



August 7, 1987

Mr. Andre Blum, Chairman  
Task Force on Municipal Disclosure  
Government Finance Officers Association  
1750 K Street, N. W.  
Washington, D.C. 20006

Re: GFOA Disclosure Guidelines for State and Local Government Securities

Dear Mr. Blum:

The Municipal Securities Rulemaking Board is pleased to comment on the exposure draft of the GFOA's Disclosure Guidelines for State and Local Government Securities (the "Guidelines"), including the proposed revisions to the Disclosure Guidelines for Offerings of Securities ("Official Statement Guidelines"), Procedural Statements in Connection with the Disclosure Guidelines ("Procedural Statements") and Guidelines for the Timely Provision of Information on a Continuing Basis ("Continuing Disclosure Guidelines"). Since the Guidelines first were published, municipal securities have become increasingly complex, particularly with regard to redemption features, and the market for municipal securities has become more sophisticated, exemplified by the development of active secondary market trading and a high volume of new issues being disseminated into the market. The Board applauds the excellent work of the Task Force on Municipal Disclosure in proposing revisions to the Guidelines that address these developments, particularly the expanded Procedural Statements and the Continuing Disclosure Guidelines. If followed by issuers, the revised Guidelines should improve the content of, and access to, issuer information about municipal securities for all market participants. The Board offers its services to assist the GFOA in publicizing the revisions to the Guidelines through educational efforts among dealers or other measures that may be appropriate. The Board also recommends the following revisions to the Guidelines to address several disclosure issues of special concern to the Board.

#### Official Statement Guidelines

As the GFOA is aware, since the Official Statement Guidelines first were published in 1975, issues of municipal securities have become increasingly complex. Often an issue can have numerous conditions under which interest rates may vary, securities may or must be put and/or

rolled over into other instruments and the securities may be called in-whole or in-part. Perhaps as a result of these developments official statements have become longer and more complicated, particularly in the areas of disclosure of call and put feature information. These documents are becoming so complex that investors may not be able to understand them.

The Introduction to the Official Statement Guidelines states that the information set forth in the official statement should be presented in a concise, understandable fashion. The GFOA should strengthen this language to emphasize that official statement disclosure is most effective when it is stated in terms that can be understood by the average investor. Moreover, the Board recommends that issuers be advised to pay particular attention that all information on each aspect of the securities, for example, all redemption features, is located in the same section of the official statement for accurate reference. Also, the GFOA should revise the penultimate paragraph of the Introduction, dealing with the availability of official statements, to include a statement that investors may obtain a copy of the official statement from the issuer, as well as from a repository, for the life of the issue.<sup>1</sup> The Board also recommends that this be stated on the cover page of the official statement.

Section I of the Official Statement Guidelines, on the Cover Page of the Official Statement, sets forth the information that should appear on the cover page. Item (10) suggests that the cover page include “a statement on the tax status of interest on the securities being offered.” In addition to whether the issue is taxable or tax-exempt under federal and state law, an issuer should disclose whether the issue is subject to the alternative minimum tax or an original issue discount. These facts are material to the tax status of the securities. In addition, Item (8) of Section I, on mandatory, optional and extraordinary redemption features, should specifically include put features of the issue, if any.

Section II, on the Summary of the Official Statement, states that the purpose of the summary is to set forth in brief form the important features of the security. While Section II states that the summary should be qualified by the entire official statement, the GFOA should emphasize more strongly the dangers of investors relying on summary information. The GFOA also should advise issuers, particularly in regard to summaries of call and put feature information, to ensure that every feature is described in the summary. An incomplete summary of redemption features may lead investors to assume that no other redemption features exist. As an alternative, Section II should suggest that none of the specific redemption features be described in the summary; rather, a statement that the issue is callable or puttable could be noted, along with a reference to the portion of the official statement describing complete redemption information.

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1 This matter is discussed below in the comments on the Procedural Statements.

The Board strongly endorses the recommendation in paragraph C of Section III, on Securities Being Offered, that issuers describe in a plan of refunding any rights reserved to modify the maturity or other terms of the escrow.<sup>2</sup> Such disclosure will help to ensure that such issues are priced accurately.<sup>3</sup> In addition, given wider reliance on, and acceptance of, using CUSIP numbers to identify municipal securities issues and their importance in automated clearance systems, the Board recommends that Section III recommend that the CUSIP numbers for an issue be included in this section to assist in the processing of the securities.

The GFOA should revise paragraph E of Section III, regarding information on put features, to recommend that issuers adopt standardized put notification periods. The Board has noticed that the notification periods for puttable securities are quite diverse. For example, investors may be required to give notice to a tender agent to put their securities anywhere from 10 to 30 days, or longer, before the actual put date. This may result in confusion for investors, as well as for dealers, and missed put dates. The Board understands that The Depository Trust Company has reviewed a number of puttable issues and you may wish to contact that organization for further information.

#### Procedural Statements

Information on issuers and their securities not only should be complete and accurate, but should be available to investors at a time and in a manner that makes the information useful for their investment decisions. The increasing complexity of municipal securities and the changing characteristics of the municipal securities market make timely and effective dissemination of information more important than ever before. The Board believes that the Procedural Statements better reflect today's information needs and, if followed, will result in an improved flow of information and a more efficient market.

The official statement is the single most important disclosure document for an issue of municipal securities. The Board strongly supports the recommendation in Procedural Statement No. 3, on Availability of Official Statements to the Public and Delivery of Official Statements to Underwriters, that issuers provide a copy of the official statement to any party that requests it. The Board urges the GFOA to emphasize that official statements should be made available to interested parties as early as possible in the offering of a new issue. Procedural Statement No. 3 also states that official statements should be provided to underwriters at a time and in sufficient quantity to allow the underwriters to mail them to investors for receipt prior to settlement. In this

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- 2 Recently, the Board expressed its concern that the market for escrowed-to-maturity bonds has been disrupted by events which have caused uncertainty concerning issuers' authority to exercise optional redemption provisions of escrowed-to-maturity bonds. It noted that it is essential that issuers, when applicable, expressly note in official statements and defeasance notices relating to escrowed-to-maturity bonds that they have reserved the right to call such bonds. Letter from Keith Brunemer, Chairman, MSRB to Jeffrey Esser, Executive Director, GFOA, dated March 17, 1987.
- 3 While disclosure in this area is essential, one unintended side effect is that issuers may begin routinely reserving the option to call escrowed-to-maturity bonds.

regard, Board rule G-32 requires dealers selling new issue municipal securities to deliver a copy of the final official statement (if one is authorized) to customers by settlement of the transaction. If the managing underwriter or a dealer serving as a financial advisor is responsible for preparing an official statement on behalf of the issuer, the rule requires that the official statement be prepared and made available promptly after the date of sale, but in no event later than two days prior to delivery of the issue to syndicate members. The Board recommends that Procedural Statement No. 3 include a specific reference to the requirements of rule G-32 to alert issuers to the time frame for official statement preparation and dissemination to which dealers are subject.

The Board is aware that occasionally issuers may delay the preparation of final official statements until certain information, such as interest rates and underwriting information, becomes available on the date of sale. Procedural Statement No. 2, on Use of Preliminary and Final Official Statements, states that official statements for competitive issues may be prepared prior to the date of sale and, with additional information printed and attached after the date of sale, delivered to investors as final official statements. Procedural Statement No. 4, on Underwriting Data, states that dealers may disclose underwriting information about negotiated issues, required by Board rule G-32, in a document separate from the official statement, thus eliminating the need for issuers to delay the final official statement for inclusion of this information.<sup>4</sup> These procedural statements should be strengthened to recommend these steps in order to encourage the earlier production of official statements. The Board also strongly urges that Procedural Statement No. 3 specifically state that, even in negotiated sales, issuers should complete official statements to the extent possible prior to the date of sale, so that final official statements may be made available to investors no later than a day or two after the date of sale.

The Board understands that, prior to the date of sale of an issue, it may be useful to distribute preliminary official statements with information on the issuer and descriptive information about the proposed securities, which information is not likely to change in the final official statement. The Board recommends that Procedural Statement No. 2, which discusses preliminary official statements, caution that preliminary official statements often are relied upon by investors in making their investment decisions and therefore should be as complete and as accurate as possible, based on information available at the time the document is prepared.<sup>5</sup>

Procedural Statement No. 8, on Dissemination of Information Releases and Providing Statements, Reports, and Releases to a Central Repository, recommends the submission of issuer disclosure documents to a central repository and other information dissemination services, which

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- 4 Procedural Statement No. 4 also states that such underwriting information may be disclosed on a confirmation of the transaction. Because of the increasing use of automated clearance and settlement systems and the inability of these systems to convey such information, the Board believes that use of a confirmation to disclose underwriting information will not be practical in most cases and suggests the reference to confirmation disclosure be deleted.
- 5 Board rule G-32 requires dealers to deliver to customers final official statements, if they are prepared, but does not require preliminary versions of the official statements to be sent if a final version is prepared.

should result in such information being more accessible to market participants.<sup>6</sup> The Board believes that issuers also should continue to be responsible for providing disclosure documents concerning their securities to interested persons upon request for the life of the securities. Such persons may be unaware that information is available from the repository or may be deterred by the cost of obtaining information from that source.<sup>7</sup> Therefore, the Board recommends that Procedural Statements Nos. 3 and 8 be amended to state that issuers should provide official statements and other information releases to any party, upon request, for the life of the issue.<sup>8</sup> While issuers should not be asked to incur all of the expenses involved in disseminating this information, the availability of disclosure documents from the issuer, at cost, should be an alternative to investors obtaining the documents from a repository. In addition, because of the importance of escrow agreements and other refunding documents in escrowed-to-maturity securities, the Board believes that the Procedural Statements should state that these documents also should be among those provided at cost by issuers to interested persons upon request and to repositories.

Procedural Statement No. 7, on Notices of Call and Call Payments, addresses the continuing problem of inadequate notification in the municipal securities market.<sup>9</sup> On November 14, 1986, the SEC sponsored a meeting of industry and regulatory organizations to discuss this issue, at which the GFOA was represented. The participants agreed on six standards that, if

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- 6 The Board has proposed an amendment to rule G-15 that would require dealers to supply customers with official statements in secondary market transactions, upon request. See MSRB Reports Vol. 7, No. 3, at 3-5 (1987). The availability of official statements in repositories would help dealers comply with this proposed rule.
  - 7 The Board understands that the cost of obtaining official statements from one repository is \$.50 per page with a minimum order of \$20 required. Official statements at other repositories cost as much as \$50 per copy.
  - 8 The Board previously has expressed to the GFOA the need for issuers to make official statements and other information about their securities available to investors for the life of the securities. Letter from Donald J. Robinson, Chairman, MSRB, to Jeffrey Esser, Executive Director, GFOA, dated April 3, 1985.
  - 9 The Board has alerted the GFOA to a number of complaints from investors, depositories and others that redemption notices sometimes inadequately identify the securities called or are not provided in a timely manner. Letter from Ralph Horn, Chairman, MSRB, to Jeffrey Esser, Executive Director, GFOA, dated March 3, 1986. The Board continues to receive such complaints on almost a weekly basis.

followed by issuers, their agents and trustees, would solve the call notification problem for future issues.<sup>10</sup> Procedural Statement No. 7 incorporates these standards<sup>11</sup> as well as a recommendation that call notices for bearer bonds be published in daily periodicals of national circulation. In addition to the six standards, the SEC recommended that issuers mail redemption notices to all registered owners by secure means such as registered mail, send follow-up notices to security holders that do not redeem securities on time, and mail redemption notices for bearer securities to security holders that supply their names and addresses for that purpose. The procedural statement should incorporate these SEC recommendations. The Board believes that, at a minimum, it is important to refer to them. The Board also recommends that the procedural statement recommend that issuers include the call notification standards in trust indentures and other governing documents of new issues to ensure compliance with the standards.

In addition, the Board urges the GFOA specifically to recommend that issuers contact their agents for call notification and trustees for existing issues to direct their compliance with the call notification standards. Such action by issuers would improve call notification for outstanding issues thereby relieving substantial deficiencies which have disadvantaged investors, dealers and depositories participating in the municipal securities market.

The Board would like to address two other procedural matters. First, although the Board understands that the Procedural Statements relate primarily to the dissemination of information about municipal securities, the Board recommends that the Procedural Statements address a continuing problem in the municipal securities market -- that of transfer delays. In May 1983, the GFOA (then the MFOA), the Securities and Exchange Commission, and the Board jointly recommended that issuers use transfer agents that agree to meet the 72-hour turnaround standard applicable to most corporate securities transfer agents or, if an issuer performs its own transfers, that the issuer voluntarily and publicly agree to meet the standard. The joint statement also suggested a standard record date of 15 days prior to interest payment date. The Board urges the GFOA to incorporate this position in a procedural statement along with a recommendation that issuers specify these standards in trust indentures and transfer agent agreements. Such a procedural statement also should recommend that issuers identify the transfer agent for an issue prior to the date of sale or award of an issue so that all parties are aware of the identity of the agent and can determine its performance record as early as possible. This could be done, for example, by identifying the transfer agent in the notice of sale or similar document.

Second, the Board has received a number of complaints concerning inadequate call notification, transfer delays and the failure of paying agents to make timely disbursements of interest and principal payments. Since these complaints should be of concern to the particular

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10 Release on Call Notification, Securities Exchange Act Release No. 34-23856 (December 3, 1986).

11 The Board notes that two of the provisions included in the procedural statement, the 30-day period between publication date and redemption date and advance notice of redemptions to registered securities depositories, appear to be limited to advance refundings. The Board believes that these standards should apply to all redemption notices.

issuer, a procedural statement should be adopted which advises issuers to designate a representative to receive such information and to include the name, title, address, and phone number of its representative in the disclosure documents for the issue.

#### Continuing Disclosure Guidelines

The considerable expansion of the section of the Guidelines on continuing disclosure reflects the market's need for up-to-date financial and other material information by municipal issuers. Since the Continuing Disclosure Guidelines originally were published in 1978, the municipal securities market has changed dramatically. The development of an active secondary market in municipal securities underscores the need for updated and accurate information about municipal securities issuers. The Board strongly endorses the GFOA's recommendation in this area.

The Board believes that, in the Introduction to the Continuing Disclosure Guidelines, the paragraph dealing with the availability of official statements should include a reference to the ability of investors to obtain a copy of official statements from the issuer, not just from a central repository, for the life of the issue.

Section V, on Changes in Indebtedness, should recommend that the cover page the CUSIP numbers of the outstanding issues be identified to facilitate identification of the securities.

In regard to Paragraph C of Section VI, on Information for Release Other Than on a Yearly Basis, the Board endorses the view that an issuer should issue a release regarding the terms of the escrow and the rights of the holders, including any rights reserved by the issuer to modify the maturity or other terms of the escrow, and the recommendation that an issuer send such release to registered securities holders. Without such information, investors may be disadvantaged in their decisions whether to retain or sell these securities.

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The Board appreciates the opportunity to comment on the Guidelines. The GFOA has addressed important disclosure issues in this revision and the municipal securities market will benefit from its work. The Board is concerned, however, that the voluntary nature of the Guidelines cannot ensure that issuers will follow its recommendations and improve municipal securities disclosure. (Given its strong interest in the adequacy of disclosure by municipal issuers, the Board will be giving continuing attention to this important area.) In order to aid the

GFOA in its efforts to bring the revised Guidelines to the attention of municipal securities market participants, the Board offers its assistance in educational and other efforts within the dealer community.

Sincerely,

H. Keith Brunnemer, Jr.  
Chairman