California Refuse Recycling Council

JOINT STATE OFFICE

September 2, 2009

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F. Street, NE
Washington, D.C. 20549-1090

RE: **File No. S7-15-09; Comments on SEC Release No. 34-60332**

Dear Ms. Murphy:

The California Refuse Recycling Council ("CRRC") respectfully submits the enclosed comments to the Securities and Exchange Commission ("SEC") related to SEC Release No. 34-60332, dated July 17, 2009, File No. S7-15-09. Our comments were prepared by some of the bond attorneys and financial service entities that work with our members.

By way of introduction, CRRC represents some 100 businesses engaged in waste collection, recycling and disposal in the State of California. The vast majority of our industry members are family owned, closely held companies with long records of service to municipalities in this state. They have been instrumental in helping California meet and exceed its goal of diverting for recycling and re-use more than 50% of solid waste materials that formerly went to landfills. Our industry is also been a leader in conversion of its fleets to clean burning fuels, with many of these fleets having already been converted to natural gas, "clean" diesel and other alternative fuels.

As our members strive to set new standards in reducing air pollution and greenhouse gas emissions and increasing recycling, access to low cost capital is ever more important as ultimately, the cost of these programs is borne by the citizens and businesses in each community and financing cost savings inure directly or indirectly to their benefit.

Although to my knowledge we have never submitted comments on proposed SEC regulations before, we are advised that the amendments to Rule 15c2-12 embodied in the Release cited above could have a negative impact on our members' ability to access a key source of this low cost capital, tax exempt debt. We therefore take this unusual step and hope that you will consider our comments and perspective before adopting any final changes.

If you have questions concerning the comments, please contact Executive Director Trish Roath at 916-444-2772 who will direct you to the appropriate person for a prompt answer. Thank you in advance for your consideration.

Sincerely,

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CRRC State President

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COMMENTS OF THE
CALIFORNIA REFUSE RECYCLING COUNCIL REGARDING
PROPOSED AMENDMENTS TO REG. Sec 240.15c2-12. (RULE 15c2-12)
MUNICIPAL SECURITIES DISCLOSURE

SEC Release No. 34-60332; File No. S7-15-09

The following comments are submitted on behalf of the California Refuse Recycling Council ("CRRC") to the Securities and Exchange Commission ("Commission") with respect to Release No. 34-60332; File No. S7-15-09 and proposed amendments to Rule 15c2-12 pursuant thereto. Our comments were prepared by an *ad hoc* group of bond attorneys and financial service entities that work with our members and the comments have been approved by the Board of Directors of CRRC.

The Release requested comments on the proposed amendments cited above relating to municipal securities disclosure. CRRC welcomes the opportunity to respond to the request for comment. While we support the SEC's efforts to improve disclosure for all types of securities, our focus will be solely on a specific proposed deletion of a subsection of Rule 15c2-12 which we believe is overbroad and is likely to cause unintended negative consequences for our members as they attempt to access low cost capital and pass those savings on to their ratepayers.

The Proposed Amendment: The amendments include the proposed deletion of the current subsection (d)(iii) which reads as follows (we have underlined the subsection proposed to be deleted):

> (d) *Exemptions.* (1) This section shall not apply to a primary offering of municipal securities in authorized denominations of $100,000 or more, if such securities…
>
> (iii) At the option of the holder thereof may be tendered to an issuer of such securities or its designated agent for redemption or purchase at par value or more at least as frequently as every nine months until maturity, earlier redemption, or purchase by an issuer or its designated agent.

Summary of Comments: The Commission's intent, to paraphrase the Federal Register comments accompanying the proposed rule changes, is to improve the availability of timely and important information regarding municipal securities so investors can make better investment decisions, effectively monitor and manage their investments and help protect themselves against fraud or misrepresentation. These are all laudable goals. However, we understand the Commission, before adopting any rule, is also required to consider whether the benefit of the rule outweighs any additional costs or other burdens imposed on those regulated. And, it must consider "whether the action would promote efficiency, competition and capital formation." Further, it prohibits the Commission from "adopting any rule that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Act." We believe the proposed deletion described above fails all of those tests as applied to our members.

The rule change and summary in the Federal Register focus primarily on three parties, the issuers, the broker-dealer/underwriters, and the MSRB. Our comments relate to the potential effect on "obligated persons" other than the Issuers and we believe too little consideration has been given to that effect, at least for a certain type of variable rate demand obligations ("VRDO's") used by our members. Whatever the merits of increasing disclosure for most such securities, we believe

the Commission has used far too broad an approach in the proposed deletion of VRDO's of very short tenor which may be put back to the issuer every seven days. We believe it will either impose significantly increased burdens and costs on our members and the citizens and businesses that they serve and/or will materially decrease competition among providers of solid waste and recycling services in California. We further believe that virtually no benefit will result from the rule change for the types of VRDO's used by our members and described below. We believe the changes will impose significantly higher costs and burdens on our members and that there will indeed by a negative impact on capital formation and competition. A discussion of the issues follows:

Structure of VRDO's Used by Our Members: Over the last fifteen years, most of our industry members have taken advantage of certain exemptions in the Internal Revenue Code which allow them to benefit from the issuance of tax exempt "private activity bonds" that have been used, among other things, for the construction of new materials recovery/recycling facilities and the purchase of new natural gas fueled vehicles and other assets which have helped the State of California and its municipalities to meet various clean air and recycling goals. These bonds were issued by the California Pollution Control Financing Authority ("CPCFA") and comprise 122 separate issues totaling $1.353 billion. (We did not attempt to separate out issues which benefited our members versus non-members but virtually all of the issues were for members.) We should note that neither any of these bonds nor any other letter of credit backed VRDO's issued by CPCFA has ever been in default (nor for that matter do we believe that any CPCFA bonds of any tenor backed by a letter of credit have defaulted in its approximately 35-year and multi-billion dollar issuance history).

Unlike the issuers and obligated persons to whom the proposed rule changes seem to be directed, our members benefiting from the bonds described are all privately held entities, almost all of which would not normally be able to access the tax exempt or indeed any other public debt markets. They do, however, have excellent credit with their banks and financial institutions. Those institutions issue letters of credit as "credit enhancement" for our members' bonds which serve two functions which significantly differentiate these bonds from many other types of VRDO's. First, the bonds are structured so that the letter of credit works in a "direct pay" method. That is, the bond trustee draws on the letter of credit rather than funds provided by the underlying borrower for all payments of interest and principal. As a result of that structure, the letter of credit also serves as an assurance to the bondholder of liquidity in the event the bondholder wishes to exercise its weekly put option. The latter, of course, assures the bondholder (short of bank default) that funds will always be available for purchase of their bonds by the remarketing agent. Further, CPCFA, as the primary issuer of these type bonds for our members in California, requires that the letter of credit bank have a credit rating of at least 'A-' or equivalent from one of the major rating agencies.

Given this structure, investors are provided information in the related disclosure document about the letter of credit bank and its rating at the time of bond issuance and are also directed where to find additional financial and other information about said bank. As a result, investors properly look to the credit of the financial institution and its rating and not to the credit of the underlying borrower in making decisions as to whether to purchase the securities. We believe the current exception is perfectly appropriate for this structure. This is evidenced by the fact that the underwriter for all the bonds referenced above for our members has informed us that it has *never* been asked by a potential bond purchaser for information on the underlying borrower.

We do not understand the benefits sought by imposing additional reporting requirements on obligated persons for this particular type of securities. The Commission seems to be concerned that holders of some VRDO's seem to be holding the securities for longer periods. We can

understand that there might be appropriate concern: a) If these bonds had no letter of credit or other credit enhancement and thus no liquidity feature; or, b) if the VRDO's featured a liquidity agreement which is not a direct pay letter of credit. In that case, the investor has some exposure to the credit of the borrower in that certain borrower financial events could result in the immediate termination of the liquidity agreement; or, c) if these were not seven day VRDO's but instead had a longer interest rate period (that even with credit enhancement are subject to the disclosure rules of Rule 15c2-12 in order to help protect the investor against early redemption and loss of the investor's expectations relating to the long term interest rate).

However, in the case of the particular VRDO's described, none of those concerns seem valid. This does not mean that protections given an ultimate investor are not proper. However, because of the nature of the direct pay letters of credit-backed VRDO's described, the letter of credit provider is and should be the focus of disclosure made to the bondholder, given the inherent additional protection of the bondholder resulting from that letter of credit. Having taken on that obligation, the letter of credit provider secures the underlying obligation of the borrower through financial and other covenants in its credit or "reimbursement" agreement. This is only proper since that bank or institution is ultimately responsible for paying back the bondholder, *notwithstanding any problems with the underlying borrower*.

Specific Anti-Competitive Issues:

- *Disclosure of Financial Material by Ultimate Borrowers Could be as Misleading as it Would be Informative:* Given that the obligation to pay principal and interest in a timely manner on the VRDO's falls on the letter of credit banks and not the ultimate borrower/obligated person, disclosure of financial information in an official statement or in continuing disclosure could mislead the investor by encouraging focus away from the financial health of the bank. A hypothetical case of an investor comparing two VRDO issues is illustrative of this point: The first is a VRDO without credit enhancement issued to benefit an investment grade, publicly traded environmental company with hundreds of millions in net income. The second is a letter of credit backed transaction where the ultimate borrower was very strong financially but only a fraction of the size of the national company. Despite the fact that the letter of credit bank securing the latter issue may be much stronger financially than the publicly traded environmental company, an investor might well choose the un-enhanced bonds of the environmental company based on a comparison between the financial statements contained in the respective official statements of the two underlying borrowers and not the bank versus the un-enhanced borrower comparison that one could argue should in fact have been made.

- *Disclosure of Financial Information by Ultimate Borrowers Would Negatively Impact Competition:* Disclosure of financial information implicit in the requirement for annual reports would be unacceptable to the great majority of our members in that it would materially impact their competitiveness. This is because most of our members serve one or two municipalities or limited geographic areas as opposed to the large, national and publicly traded companies which serve much of the nation. In fact, in most cases, the right to serve a community is often determined by a bid process where even an incumbent service provider often must compete against others to retain its contracts.

  While those public companies do report their financial results, they do not do so on a community by community or even state by state basis. As a result, there is an even playing field because neither the closely held entity nor the publicly traded company has any significant financial information on the other relevant to the limited service area in which they wish to compete. If, under the proposed rule change by the Commission, the smaller entities were required to provide such financial information, at the very least it would put

them at a significant disadvantage since the public entity would have access to otherwise proprietary financial information relevant to the local area and not vice versa. Even in areas such as commercial waste and recycling where long term contracts are not as common, such financial disclosure by the smaller competitor could be used in predatory pricing and other unfair competitive practices to the detriment of smaller competitors and indeed, competition itself.

Ultimately, that would either hurt competition in general by placing a large group of active smaller competitors at a disadvantage or would effectively force them to give up the benefits of tax exempt finance. Were the latter and more likely case to occur, there would be a similar negative effect on their ability to compete on price with their large competitors. Or, where the community wished to retain the smaller service provider for reasons not solely related to cost of service, the costs to their residential and commercial ratepayers would have to rise due to the loss of the ability of that service provider to obtain tax exempt interest rates on debt it would still need to obtain to finance necessary capital expenditures.

If one assumes an average of 1.5-2% difference between tax exempt and conventional interest rates for the fifteen year period for which we provided totals of these types of VRDO's in California described above, the potential annual loss to California ratepayers from non-public companies withdrawing from the tax exempt markets would have been between approximately $20 and $27 million. (We acknowledge that the difference in rates has been much less recently but the historical data and future results are likely to be consistent with the differences described.)

- *Financial Disclosure Will Not Assist in Predicting Early Redemptions:* We don't understand the benefits sought to be achieved by the rule changes for the types of VRDOs described but perhaps it is to provide timely notice of when a bondholder might get its bonds redeemed prior to maturity. Since VRDO's are sold and trade at par value, and as the Commission points out, the VRDO market is quite large thereby providing ample other purchase opportunities, the actual harm to the investor of an early redemption is unclear. But, if this is a goal, we would suggest that financial disclosure by obligated persons such as our members would not contribute to this goal. The reason is the same as cited above—that such disclosure can be as misleading as it is informative. Because the large companies do not report their financials on a state by state basis, much less a regional or community one, their financials will give little guidance as to their intentions in any given state or area. In fact, in California, in some cases, the publicly traded companies have lost contracts or otherwise withdrawn from a service area for various reasons. In some of those cases, bonds issued for assets used in the discontinued service were either redeemed or the obligations assumed by another entity and reissued with new letters of credit. Little to no information contained in the financial information provided by the public companies would assist a bondholder in determining the likelihood of such events.

Specific Additional Costs and Burdens:

The additional reporting burdens which would be imposed on these formerly exempt VRDO's of all types of events (some of which have been increased and the deadline for reporting shortened pursuant to other of the proposed amendments) and penalties for failure to so report would pose additional costs and administrative burdens on these small companies with no obvious benefit. Specific issues are raised below.

- *Financial Disclosure Will Impose Significant Additional Costs on Smaller Borrowers:* The VRDO's issued described above average less than $11 million per issue and the par amounts

of some transactions have been only a few million dollars. Due to the size of either the borrowers or the bond issues, the letter of credit bank does not require audited financial statements, instead being satisfied with accountant reviewed statements and knowing their customer. And, even for those companies which are of a size where audited statements are required, they are never required for all constituent entities making up these larger businesses' operations. The proposed rule change would seem to impose such an audit requirement. This could increase the costs to a small borrower by $30-40,000 annually and that is if it only operates through one corporate entity. Many of our members operate with a number of entities for many reasons including the need to separate operations in one city from a neighboring one due to differences in contracts and regulatory procedures. Were all such entities required to be audited, and/or consolidated audited statements prepared or prepared in detail not otherwise required for closely held entities, the annual cost burden could increase to the hundreds of thousands of dollars. Again, as a practical matter, this would result in a withdrawal from the tax exempt markets by these companies with the negative results described above.

- *Other Disclosure Requirements Would also Impose Significant Costs or Result in Negative Competitive Impacts:* We are not in a position at this point to analyze the exact cost or other impacts of the significant additional reporting requirements if the exemption from those requirements for VRDO's described herein is eliminated. However, many of our members do not have large staffs and in many cases, do not have financial professionals beyond a controller-level person. Assuming that such reporting would be meaningful to investors—which we do not believe is the case, as noted above—it would be difficult to impossible for such companies to comply with a ten day deadline and in fact, their letter of credit banks impose no such short deadline for many of the otherwise reportable events required by such banks.

  In one particular requirement, the anti-competitive effect would likely be significant. That is the requirement that any acquisition or merger be reported upon signing of an agreement therefor. In California and elsewhere, such agreements between closely held companies are often signed well before a public announcement. Often they are signed before the lender (and issuer of the letter of credit for any outstanding VRDO's) has approved although such lender approval is ultimately required. And, approval of any such arrangement is also generally required by the served municipalities and thereafter considerable time and money is spent in gathering information for presentation to those municipalities in order to gain such approval. Were the announcement required to be reported within ten days, a competitor could seek to disturb the arrangement which still would be contingent upon those approvals. This would make such acquisitions and mergers among privately held entities very difficult and in some cases impossible. Were that the case, smaller companies would likely forego the benefits of tax exempt finance with the negative effects cited above.

Conclusion

For the reasons set forth herein, we believe that the change to Rule 15c2-12 described above violates the Commission's own standards and those imposed by law as described in the introduction to this material. We hope, therefore, that either the proposed deletion will be withdrawn, or perhaps some compromise language can be drafted to continue a limited exception from disclosure for letter of credit backed VRDO's where the letter of credit is issued by a publicly traded financial institution and works in the "direct pay" manner described above.