M E M O R A N D U M

TO: Participants in 1988 ABA/SEC Annual Roundtable

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RE: Topics for Discussion Regarding Municipal Disclosure

DATED: December 5, 1988

I. PROPOSED RULE 15c2-12

A. Applicability of Proposed Rule.

1. General Observation.

The proposed Rule does not differentiate among different types of municipal offerings. For example, it does not distinguish (i) by type of issuer (e.g., general purpose entity, special purpose issuer, conduit issuer), (ii) by source of payment (e.g., general obligation, special obligation, conduit financing agreement), (iii) by nature of the instrument (e.g., short-term obligation vs. long-term obligation) or (iv) by method of distribution (e.g., public offering, limited distribution, private placement).

2. Threshold.

(a) The proposed Rule would apply to any offering of municipal securities in excess of $10 million.

(b) The data in SEC Release No. 34-26100 indicates a greater need for disclosure, based on the number of issues in which defaults have occurred in the recent past, in issues of less than $10 million that involve conduit financings by municipal issuers on behalf of private users.

(c) Consideration should be given to whether a lower threshold should be applied to conduit securities than to other securities and whether distinctions should be drawn among such other securities (e.g., general obligation securities of general purpose state or local entities, revenue obligations of governmentally owned enterprises and obligations of special tax districts and tax increment districts).

3. Limited Offering Exemption.

(a) The proposed Rule, as explained in Release 34-2100 and by the staff in public meetings, does not provide for a limited offering or private placement exemption.

(b) Such an exemption may be implicit either because of the thrust of the proposed Rule in regulating municipal securities dealers when acting as underwriters or because of the Rule's definition of "underwriter" incorporating the 1933 Act concept of "distribution" as interpreted in the release proposing Rule 144A. If so, this should be made clear.

(c) If the Rule as proposed does not incorporate a limited offering or private placement exemption, consideration should be given to expressly including one in order to preserve the flexibility provided under current law. Such consideration could include whether restrictions to prevent "flow back" should be included and, if so, what form they should take.

B. Substance.

1. Adequacy of Disclosure.

(a) Apparently, the proposed Rule is not intended to address the adequacy of disclosure or to establish substantive standards for official statements, as opposed to dealing with the mechanics of requiring disclosure in a timely manner. The apparent intent of the Commission is to leave the determination of the standards of adequacy to the municipal securities industry and the courts through SEC enforcement proceedings and private causes of action under Rule 10b-5.

(b) Consideration should be given to making this intention clear.

2. Flexibility in Methods of Disclosure.

(a) The proposed Rule's emphasis on an "official statement" harkens back to the original 1933 Act concept of discrete distribution disclosure documents that may be too static and, in fact, impede development of an integrated disclosure approach in the municipal securities field.

(b) Consideration should be given to making clear that reference to an official statement is intended to be a flexible concept which could include incorporation of other materials by reference. (See II below.)

3. Status of Official Statement upon Review.

(a) The proposed Rule requires a broker, dealer or municipal securities dealer (an "underwriter") to obtain and review, prior to bidding for or purchasing municipal securities, an official statement that is complete except for certain specified information directly related to the sale (i.e., price, interest rate, selling compensation, amount of proceeds, delivery date, etc.).

(b) SEC Release No. 34-26100 indicates that the Commission does not intend that material information which is discovered to be misstated or omitted or which reflects changes after the official statement is obtained and reviewed should not be corrected in the final official statement.

(c) Consideration should be given to clarifying the Rule itself to state this intent, since the proposed Rule is inflexible on its face.

4. Obligation to Disseminate Preliminary Official Statements and Final Official Statements.

(a) The proposed Rule requires the underwriter to send (i) a copy of the preliminary official statement to potential purchasers, without specifying a cut-off date, and (ii) a copy of the final official statement to any person at any time, upon request.

(b) Consideration should be given to terminating the obligations to disseminate the preliminary official statement at the time the final official statement becomes available and terminating the obligation to disseminate the final official statement if a copy has been deposited in a central repository. (See II below.)

5. Time Period for Providing Final Official Statement.

(a) The proposed Rule in effect requires issuers to provide a final official statement within two business days after the purchase agreement has been executed.

(b) Consideration should be given to (i) whether two business days is too short a period of time, and (ii) the conditions under which failure to comply will not constitute a violation of the Rule.

(c) Particularly in smaller localities, and even in large metropolitan areas during "crunch" periods, it may be difficult or impossible for the printer to meet the two business day requirement.

II. CENTRAL REPOSITORY

A. Official Positions Regarding Creation of a Central Repository.

1. MSRB.

The Municipal Securities Rulemaking Board ("MSRB") proposed to the SEC in a letter dated December 17, 1987 that the SEC adopt a rule requiring issuers to file official statements and other documents, such as defeasance escrow agreements, with a central repository.

2. SEC.

SEC Release No. 34-26100 does not specifically endorse the concept of a central repository but requests comments on a broad range of topics.

3. ABA

(a) The ABA already is on record as endorsing the concept of a central repository.

(b) A central repository would make available on a continuing basis the description in the final official statement of the structure of the securities, e.g., redemption features. In addition, it would provide a means of (i) ending the obligation of underwriters to disseminate a final official statement (see I.B.2. above), (ii) facilitating incorporation by reference, and (iii) encouraging the filing of periodic information statements. (See C below.)

B. Specific Topics for Consideration.

1. The major areas of concern are raised by the MSRB's proposals that:

(a) the repository be created and operated under governmental auspices, presumably those of the MSRB (in order to insure proper operation),

(b) the filings be mandatory (in order to achieve comprehensive covereage), and

(c) the obligation to file be imposed upon the issuer (since the official statement is deemed to be "the issuer's document").

2. While (a) and (b) may be appropriate, consideration should be given to imposing the obligation to file on the underwriter by an amendment to MSRB Rule G-32 on the grounds that (i) it will evoke less resistance from issuers and (ii) it likely will prove more effective since the underwriter probably is in the best position of any participant in the financing to make the filing. (Underwriters, for example, currently are required to deliver copies of the official statement to the CUSIP Service Bureau in order to obtain a CUSIP number and regularly do so.)

C. Relevance to Periodic Reporting.

1. It is desirable to encourage periodic reporting by municipal issuers, both to facilitate the distribution process and to improve the quality of information available to the secondary market. The Government Finance Officers Association has taken steps in this direction in their Disclosure Guidelines for State and Local Government Securities ("Guidelines for Timely Provision of Information on a Continuing Basis").

2. A central repository would not only preserve for the secondary market information furnished at the time of distribution but would encourage periodic reporting by establishing a recognized place to receive the information and by increasing the ability of issuers to incorporate periodic reports by reference in satisfying their disclosure obligations on distributions, a flexibility of which issuers likely would want to take advantage.

III. INTERPRETIVE RELASE

A. General Observation.

The consensus of most major municipal brokers and dealers, as well as counsel in the industry, is that the Interpretive Release accurately reflects the state of the law insofar as the disclosure and reasonable investigation obligations of an underwriter of municipal securities are concerned. Clarification of certain statements, particularly in competitively bid offerings, however, may be helpful.

B. Other Areas for Clarification: Credit Enhanced Financings.

There currently is uncertainty and inconsistent practice with respect to disclosure and reasonable investigation obligations in municipal securities offerings

backed by third-party credit enhancements. These include financings backed by bank letters of credit, municipal bond insurance and guaranteed investment contracts. The questions within the industry involve disclosure and investigation with respect to both the credit enhancer and the underlying obligor. It may be desirable to clarify this area through interpretation.

IV. SEC'S VIEWS ON DISCLOSURE OBLIGATIONS OF COUNSEL REGARDING AREAS OF LAW COVERED BY ITS OPINION.

A. In the Staff Report On The Investigation In The Matter Of Transactions In Washington Public Power Supply System Securities (the "Staff Report"), the staff points out that at the time bond counsel and special counsel to the Supply System issued their unqualified opinions as to the legality and enforceability of the Participants' Agreements securing the Project 4 & 5 Bonds, it knew there were arguments that take-or-pay contracts might not be authorized by existing statutes (pp. 23-24, 285-286, 300, 311-314, 324).

B. The Staff Report observes:

> ". . . bond counsel and special counsel were principally responsible for disclosure [regarding the validity of the take-or-pay contracts] through their opinion letters and the disclosure in the text of the official statements. Although opinions on legal issues frequently contain some element of uncertainty, the state of the law was not as clear as those relying on the counsels' opinions might reasonably have assumed (p. 374).

* * * *

C. In the Report of the Securities and Exchange Commission on Regulation of Municipal Securities, dated September 22, 1988, the Commission commented:

> The Staff Report also indicates that the official statements concerning the guarantees of the participating utilities failed to disclose uncertainties with respect to the validity and enforceability of many of the agreements between the Supply System and the participating utilities.

D. The implication of the quotations from the Staff Report and the Report of the Commission seems to be that counsel has an obligation to disclose in its opinion or in the official

statement areas of the law that are not absolutely clear but on which it has satisfied itself it can render an unqualified opinion.

E. If this implication is correct, this view may deserve reconsideration. Such a position is contrary to industry practice and, in the view of many, to good policy.