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SEC Field Hearing

“Looking at Disclosures: Issuer and Investor Perspective”

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Good morning/afternoon. My name is Paul Nolan, and I am a Senior Municipal Analyst for Asset Preservation Advisors (APA), a municipal bond management firm in Atlanta with \$1.7 billion assets under management and that monitors some 3,000 municipal bond issuers for investors, mostly in the investment rating category. I am happy to have this opportunity to share with the Securities and Exchange Commission, issuers, and those in the audience my general thoughts and experiences with disclosure as a municipal bond credit analyst with some 14 years of experience. Prior to APA, I spent five years with McDonnell Investment Management, another asset management firm in Illinois, and I spent a little over five years at Moody’s Investors Service as a Credit Analyst in Chicago and New York. My sectors of coverage in the muni world include State and Local General Obligation debt, water/sewer, toll roads, hospitals, public and private higher education, community colleges, and other muni sectors. I have also worked in the government and not-for-profit sectors.

Today, I will discuss my perspectives on primary and secondary market disclosure. And while this may seem obvious, I think it needs to be stated up front: Consistent, timely, and accurate disclosure

throughout the life of the bonds needs to be improved, especially in the secondary market and in particular with regards to infrequent issuers. While disclosure from issuers has become better over the years through rule 15c2-12 and the establishment of EMMA, there is always room for improvement.

Disclosure documents are important to investors, the market, and of course firms such as APA. As a registered investment advisor, APA purchases municipal bonds on both the primary and secondary markets. APA focuses exclusively on tax-free and taxable municipal securities for high net worth investors. Our main objective for our clients is to preserve capital. Let me say it again: preserve client capital. This is accomplished through fundamental credit analysis.

Fundamental credit analysis is an objective examination of an issuer's willingness and *ability* to make debt service payments. These underlying credit fundamentals vary by sector, with hospital issuers having different credit fundamentals than those of a city or county. Yet, regardless of the sector, investors should have constant access to timely, accurate, and consistent information over the duration of the outstanding bonds. It is paramount that all interest parties have access to the necessary information, hopefully free of charge, so that one can develop objective opinions on the willingness *and ability* of these issuers to make timely debt service payments. This allows the aforementioned interested parties to compare credits from not only an underlying credit perspective but also from a relative value perspective. Across the rating spectrum and when comparing two issuers with the same rating, all are not equal with regards to their ability to make debt payments. As such, disclosure items are a necessity, particular in the secondary market where information is often outdated, incomplete or unavailable. There also needs to be more than just audited financial statements disclosed, with specific sector criteria also provided.

The bottom line: disclosure in the primary market, through information found in the Official Statement (or OS), has improved under Rule 15c2-12, the amendment to the rule, and with the establishment of

EMMA. Yet there could be additional items added on a more consistent basis. There also needs to be a more uniform, standard set of guidelines established for the type of information expected from issuers in an OS and in terms of what items they intend to disclose on an ongoing basis.

For example, I have found that one piece of information not found in an official statement on a consistent basis is up-to-date and/or more detailed information on recent financial performance upon issuance. If the issuer's audit year ends on June 30th and the issuer is coming to market with bonds in December of that same year, six months have passed since that last audit. The financial position of the issuing entity could have changed, either positively or negatively, during that time. It would be beneficial to have the updated information, in the form of quarterly or even semi-annual report, even if unaudited. It would also be helpful to have other relevant recent information, such as tax collection rates for a GO issuer or updated debt service coverage for a water sewer deal. Take a look at a health care or a CCRC OS as a model for primary disclosure, as these issuers more often than not provide quarterly financial performance numbers along with up-to-date utilization figures.

I do need to say this: Not all issuers are created equal when it comes to disclosure. Some issuers provide investors with copious amounts of data in which to analyze while others provide the bare minimum. In our view, a uniform, set standard on the exact type of information included in a OS is necessary as well as what additional items will be disclosed over the life of the bonds on EMMA.

Another issue, especially in the primary market for General Obligation debt, is limited input on disclosure documents and other key legal provisions that investors might like to see as added security, such as rate covenants, additional bonds tests, or reserve funds. It would be beneficial to the market if issuers and underwriters could be provided input on these key documents from investors before the deal is finalized.

As for the secondary market, I would say the following:

1. In general, the information disclosed to EMMA and the market as a whole is often incomplete and not what was promised in the OS disclosure statement.
2. It is not provided in a timely manner, often after the established deadline.
3. And in some cases is unavailable, as it was not submitted to EMMA.
4. We have also found a significant delay in the filing of material event notices.
5. There seems to be a lack of enforcement for non-compliance. We understand that in the OS the issuer is just following rule 15c2-12 (and the subsequent amendments), but what happens if the issuer fails to file the agreed upon disclosure documents in the prescribed amount of time? There seems to be no recourse for investors or issuer penalty for non-compliance of promised documents other issuance of a non-disclosure violation. The same cannot be said in the corporate world.

And in general, once again I would say that the health care sector is the model citizen for disclosure in the secondary market. Personally, I have found that this sector has done a distinctly better job at providing the market with up-to-date quarterly information on financial operations, utilization data, and other fundamental information, compared to other sectors.

I understand that those running a state or local government entity or not-for-profit have many things on their plate. So perhaps disclosure documents are not high on a long list of tasks that are in need of being performed. But I have found numerous examples of issuers providing complete and timely information on EMMA, most often in a statistical section in the back of a recent audit. I always believed that if one sector or issuer can do it, why can't all sectors and issuers provide the information? Maybe part of the problem is that we analysts have an obligation to further educate issuers on the benefits of timely and complete disclosure.

With some 50,000- 60,000 issuers and nearly \$3 trillion in debt outstanding, the municipal world needs to improve disclosure, especially in the secondary market. Investors can no longer rely on the few bond insurers left to make payments in the event of a default. They cannot rely on the rating agencies, which charge a fee for services, for timely and complete information on the surveillance of bonds for which they purchased. They must have access to the data themselves to bring greater transparency to the muni market.

This panel and others held in the past are a step in the right direction for improved disclosure. However, even with these panels, recommendations made by the National Federation of Municipal Analysts through various white papers on disclosure, recommendations from GFOA, and the improved ability for analysts and investors to access offering statements and other information on EMMA, investors can still sometimes be at a loss when researching a particular bond, especially from small issuers that do not issue bonds frequently. Compare this to the corporate world. Improvement in disclosure coupled with some sort of recourse for investors if an entity fails to disclose the agreed upon documents may provide a catalyst for issuers and underwriters to improve disclosure.

Thank you for listening, and I look forward to answering any questions.

Paul Nolan