Securities and Exchange Commission Field Hearing

Municipal Securities Disclosure
September 21, 2010

Good afternoon, Commissioner Walters and colleagues, my name is James McIntire. I am the Treasurer for the State of Washington. I want to thank you for this opportunity to share with you my comments regarding the Disclosure of Significant Liabilities.

I would like to divide my comments into three segments: (1) a brief description of our disclosure activities in the State of Washington, which I offer in my position as State Treasurer; (2) a brief summary of the adopted policy positions of the National Association of State Treasurers (NAST), which I offer as the Western Regional Vice President of NAST; and (3) my personal suggestions about moving forward on the SEC's disclosure concerns regarding municipal securities.

Municipal Securities Disclosure in the State of Washington

Washington State has been a national leader in municipal securities disclosure practices – we have deliberately tried to distinguish ourselves through timely and accurate financial reporting.

- Washington is a frequent issuer in the financial markets – we have been in the market 16 times over the past 21 months with a combination of tax-exempt, taxable and Build America general obligation bonds, and smaller issues of certificates of participation.

- The frequency of our issues has increased over the past several years due to more fragile financial markets, the need to fund transportation projects and with opportunities for significant refundings.

- Washington is committed to transparency in its financial affairs to protect investors and to keep taxpayers informed of essential infrastructure projects and the uses of their tax dollars.

- In addition to providing timely and accurate financial reporting, the state offers detailed reports to investors including:

    - Quarterly economic and revenue forecasts prepared by an independent economist and overseen by a bi-partisan commission with legislative and executive members. These reports are in many ways the public sector equivalent of quarterly corporate statements.

    - We provide monthly economic and revenue updates on the state's revenue collections and the state of the economy.

- The Office of the State Actuary prepares annual pension reporting with assets and liability valuations prepared according to defined actuarial assumptions and methodologies.

- Recently the Actuary supplemented these standard pension valuations with an alternative Risk Assessment study, using stochastic components to quantify the likelihood and magnitude of future outcomes for the pension system.

- Providing timely and comprehensive disclosure is a major undertaking for my office. As a state issuer, we interact with other agencies such as the Governor's budget office, the Department of Transportation, the State Actuary, the State Auditor, and the Attorney General's office to ensure our documents accurately reflect the most current available financial information. This entails the coordination of information from agencies under 5 separately elected executive officials, plus the Legislature.

- We are working to deliver the data to the market more quickly: our goal is to release audited financials 120 days after the close of the fiscal year – the MSRB target – as soon as possible.

  - This year we expect to meet the MSRB interim goal of 150-days and identify the measures needed to cut to 120 days. This is a real challenge, given that Washington has 9 separately elected executive officials.

- The state does not mandate disclosure practices for local issuers, although it does provide a statutory framework for funding purpose and approval by local governing bodies and/or voters. Debt levels are governed largely by revenue related limitations, some are statutory and others constitutional.

- We believe in setting a good example for localities throughout the state when it comes to producing thorough and timely disclosure, and recently have worked with the State Superintendent of Public Instruction to improve guidance to local school districts in the use of financial advisors for bond sales.

- We are committed to meeting GASB requirements. We have consistently achieved the Certificate of Achievement in Financial Reporting in association with our CAFR. We believe establishing standards for accounting and reporting is to the benefit of both the issuer community and the investor community.

NAST Policy Positions:

As the Western Regional Vice President of the National Association of State Treasurers, I would like to offer the following summary of the Association's official policy positions regarding securities disclosure:

- NAST *supported* the creation of EMMA and *supports* expanding the usefulness of EMMA as a central repository.

- NAST *encourages* and *promotes* frequent and timely disclosure of information to the municipal securities market. To this end, NAST is prepared to work with other organizations and associations to better define what financial, operating and other information is relevant and useful to the market recognizing the significant differences of issuers by size, sector and frequency of issuance.

- NAST *supports* the regulation of all financial intermediaries in the municipal securities market.

- NAST *supports* an independent and equitably funded GASB. NAST maintains that funding for GASB should come primarily from state and local governments. NAST *opposes* federal funding or oversight of GASB as well as any direct federal mandates on issuers of municipal securities to comply with GASB accounting standards.

- NAST *opposes* preemption of state and local finance authority and state oversight of the debt issuance process through revision or repeal of the Tower Amendment or legislation that would subject state and local government issuers to federal disclosure laws and registration of municipal securities with the SEC.

- Finally, NAST *encourages* the rating agencies to carry out their commitment to utilize a single rating scale for all debt instruments such that a rating applied to a municipal bond indicates the same credit risk as that same rating applied to corporate bonds, while also recognizing the need for relative ratings amongst municipal issuers. Ratings should measure the ability of an issuer to meet its obligation to investors as promised in the bond documents, such obligation primarily being to pay debt service on time and in full.

Moving Forward on Municipal Securities Disclosure

I believe comprehensive and timely disclosure is of increasing importance in the current environment due to two primary factors:

- First, retail investors are becoming an increasing percentage of municipal bond buyers and relative to institutional investors, they lack access to credit and research materials;
    - Retail investors are increasingly drawn to municipal bonds due to their historical (and perceived) safety;
    - This is expected to continue as a greater percentage of the population nears retirement age;
- Second, the mixed performance of rating agencies and the homogenization of ratings offers a muddled picture for retail investors;
    - With the recalibration and homogenization of ratings, it is increasingly difficult for investors to compare municipal credits relative to one another. A much broader group of states now has the same rating as the State of Washington;
    - It is also difficult for investors to compare corporate credits to municipal credits because despite recalibration, because the scales are not the same with respect to measuring the ultimate risk of default or recovery – municipal risk remains overstated relative to corporate risk.

According to the Moody's Default Study, released in February 2010, from 1970 through 2009, there have been only 54 defaults in the municipal sector, 78% of those occurred in healthcare, housing finance. Only three were general obligation bonds.

- The average 5-year cumulative default rate for *investment grade* municipal debt is 0.03% compared to 0.97% for investment grade corporate issuers.
- Taking that a step further, the average 10-year cumulative default rate for a *triple-A* corporate bond is 0.50% whereas the cumulative default rate for an *A-rated* municipal bond (over the same time period) is 0.03%. On average, that means that a retail buyer buying a triple-A corporate bond is taking a risk more than fifteen times than if they had bought an A-rated municipal bond.
- Recovery for municipal defaults is also much higher than that of senior unsecured bonds of corporate issuers. The average thirty day post-default price for a defaulted municipal bond is 60 cents on the dollar versus 37.5 cents for its corporate equivalent.

Even though Washington is able to be in the forefront of public disclosure, not all state and local governments are in the position to achieve some of the more aggressive timetables envisioned by the MSRB. In difficult budget periods, it is even more important to realize that imposing new regulatory requirements on municipal issuers

will come at a significant monetary cost at a time when issuers are working to contain costs to protect their financial health, to the benefit of both taxpayers and bondholders.

I know that it is not the focus of this hearing, but I must emphasize that a repeal of the Tower Amendment and imposition of a set of uniform federal regulations on the issuance of municipal securities could have a devastating impact on state and local budgets at a time when we can least afford it. It could also have a dramatic impact on the access to the market by small municipalities, and could simply cause numerous infrastructure projects to grind to a halt before the statutory and constitutional framework around state and local accounting and debt issuance could be transformed.

And what would be the practical benefit for all of this activity? How many of the precious few defaults would be prevented? What marginal benefit would this produce for retail investors? How would you respond to the outrage of local governments across the country about the changes necessary, the added costs, and in many cases, lack of access to capital markets? Do you even have the resources to approve securities registrations from 50,000 issuers – only a few of which may have the capacity and economy of scale to maintain shelf registration materials.

These rhetorical questions point us in a much more practical direction. There may be significantly more value in using your new authority over the rating agencies to promote higher standards in their assessments, making them much more reflective of the actual risks they face in the municipal bond market. I believe that this approach would produce much greater marginal benefits

At the same time, many of us in the municipal issuer community will continue to strive for excellence in accounting standards and reporting, and continue to focus on optimizing the use of EMMA as a depository. We certainly hope to work with you and a reconstituted MSRB in doing so.

Thank you for this opportunity to comment. I look forward to your questions.