



February 2019

Amendments to Continuing Disclosure Obligations Under Rule 15c2-12

The Securities and Exchange Commission (SEC) has amended Rule 15c2-12 to add two new events which must be included in continuing disclosure agreements (CDAs) for municipal securities issued on or after February 27, 2019. The new events are:

- (15) incurrence of a **financial obligation** of the obligated person, **if material**, or agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation of the obligated person, any of which affect security holders, **if material**; and
- (16) default, event of acceleration, termination event, modification of terms, or other similar events under the terms of a financial obligation of the obligated person, any of which **reflect financial difficulties**.

An “obligated person” is an issuer of municipal securities, or any person committed by contract or other arrangement to support payment of all, or part, of the obligations on municipal securities (other than providers of municipal bond insurance, letters of credit, or other liquidity facilities).

The SEC’s release of the amendments in the Federal Register (the “SEC Release”) states that the new events are designed to increase transparency in the municipal securities market by requiring timely disclosure of information related to financial obligations that could affect the issuer’s or obligated person’s liquidity, creditworthiness, or an existing security holder’s rights. Although many industry groups have called for voluntary disclosure of the incurrence of material financial obligations, such as direct purchase and direct loan transactions with financial institutions, few disclosures have been made. Rule 15c2-12, as amended (the “Amended Rule”), will require underwriters in a primary offering of municipal securities to ensure that CDAs entered into on and after February 27, 2019 contain the two new events.

"Financial Obligation"

The Amended Rule defines “financial obligation” to mean a (i) debt obligation, (ii) derivative instrument entered into in connection with, or pledged as security or a source of payment for, an existing or planned debt obligation, or (iii) guarantee of (i) or (ii). The definition excludes municipal securities as to which a final official statement has been provided to the Municipal Securities Rulemaking Board (MSRB) consistent with Rule 15c2-12.

The SEC Release provides that the definition of “debt obligation” is intended to capture short-term and long-term debt obligations of an issuer or obligated person under the terms of an indenture, loan agreement, or similar contract to be repaid over time. The SEC Release also provides that “debt obligation” can include lease arrangements entered into that operate as vehicles to borrow money, formerly known as “capital leases” or “financing leases,” but should not include ordinary financial and operating liabilities incurred in the normal course of business.

The SEC Release defines “derivative instrument” as a swap, security-based swap, futures contract, forward contract, option or any similar instrument to which an issuer or obligated person is a counterparty. The SEC Release provides that including “guarantee” in the definition of financial obligation is intended to capture

contingent financial obligations of an issuer or obligated person to secure obligations of a third party or obligations of the issuer or obligated person.

The Amended Rule also requires the disclosure of an agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation which affect security holders. Although not applicable to general obligation bonds, issuers of revenue bonds who modify the terms of the applicable indenture or resolution may be required to disclose such terms.

"If Material"

There is no definition or standard of materiality in the Amended Rule. Instead, the SEC restated in the SEC Release that the determination of materiality should be based on whether the information would be important to the total mix of information made available to a reasonable investor. Issuers and obligated persons will need to work with their auditors and municipal advisors to determine which financial obligations require disclosure. Underwriters will presumably review audited financial statements and social media sources to determine compliance with the Amended Rule.

DEFAULTS AND OTHER EVENTS UNDER FINANCIAL OBLIGATIONS

Any issuer or obligated person entering into a CDA on or after February 27, 2019 will be required to disclose a default, event of acceleration, termination event, modification of terms, or other similar events under the terms of a financial obligation which reflects financial difficulties, even if such an event relates to a financial obligation incurred prior to February 27, 2019. There is no materiality qualifier for these types of events. The term "financial difficulties" is not defined, but has been included in Rule 15c2-12 since 1994 without much controversy.

INFORMATION TO BE DISCLOSED

The SEC Release provides that the disclosure of the incurrence of a financial obligation should include a description of the material terms, such as the date of incurrence, principal amount, maturity and amortization, interest rate (if fixed) or method of computing the interest rate (if variable), including any default rates, and other terms. The SEC Release also provides that issuers and obligated persons can alternatively, or in addition, submit copies of term sheets, commitment letters or the actual transaction documents. Confidential information is not required to be submitted and issuers and obligated persons should work with their lenders and other transaction participants to agree on the information to be disclosed under the Amended Rule. Disclosures for agreements which affect security holders and events reflecting financial difficulties would include a description of the agreement or event and any information the issuer or obligated person believes would be important to a reasonable investor. The Government Finance Officers Association (GFOA) has prepared templates for disclosure of the two new events on its [website](#).

Disclosures are to be made to the MSRB through the Electronic Municipal Market Access (EMMA) system in the same manner as other event reporting. The EMMA system is being modified for reporting of the new events. Similar to other events, disclosure of the incurrence of a financial obligation and the other new events under the Amended Rule are required to be made within **ten (10) business days** of the occurrence of the event.

NEXT STEPS

Issuers and obligated persons, especially those entering into numerous financial obligations on an annual basis, should consult with their municipal advisors about adopting procedures to ensure new financial obligations, agreements related to financial obligations, and any events reflecting financial difficulties are identified and reported in a timely manner to those in charge of continuing disclosure reporting. Once these new events are included in an issuer's or obligated person's CDA, the incurrence of a financial obligation, an agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation, or a default, event of acceleration, termination event, modification of terms, or other similar events under the terms of a financial obligation of an issuer or obligated person which reflects financial difficulties, will be required to be reported to the MSRB within ten (10) business days of the occurrence of the event. Underwriters hired to sell municipal securities in a negotiated offering, and underwriters bidding on municipal bonds and notes in competitive transactions, are likely to review audited financial statements and other sources to confirm that issuers and obligated persons have complied with reporting for these new events.

FOR MORE INFORMATION

If you have any questions regarding the Amended Rule, please do not hesitate to contact one of the members of our [Public Finance Group](#) below:



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