

Disclosure Lapses Bring Expensive and Tough SEC Enforcement – Internal Disclosure Policies and Procedures A Key Focus

The Securities and Exchange Commission (SEC) recently issued its fourth cease and desist order of 2013 regarding municipal disclosure failures. An Indiana school district is the subject of *In Re West Clark Community Schools*¹ (Order) in which the SEC found that the school district misled investors in a 2007 offering document by falsely stating it had complied with prior continuing disclosure obligations.² The school district agreed to a settlement of the charges, resulting in the agreed Order.

The West Clark Community Schools enforcement action follows closely on the heels of the SEC's orders regarding the State of Illinois (pension disclosure),³ the City of Harrisburg (public statements posted on the City's website)⁴ and the City of South Miami (misstatements regarding federal tax compliance).⁵ The SEC's approach in these enforcement actions is consistent with its report on the municipal securities market published in July 2012.⁶ In the report, the SEC recommended, among other things, it be given direct authority over municipal issuers so that, among other things, the SEC "could consider the appropriate disclosure policies and procedures that municipal issuers should adopt to assure that they will satisfy their primary and ongoing disclosure obligations."

Congress has not yet given the SEC that direct authority, but through its enforcement actions the SEC is demonstrating what it might do with that authority and, on a case-by-case basis, asserting the authority it possesses at present.

The SEC's Messages to Municipal Issuers

One clear message to be taken from these orders is that each municipal issuer, regardless of size or frequency of issuance, needs to review whether, and exactly how, it is meeting its disclosure responsibilities under the federal securities laws. Another obvious message is that the SEC is motivated, and is devoting the resources necessary, to detect and prosecute violations.

Your Recommended Response

It is expensive and distracting to become the subject of an SEC enforcement action. It is recommended, therefore, that each municipal issuer (i) review its internal disclosure policies and procedures with its administrative staff and experienced disclosure counsel, (ii) confirm the conformity of those policies and procedures with the SEC's expectations and (iii) confirm its

¹ Securities Act of 1933 Release No. 9435 / July 29, 2013; Securities Exchange Act of 1934 Release No. 70057 / July 29, 2013; Administrative Proceeding File No. 3-15391.

² In a companion order, the SEC also held the underwriter of the 2007 bond issue accountable for its inadequate diligence as to the school district's compliance with its prior commitments, as well as other unrelated rule violations.

³ Securities Act of 1933 Release No. 9389 / March 11, 2013; Administrative Proceeding File No. 3-15237.

⁴ Securities Act of 1934 Release No. 69515 / May 6, 2013; Administrative Proceeding File No. 3-15316.

⁵ Securities Act of 1933 Release No. 9404 / May 22, 2013; Administrative Proceeding File No. 3-15329.

⁶ Report on the Municipal Securities Market, U.S. Securities and Exchange Commission, July 31, 2012.

compliance with the commitments it has made. An issuer's adoption of, and consistent adherence to, policies and procedures that meet the SEC's expectations are likely to reduce the risk of aggressive SEC enforcement action if there is ever an isolated lapse in compliance.

More on Policies, Procedures and Training

According to the Order, the school district agreed to bring all required filings current (which appears to have been done in 2010), adopt enhanced policies and procedures regarding its contractual continuing disclosure obligations, implement annual training for personnel involved in the bond disclosure process, and establish policies and procedures to ensure all required notices and filings are made electronically through the Municipal Securities Rulemaking Board (MSRB).

The school district's enhanced policies and procedures will include, according to the Order, (i) designation of an employee responsible for ensuring the school district's compliance with all contractually required continuing disclosure covenants, (ii) annual certification by that employee to the superintendent that continuing disclosure submissions are current and accurate and (iii) certification by that employee that any information regarding the school district included in an offering document for any future securities offering is accurate and complete. The school district is also required to disclose the terms of the Order in any future offering document for five years.

The order provides that annual training must include a review of the school district's obligations under the federal securities laws and its disclosure policies. Upon completion of the annual training, all trained personnel must certify completion of the training and that they understand and will comply with the school district's disclosure policies. A copy of the enhanced disclosure policies is required to be posted on the MSRB's EMMA website, as are any subsequent amendments to those policies.

An "Ounce of Prevention"

The Squire Sanders lawyer with whom you regularly work is available to address any questions you may have concerning your entity's disclosure "readiness" in the context of the SEC's stated expectations as to disclosure policies and procedures. We counsel municipal issuers on a regular basis as to disclosure matters, including processes for development and handling of information to be set forth in offering documents and continuing disclosure submissions. In many instances, little more than better documentation of existing processes and of responsibility for information that is already presumed will be needed to meet the SEC's expectations.