect in June, 2009, investors have had access to official statements in a more timely manner than in the past when such official statements were mailed to them.

On May 23, 2011, the MSRB increased the ability of issuers and obligated persons to submit information and documents to EMMA on a voluntary basis. Issuers now may voluntarily submit preliminary official statements and other related pre-sale documents, such as notices of sale or advertisements announcing an upcoming new issue. They may also submit official statements and advance refunding documents. As noted above, issuers and obligated persons also may submit information related to the preparation and timing of submission of audited financial information and/or annual financial information and hyperlinks to other disclosure information on the issuer or obligated person’s website.

F. Possible Enhancements to EMMA and Other MSRB Information Systems

The MSRB regularly evaluates EMMA’s use and effectiveness, as well as the evolving and on-going needs of stakeholders in the municipal marketplace, in order to sustain EMMA’s relevance to the municipal finance industry. MSRB will continue to make refinements to EMMA in support of enhanced disclosure. More broadly, the MSRB is now engaged in the development of a five-year plan for improvements to all of its information systems. We will be seeking input from market participants and from regulators on the development of the plan and welcome the Commission’s ideas.



G. Other MSRB Disclosure Initiatives

Each year, the MSRB invites key municipal market participants and policymakers to participate in a roundtable discussion of issues concerning disclosure. The Roundtable that took place in January 2010 was a catalyst for discussions about the types of financial disclosures that issuers already prepare that could supplement the annual financial disclosures required by Rule 15c2-12, on a voluntary basis.<sup>16</sup> In January 2011, the MSRB hosted a Roundtable that focused on issues related to concerns regarding unfunded pension liabilities of state and local governments and disclosure obligations under federal securities law regarding state and local pension fund liabilities and the related SEC settlement with the State of New Jersey. It was followed in June by another discussion of public pension funds and a session that focused on ideas for improving continuing disclosure compliance.

We appreciate this opportunity to provide input to the Commission on this important topic. We believe that our rulemaking has had a positive impact on the municipal finance industry and has made significant contributions to improvements in the quality, timeliness and content of disclosure to investors. We look forward to working with you and the other members of the Commission as you proceed with municipal market disclosure reform. If you or the Commission's staff members have any questions, or if we can provide additional information, please feel free to call me or the Board's staff.

Very truly yours,



Michael G. Bartolotta  
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<sup>16</sup> See, e.g., item 7 in the Government Finance Officers Association's Best Practice on "Understanding Your Continuing Disclosure Responsibilities (2010)."



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