CALIFORNIA DEBT AND INVESTMENT ADVISORY COMMISSION

WEBINAR TRANSCRIPT

Achieving the Grade: School District Continuing Disclosure Practices in Today's Market
November 14, 2012

>> Welcome, everyone. This is Mark Campbell, executive director for CDIAC to our next in a series of webinars, achieving the grade, school district continuing disclosure practices in today's market. I'm just going to launch this with a couple of brief comments and some administrative activities. And then turn it over to an excellent panel speakers. They include Lynn Gruber, principal Koppel and Gruber public finance. She will facilitate the discussion today she works on school districts continuing disclosure formation and administration of community facilities districts. Developing fee reports and other projects, which areas Don Field, partner at Orrick, Herrington and Sutcliffe out of the San Francisco office is that right? I believe so.

>> Orange County

>> Thank you. Where he his lead attorney for (inaudible) extensive experience and ongoing counsel disclosure counsel underwriter and financing techniques used by school and community college districts. George Greer partners securities litigation and enforcement with Orrick Herrington and Sutcliffe in their Seattle office focuses on complex commercial litigation with an emphasis on securities. He has conducted a number of internal investigations on behalf of the boards of directors in public and private companies and is a speaker at conferences and seminars and Frank Vega, senior vice president of Piper Jaffray in the Los Angeles office where he specializes in structuring property tax supported debt, cops, revenue bonds text anticipation notes additional information on each of the speaker's bio is available on the website. So before we begin we are going to do a couple pulling questions to allow the speakers to get some context.

To begin with our first polling question should show up in a minute. If you are a representative of public agency are you from one of the following city, County, federal state, special district or other. Go ahead and take that off and we will provide the results to you. Okay it looks like the majority are from other. Nearly 50%, 24% County, about less than 20% federal, state. And 9% special district. The next polling question, so we are interested in understanding whether you have received a letter from the SEC. A simple yes/ no response to get an idea of whether any of your financings have been subject to any SEC reviews. Looks like 100% say no. I guess that is a good thing okay, finally, do you submit your disclosure information to the MS system? And of course today's topic really recognizes the unique nature of school district financing and in particular the disclosure process and the results look like about two thirds of you, three quarters of you do not, 28% do. Throughout the presentation today feel free to submit questions to the speakers. Our intent is to cover those at the end of the presentation however if they do relate to a specific topic the speakers covering and they have an opportunity to view it and respond to it they will, otherwise recognize they will address us at the end of the presentation. Life captioning is provided for this program. You will have to access that through the URL. At www.streamtext.net\player?event=CDIAC and that will provide a waiting for the go to webinar portal and you will access live captioning through that. And lastly I want to acknowledge that there are certificates of attendance available for participants and you can receive those

by e-mailing CDIAC at CDIAC_Treas.@CA.gov. So having covered all of those administrative tasks I'm going to turn it over now to Lynn and begin the seminar, thanks, Lynn.

>> This morning I want to talk a little bit about the purpose of the webinar, continuing disclosure is a way that issuers communicate with their bondholders and without the market really doesn't have any information to base their decisions on so today we want to educate you on the process and your role as an issuer answers coming about because the SEC is stepping up the requests relating to disclosure and George will be talking more about that and CDIAC in DBC debt have completed research studies that show that missing disclosure is on the horizon during the economic downturn when the market is more concerned about default and needs for disclosure the disclosure submission actually has decreased. And the older the information that is disclosed, the less relevant and useful it is to the market.

So DBC data studied about 17,000 bond issues from 2005 two 2009 so they seek bonds issued between 1996 and 2003. They focused on two things, the financial statement disclosure and also the timing of disclosure and what this slide shows is that 43% of the bombs our current about 56% have either failed to disclose for one or more years and in 2009 40% failed to file and this slide shows only 42% of the bond issues are current. This is countrywide. So it does show that compliance is and where we need to have it.

CDIAC also did a California study similar criteria for one year only for the 2010 year and they look at different market sectors K-12 CFC GPA RDA bonds and all other bonds and this slide shows the school district sector. So 60% have been filed on time which is better than the national average but the other sectors of the California have a 72% on-time submission so we have some work to do there. With that I will turn it over to Don Field to give you more information on the background and process of continuing disclosure.

>> Thank you and I'm going to start with a general overview of disclosure requirements for musical issuers under federal securities laws. Municipal issuers are not obligated to make any disclosures unless required to do so by law or agreement. Now, unlike corporate securities municipal securities generally are exempt from the registration requirements of federal and state securities laws however municipal securities are subject to securities laws disclosure rules generally referred to as the anti-fraud rules. And in this regard statements made by me to split issuers to investors or potential investors and even statements to the public generally is likely to be heard and relied upon by the securities market are subject to regulation by the Securities and Exchange Commission under two key antifraud provisions of federal law which are section 17 a of the securities act and rule 10 be five promulgated by the SEC pursuant to section 10 of the Securities Exchange Act. In addition section 14 your of this courteous exchange act requires disclosure in association with (inaudible) purchase of outstanding securities these laws and regulations are designed to ensure that parties buying or selling securities have access to information necessary to make an informed investment decision. In order to comply with the laws public or offering, in order to comply with the laws for public offering of municipal securities issuers prepare a document analogous to a corporate prospectus called an official statement. That includes all of the information and investor would need to decide whether to purchase the offered securities. Again, municipal and she issuers must assure

that in connection with the issuance and sale of municipal securities to the public prospective purchasers are providing the information they need to make an informed investment decision. Under the antifraud laws it is unlawful connection with the purchase or sale of a municipal security to make any untrue statement of material fact or to omit a statement of material fact necessary in order to make the statements made in light of the circumstances under which they were made and not misleading.

The other benefits to the disclosure municipal issuers who tell their story in a clear and complete way and develop a reputation for clear disclosure can drive financial benefits and the price paid for their bonds. And the benefit of good municipal disclosure has been further enhanced by the recent decline in the use of bond insurance and in confidence and bond ratings as a complete measure of credit quality. Investors now to a greater extent than ever need and desire to make their credit evaluation and an informed evaluation requires comprehensive and adequate disclosure. On the other hand in adequate disclosure practices can lead to such outcomes or consequences as investigations by the SEC which is what George will discuss later in the presentation, investigations by local district attorney or US Justice Department, and imposition of fines or penalties, civil suits or damages, substantial out-of-pocket costs to defend against government or private investigation sources and harm to an issuer's reputation and investors confidence.

So disclosures at the outset are very important and we will get into the requirements of continuing disclosure. But other than what is with respect to tender offers are generally is no obligation to provide post-issuance disclosure except to the extent the issuer has agreed to do so. Of course if and issuers making a statement it should expect to reach a securities market has an obligation to make sure the statements are not misleading to investors.

So I said that there is no legal obligation form the issuer to make post-issuance disclosure. So, how are municipal issuers subject to ongoing disclosure obligations? Well the SEC currently regulates other participants in municipal financings including underwriters broker-dealers and reading agencies and the regulatory regime imposed on these entities can have indirect impacts on issuers. One example of this is SEC rule 15c2-12 which is applicable to underwriters but requires them to cause initial issuers to prepare official statements and to undertake in writing to provide post-issuance disclosures to holders of securities under most circumstances. By conditioning municipal access to public workers the SEC indirectly imposes an obligation on issuers. So if we could move to the next slide.

The requirement that issuers prepare an official statement and what an official statement is important as we will discuss later but for now let's focus on the continuing disclosure requirements of rule 15c2-12. Rule 15c2-12 pars participating underwriters of municipal securities in the principal amount of $1 million award to reasonably determined that each issuer or any other obligated person has undertaken a written agreement for the benefit of folders of those securities to provide specific categories of ongoing information. Does underwriters require issuers of musical securities to undertake continuing disclosure obligations pursuant to continuing disclosure agreements or certificates. And we can move to the next slide.

Before get to the specifics of continuing disclosure requirements of 15c2-12 it's important to take a step back and understand the reasons for the requirement. Part in 1995 municipal issuers generally have no obligation direct or indirect to provide ongoing disclosure. Thus if a municipal issuers sold securities or bonds it was generally under no obligation to provide any updates to its initial offering disclosure unless and until it sold an additional security in the market. As you can imagine this created issues for investors that want to treating medicinal securities in the secondary market. In this regard the SCC in his 1992 report on the municipal securities market cited a number of reasons why considered establishing the continuing disclosure requirement a necessity for the market. One being that for investors to make informed and intelligent investment decisions in the secondary market it is important that. The continuing disclosure be available. Another being that the secondary market has impaired efficiency when there is lack of continuing and pertinent information. And third, another being that incomplete information impacts pricing with the likelihood that pricing will inaccurately reflect value.As a result in 1994 the SEC adopted the amendments to 15c2-12 that required continuing disclosure obligations.

So let's move to the next slide and start walking through the continuing disclosure components of rule 15c2-12. Again it requires participating underwriters of municipal securities to reasonably determined that each issuer or any other updated person has undertaken in a written agreement for the benefit of folders of the securities to provide specific categories of ongoing information. Now, in California school district financing the school district is generally the only obligated person. However there are some instances in which there may be other obligated persons. So what is an obligated person? And obligated person is defined to mean any person who is either generally or through an enterprise found or account of such person committed by contract or other arrangement to support payment of all or part of the obligations on the municipal securities to be sold.

Notice generally accepted that a person's obligation must before material portion of the annual debt service in order for the person to be an obligated person. However a tax there is not, passive taxpayer is not an obligated person even if the taxpayer represents a significant portion of the issuer's tax base. Thus for school district general obligation bonds and lease revenue supported that including CLP's, the school district is only, ordinarily the only obligated person. In regards to school district general obligation bonds, this is the case even in the situation where a single taxpayer within the district pays a large percentage of the taxpayers levied within the district. Again they are a passive taxpayer. Similarly, a nonprofit corporation or joint powers authority acting as the issuers on behalf of the school districts lease revenue debt is not deemed an obligate a person because the source of the debt service is the school districts lease payments. Now on the other hand a landowner developing in a mello roos is financing is often considered an obligated person and that they are generally responsible at least initially for a material portion of the annual debt service on the related bonds and they are not just a passive taxpayer in that they are materially developed in the development and success of the related project. So let's move to the next slide take about types of information required under 15c2-12.

There are four specific categories of ongoing information to be provided under the rule. First certain annual financial information of the type presenting the official statement for each obligated person for whom financial or operating data is presented in the final official statement must be provided. As we will discuss in a few minutes,

this information will vary based on the type of financing involved. Second, audited financial statements when it is available for each such obligate a person must be provided. Now the first two categories generally make up what is known as the issuer's annual report. Which we will be discussed in more detail in a few minutes. Third notice must be provided in a timely manner not in excess of 10 business days after the occurrence of certain types of events are likely to be material to bondholders or potential investors and forth, notice must be provided of any failure to file the required annual financial information described in the first category on or before the date specified in a written agreement. As we will discuss more in a moment, this information must be disseminated to the market through the municipal securities rulemaking Board's electronic municipal market access system otherwise known as the MS system.

Let's move to the next slide. Now, again rule 15c2-12 requires participating underwriters of medicinal securities to reasonably determined that each issuer or any other obligated person has undertaken in a written agreement for the benefit of folders of securities to provide the specific categories of ongoing information. So let's talk about the content of the required written agreement or contract. Any agreement, the issuer must agree to provide the required ongoing information. In addition, the written agreement or contract must identify each person from annual financial information and notice of material events will be provided. It must specify in reasonable detail the type of ongoing financial information to be provided. And it must specify the accounting principles pursuant to which the financial statements will be prepared and whether the financial statements will be audited. Finally it must specify the date on which the annual financial information for the preceding fiscal year will be provided. Now the written agreement may also provide that the continuing disclosure obligation may be terminated with respect to any obligated person if and when such person owner remains an obligated person. Now in school district financing you generally don't have to worry about that because the school district is generally going to remain an obligated person until the debt is paid at maturity however there are some instances where a person at some point may not remain an obligated person. For example for a landowner developer in a mello roos is financing is developed and sold substantially all of the lots of the development and therefore is no longer responsible for material portion of the annual debt service on the related bonds, such landowner developer can be relieved of his or her obligation to provide ongoing information.

Let's move to the next slide. Now, an agreement is often entered into with the bond trustee for the related financing. This can be helpful because there's a third-party monitoring that the ongoing disclosure is provided. However the issuer has the option to execute a continuing disclosure certificate instead of an agreement in such case the issuer can either assume dissemination responsibility or appoint a dissemination agent but there may not be a third-party monitoring compliance. To avoid ongoing fees especially in the current budget situation many school districts have decided to assume dissemination responsibility. However to avoid coming out of compliance is important that such school districts put systems in place to make sure that the school districts, I'm sorry to make sure the requirement is not missed if there any changes in staffing or staff responsibilities. As we will hear from George in a few minutes, noncompliance can be very costly if it results in an SEC investigation so if the school district is not confident that the systems will ensure compliance of may want to consider to have a third-party engaged to ensure compliance. In all cases the person responsible for disseminating the ongoing disclosures

required to provide information to the market through DMS system. And Lynn is going to talk about that briefly now.

>> As I mentioned, the disclosure information is to be submitted to the MS system which is the electronic municipal market access system. Age is a centralized online source for municipal bond information encouraging compliance and transparency. It is free to users. And very easy to use. Next slide please. And provides for the electronic posting of reports, second offense, voluntary information and other information and the EMMA website is there on the slide. The MSRP continues to date information available on EMMA, and now includes trade information is also if you have gone on to my recently I encourage you to get onto EMMA and do some searching around searching around and find what's available.

>> Thanks Lynn, some obligations are exempt from continuing disclosure requirements including some short-term obligations and privately placed securities or subject to lesser ongoing disclosure requirements including tax and revenue anticipation notes or TRA in. However the school district financing will be subject to the continuing disclosure requirements so we will not spend time discussing exemptions in detail other than to note that there are some so if we could go to the next slide.

>> One more slide, slide number 18. The annual ongoing information provided to the secondary market as opposed to the event notices is submitted to EMMA in the form of an annual report. The content of the annual report is detailed in the convenient disclosure agreement as previously discussed generally discuss the issuer's audited financial statements and the other annual information of the type presented the official statement for the related financing. The due date for the annual report is also detailed in the continuing disclosure agreement. Most issuers agreed to provide the report within 6 to 9 months after the end of the fiscal year.

There are various types of school district financings include lease financings or certificates of participation. General obligation bonds, community facilities districts Mello Roos financing, bond anticipation of some tax revenue anticipation notes, and the other annual information required to be provided will be based on the type of financing involved.

Let's look at the typical types of school district financing. The repayment of fiscal disagree subrogation or CLP financing will generally be dependent on the school district's general fund the type of information that will be presented on the official statement for the financing and therefore required to be updated while the obligation remains outstanding includes information about the school districts adopted budget, other outstanding obligations, average daily attendance, base revenue not met, number and type of district employees, assess value information and taxable property within the district, CalPERS and Cal STR information and investment policies and County pull information because that is where the districts funds are going to be held. All of this information relates to the general financial health of district and really the repayment source of the debt so let's move to the next slide. Now a school district general obligation bond is repaid with property taxes levied on the taxable property within the boundaries of the school district. The type of information I would be presented in the official statement

for the financing and therefore required to be updated whether bonds remain outstanding include property tax information including the assessed values of taxable property within the district, general taxpayer information initially to talk to the taxpayer within the district to show how diverse the tax base is and also property tax levies, collections handling currencies. Again, there will be County information in areas will including whether the county has a teeter plan in place which impacts the district exposure to text doing menses as well as account investment will information is the county holds the property taxes collected to repay the bonds in the County pull. Now it is important to note that for various reasons, rating agencies rate California school district general obligation bonds in part based on the school district's general finances even though the bones are payable from property taxes. Thus continuing disclosure agreements for school districts bonds will also require updates for the same information generally provided for general fund or CFP financings.

Now a CFD or Mello Roo financing is because special taxes levied on the property within the boundaries of the community facilities District that is the type of information that would be presented in the official statement for financing and therefore required to be updated whether financing remains outstanding includes bond information for the related CFD including information about the CFD outstanding bonds and reserve fund balance and also information about the community facilities District itself. The total assessed valuation of property within the district, special textile includes information, foreclosure information and also land owner information again, to show the diversity of the land ownership within a CFD.

Now, and issuer of the notes is not required to enter into a continuing disclosure agreement is the notes are in authorized denominations of $100,000 or more and have maturity of nine months or less. Moreover if the notes of the student maturity of 18 months or less the issuers will be required to provide the event notices to be discussed in a few moments. Otherwise the other annual information that will need to be updated with respect to a note financing will be based on the type of the node. For example a general obligation bond anticipation note would require updates of information similar to what would be provided with respect to a general obligation bond financing.

Now, as previously discussed, the anti-fraud rules apply to disclosures reasonably expected to reach investors in the trading markets. Annual reports and material event notices must therefore be accurate and not omit any information needed to make the disclosures not misleading. Issuers are not required to disclose all material information, but the information that is disclosed must not be misleading. An example of this would be fiscal district was required to disclose its ADA figures and consistently had upward trending ADA that new ADA was going to drop dramatically and the following year, and in such situations is likely that the school district would be obligated to disclose the additional information rather than just reporting the most recent figures showing the consistent trend upward. So, when reviewing your disclosures you always need to keep in mind that you want to make sure that there is no material misstatement or omissions in your disclosure of the updated information.

So let's move to the next slide. In addition to the annual ongoing information rule 15c2-12 requires the notice of certain significant offense be given in a timely manner not in excess of 10 business days after the occurrence of

the event. In the case of 9, 11 those notices will always be given. In the case of seven events, the notice will be given if the events are material. Moving to slide 26 it shows the events that need to be noticed in all events. The SEC is essentially determined that these events are always important to investors and therefore require the notice be given of these events in all cases. When you look at the list which includes things like default and substitutions of security should be obvious that these would be important for investors to know. Now slide number 27 shows the events that may not be important to investors depending on the circumstances and therefore notice of these events is only required if the event is material.

So of course it is important for issuers to be very familiar with both types of events, some of this can be required, provided when required and again Mr. leads to the issuers having systems in place to make sure it meets its continuing disclosure obligations.

Move to the next slide. Now, rule 15c2-12 requires underwriters to cause any issuers to prepare official statements and undertaken writing to provide post-issuance disclosures to holders of securities. In addition, rule 15c2-12 provides that an official statement must contain a description of the continuing disclosure undertaken and any instances in the previous five years in which the issuer or other obligated person failed to comply in all material respects. Now, Georges going to discuss the role of this requirement with respect to the antifraud rules and the SEC recent inquiries into California school district continuing disclosure compliance. But I want to make the point that careful and diligent attention to each disclosure undertaken can improve the issuers relations with investors for future financings. Providing updated and timely information on a timely basis is a great way to for to investor that the issuers managing its affairs well and being able to indicate that you have not failed to comply will reduce or eliminate investor worries that updated information will not be available for secondary market trades. And maybe I could ask for and if you could comment on this slide, just on the investor compliance

>> absolutely done, thank you and good morning everyone. Everything Don has raised some excellent points and I think with the focus of the securities and exchange commission I think it is quite apparent that they take this very seriously because I think some of the background to all of this was during the financial crisis and a lot of the negative press that notably surrounded some bond transactions that didn't go well outside of California but nonetheless, that did occur as well as some of the things that we've been seeing here in California with regard to some general municipality bankruptcies and negative financial results has certainly caused some angst in the financial markets and these rules aren't intended to provide additional work and to penalize school districts, but rather to ensure that there is a fair and transparent marketplace. But investors can reasonably base their decisions to bind your bonds or TRA and or CLP, so the idea here is to not just provide what the bare minimum requirements are under the law and we will get to this a little later in the presentation, but rather to show and to give the investing community some reassurances that the school districts will constantly update and provide this information.

And so it's really more a matter of trying to put best practices in place so that there is sort of a routine mechanism by which any material even will be posted or rather your annual reports are posted in a timely manner because

this is ultimately where investors base their decisions to buy your bonds and how that impacts USA school district is, the moinvestors that you have ipation you have in a bond sale So, this is anthe Scotus will provide information to the responsible dissemination agent which could be internal party or staff member they also going to distribute the annual reports and notices to the board and notify board members to review and comment on the disclosures. Again the antifraud rules apply to disclosures reasonably expected to reach investors and the trading market so the information disclosed must not be dissuaded misleading and careful attention should be given to determine whether information even if accurate is misleading like the ADA example I gave previously. And the board members, staff should review the disclosure statements themselves in light of the antifraud rules.

And what about board members? Well, they should provide oversight. Board members often have knowledge and insight into matters which may be relevant to the information being disclosed and may come as a different perspective than staff so they should be should be reviewing it with the determination of whether any information is misleading even if accurate as well. They should review the documents and ask the staff and consultants and improve the distribution of the disclosure statements. So with this in mind let's take a few minutes for Lynn to walk through the timing of disclosure and the disclosure process.

>> As Don was sitting typically with Geos general obligation we do see annual reporting requirement and as Don also said with CFD is our mellow Roos districts, with a developer who is an obligate a person we typically see a semiannual reporting obligation during the time that the developer is an obligate a person which means they are responsible for a good person good portion of the debt service on an annual basis. The typical due dates are January 31 which is about six months after the end of the fiscal year and March 31 the DPC data report mentions over 180 days after the fiscal year ended the information becomes less relevant and more still so we encourage our clients to disclose this soon as those audited financials are available. And again the significant events must be filed within 10 days after the even and we did have a couple questions that I think Don, it might be a good time now to go over them since they are both related to significant events. The first question was, does attend a business rule on material events apply to all issuers even if they don't have recent issues?

>> So I guess what they are saying if there is no bonds issued you wouldn't have to disclose anything but if you have an issue, marketplace you would need to disclose those material events is what I am reading into that.

>> The 10 day business rule applies, by the way, the material even notice requirement changed in 2010. It used to be that all of the significant events that were listed you had to make a determination of whether they were material and then you had to disclose them. In 2010, the rule was amended to split them into two categories so again, some are shown as always being disclosed when they occurred, and others you make the determination if they were material they were disclosed and they were required to be disclosed within the 10 business days.

>> Okay.

>> I'm just looking back at the ruler believe the role prior to 21 2010 was they had to be in a timely manner and there was district 10 business day rule. So if you have an outstanding financing that was issued prior to 2010 you have to locate your continuing disclosure agreement and fill that the procedures set forth in their which would include once the event occurred, that you make a material determination whether the event was material and then disclose it in a timely manner, but the 10 business days limit was not expressly put into the role prior to 2010.

>> Okay then the second question which is pretty significant specific with the issuance of 4.6 million incomes which would be material for our district in parentheses (inaudible) we considered a 10 day type of event requiring disclosure? We have not previously been the party responsible for disclosure for our cops output are responsible for continuing disclosure on the GL.

>> Well, (difeasance) is listed as one of the event notices. So, you would have to fall your continuing disclosure agreement and disclose the (difeasance), if that obligation was issued after the continuing disclosure obligation was put into place. The issuance of new debt of course is going to generally be disclosed when you are entering the public offering the public markets in an official statement but if it is a private placement that is one of the issues that the MSRP and the SEC is trying to address and there is currently no much guidance as to whether you are supposed to disclose and how you disclose a privately placed obligation. So that is an open question at the moment.

>> And CDIAC has said they will post a 2010 material event reference card to the website so that will also be available to the attendees information. Next slide, please. So, this diagram just shows a graphic how the disclosure process works. First, the district prepares the report and again, as Don has mentioned, the district may be hiring a third party consultant to prepare that report, but they should be reviewing it as well as having the board review it and if there is a developer who is required to prepare a report as an obligate a person and a model so. The report. Those would then be reviewed by the board at a minimum and in some cases the districts have the board approve them and review them. Those would then be sent to the dissemination agent. Again the dissemination agent may be the district, third-party or the trustee in many cases as well. And the dissemination agent then distributes the report. Primarily to EMMA, which then hits the bond market. The bond market could not obtain the disclosure information and the dissemination also would send it to the underwriter and if the trustee is not the dissemination would then also send it to the trustee.

With that I will send it back to Don.

>> Great, thank you let's quickly revisit the fact that rule 15c2-12 places the obligation on underwriters of municipal securities to determine whether each issuer or other obligated person has undertaken in a written agreement to provide the continuing disclosure. The SEC has recently made clear that underwriters cannot rely solely on patients by the issuer obligate a person has to its compliance with continuing disclosure, but should obtain evidence reasonably sufficient to determine whether and when such filings and even notices were in fact provided. The issuers of municipal securities will likely see more to diligence by underwriters in this area and may

be requested to take additional steps to ensure compliance especially where an issuer has made previous failures to comply. And this is sort of an important underwriter obligation. I wonder if you have any comments on this slide?

>> I do, I is possible I'd like to maybe just bond to this section toward the end because I think it gets to some of those slides specifically about having best practices in place but I would like to maybe addresses a little later in the presentation.

>> Okay and with that I think we will turn it over to George to talk about the SEC and SEC investigations.

>> Thank you, Don, good morning, all. If you could go to the next slide. I'm going to discuss the SEC's enforcement activity concerning municipal securities and offerings by school districts in particular and this piece of the presentation touches on the stick related to disclosure as opposed to the carrot of having better investor relations and lower cost of funds. Want to begin by briefly touching on the SEC source of authority. Don did a nice job of reviewing met briefly I think it will help you understand the springboard that the SEC uses and particularly see how it performs some of the recent enforcement activity. So there are two general pieces of securities laws at the federal level. The securities act of 1933 and the securities and exchange act of 1934. In short and those are the 33 and 34 acts. Municipal and school districts trees are generally exempt from registration requirements under the 33 act. And the dollar M and 34 act prohibits both the SEC and medicinal securities firm requiring municipal issuers to file disclosures and advance of issuing debt securities. So what is the basis for potential exposure? The basis is the 33 and 34 acts both require you directly to speak. If you do speak you are subject to the antifraud positions, provisions included in the 33 and 34 act which prohibited access, which is prohibiting sale of securities by use of materials which contain materially false information or admit information that is necessary not to make other information which was disclosed not misleading. And what is material, the courts are all over the board on materiality. They essentially use a reasonable investor standard, what would matter to a reasonably investor but as you would suspect that please it very much case to case.

As Don mentioned, the 34 have to do is give the SEC authority to regulate dealers and municipal securities. And it in turn has adopted rule 15c2-12 which effectively which effectively requires the underwriters of most municipal bonds to mandate in their contractual arrangements with the issuers that they provide official statements in, and commit to making ongoing disclosures. So, consequently the school districts are effectively required to make public statements. The statements are subject to the antifraud provisions in the SEC then goes to work. 15c2-12 is the SEC's method of indirect regulation since it cannot directly regulate. As Don described, various pieces of information must be provided both in the official statement annually and in certain event so on 10 days notice and the big plug for the SEC the flight has been those have not failed to comply representations, so what is that? More recently the underwriters have been required to get issuers to make representations in the official statements, but they have not failed to comply with the ongoing disclosure obligations. As was reflected in the slides that Lynn reviewed, many issuers are in fact in noncompliance. But nonetheless not sufficient due diligence there is the risk at least in the absence of sufficient due diligence that they nonetheless make the representation that they have

not failed to comply. That is a big potential pitfall for school districts. It is a big hug for the SEC in policing school district dissemination of information through the antifraud provisions. Because if you make the representation that you have not failed to comply and indeed you have failed to comply you have arguably violated the antifraud provisions of the federal securities laws.

The SEC has been active in this arena. In the spring of this year in April it launched a broad sweep of California municipal issuers studying requests for information to at least 10 municipal issuers that I know of, which means that there are more and it included a number of school districts. I know 100% of (inaudible) have not heard from the SEC but should take comfort from because we do know that a number of participants in California have heard from the SEC this year so if you look at the next slide the seat that the SEC issued in the spring, the requests are essentially identical from one set of requests to the next guilty difference being the substitution of the identifying information for the particular issuers issuances. The documents and information requested include all information related to compliance with annual filing and material even filing obligations and in particular all the documents and other information related to representations and official statements that the issuer has not failed to make required annual filings the requests are very broad, the request asks for open medications not only internal communications related to both ongoing compliance and have not failed to comply representation but also for communications with underwriters and others related to the topic. In addition to asking for documents the issuers were asked to create a chronology of events that led up to the representations in official statements that the issuer had not failed to comply essentially asking the issuers to explain what due diligence they conducted before making a representation. In short responding to the request has been a major undertaking and it is not as simple as just wrapping your files for particular issuance of the tab or out of the shelf because the SEC's specifically seasonal forms of medication including electronic communications of school districts have been required to go back and search through e-mails and other electronic media which is invariably with very little light around an extremely extensive undertaking. I wish I could tell you it's already tens of thousands of dollars because even in the case of small issuers and trying to do it the most efficient way it is often a six-figure number.

So we expect that the sleep that was launched in California earlier this year is likely a sign of things to come as the SEC has hiked its focus on municipal securities and it has some new tools to help it flex its muscles. So the evidence that the SEC is very much focused on municipal securities it created a specialized unit within the division of enforcement now 18 months or so ago at the devoted skip exclusively to medicinal securities and public education funds. The unit has 35 full-time attorneys in it, they are spread across both the national office in DC and a number of the regional offices including and not the SEC San Francisco and Los Angeles regional offices in my view this is a self fulfilling prophecy. Those 35 attorneys that have to have something to show for their efforts, so if you have not heard from the SEC to date there is at least a genuine risk that you will at some point in the future. In addition to staffing up there has been a steady drumbeat of public statements from senior SEC officials emphasizing the municipal enforcement agenda. Lynn Greenberg who is the head of the national securities enforcement unit is announcing one settlement said that they very much intend to be out there sending a message to the municipal and local participants that they need to be taking seriously the obligations under the federal securities laws or there will be consequences. Speaking more recently a public finance conference she said if we find that you clearly

represented (inaudible) we will be holding you accountable in the SEC does not (inaudible) particularly cold, but in addition going after the issuers themselves the SEC has also pursued responsible individuals associated with the issuers.

So it has a removed focus (inaudible) ended as additional tools at its disposal. Some important new tools, Dodd Frank includes a provision that authorizes the SEC to impose monetary penalties for administrative proceedings. In other words, they don't have to go to court and get a judge in a civil action in a federal court to agree that penalties should be imposed. They can now do that through internal administrative proceeding in front of an administrative law judge and they are very much playing on their own home court when they do that, Dodd Frank also includes a whistleblower bounty program to which whistleblowers may receive up to 30% for covers greater than $1 million. Which provides a significant percentage, the SEC has reported since the institution of the program, it receives an average of seven whistleblower tips a day. That is across all subject matter areas, not just municipal securities. But Mark Siegler, who is the deputy chief of the municipal securities enforcement unit has reported memorable whistleblower dispense have contacted the SEC about municipal bond abuses to the SEC attention under the whistleblower program. So that is an example of them are, the more robust tools now at the SEC's disposal complying with the focus on municipal market but I think provides with a big piece of the state that should encourage you to pay close attention to your ongoing disclosure obligations

So what can we be doing about that? I think compliance training is important focus more about just want to observe that we are dealing with some school districts that we represented in connection with the California suite that I described earlier, not all of them, but some of them exhibited a remarkable lack of familiarity with the ongoing disclosure requirements. I'm not critical is that I don't find it terribly surprising given the limited resources and the reality that individuals are wearing many hats. But the lack of familiarity with both of school districts and the individuals at risk. So really attend to compliance training, document retention policies. Most districts have some form of document retention policies. The difficulty is that often does the document retention policies are honored in the breach, which is to say that they are not routinely followed. Until a request comes from the government for information, then the district starts issuing threats document retention policies which means that the documents start disappearing because the policies said they should no longer exists. So that is a good way to get in trouble if you have a document retention policy it is imperative that it be systematically followed. So as not to give the appearance of being manipulated in order to disappear evidence. It's also but in that context to make sure that the appropriate people understand how the IT systems work in advance. Many IT systems have automatic dilution in their backup tape (inaudible) that happen periodically and those need to be disabled as soon as you learn of an SEC investigation otherwise without anybody really paying attention, there is a risk that important evidence will be lost. So, make sure that there is somebody who understands how their systems work.

What happens when you get, when you learn of an investigation if you get a letter from the SEC, what should you do? First, this might seem self-evident but I would encourage you to take the investigation seriously. The SEC may conduct in fact does conduct what it calls informal investigations. Even though they conduct informal investigations it does not conduct casual investigations and you should not be lulled to sleep by that. I have had clients who

referred, they spoke to us on the view that because the informal letters always, the statement saying that it is an informal investigation and they are asking for voluntary cooperation, you know voluntary production of documents and information, that they are free to encourage. That is not the case. It knowing it is a sure ticket to get a formal investigation and a subpoena as opposed to a letter, so take the investigation seriously. From the first moment you learn of the investigation take all appropriate steps to preserve documents. As in many cases, oftentimes individuals and issuers get in trouble not for some underlying substantive problem, but for destroying documents or evidence even if it is completely unintentionally. Because there was not an effort to preserve information.

I would encourage you to retain counsel experienced in dealing with the SEC as we discussed in a bit, they can among other things often negotiate narrowing of documents and information requested by the SEC because they know where the lines can be drawn and they know what the SEC has agreed to in past instances. And the document collection effort is often the most expensive part of the exercise. So, getting those requests narrowed it can result in big savings. Please take care to preserve the attorney-client privilege. As these requests come in a natural thing is to start a hallway conversation, or for the school board to have discussions that are open and not in the presence of counsel. That is not a good idea. It is better for the frank exchange of information that goes on internally to have the protection of the attorney-client privilege. So be careful to include your lawyer in that discussion. Interested quickly and thoroughly the documents often require information or chronologies of events, providing inaccurate information is a sure way to get in trouble with the SEC even if it is a mistake resulting from not having sufficiently thorough investigation.

Among the additional steps to take is to evaluate taxpayer confidentiality. Oftentimes the requests from SEC they will request information about the taxpayer base because if the taxpayer base oftentimes it is the support for the issuance. There is a tension here between your obligation to protect taxpayer confidentiality and to respond to the SEC inquiries. Those things can be put together well, but you have to just be careful there. As I mentioned seek to narrow the scope of the document request because the SEC will almost always agree to narrowing the document request. They start off very probably because they have less than complete information and they are worried about missing things, but through a substantive discussion they will agree to narrow it and finally evaluate whether there is a duty to disclose the investigation itself. That could well, depending on the circumstances amount to a material event that needs to be disclosed in some fashion.

So, the next slide, please. Finally just an overview of what the SEC investigation, first where does it get the information, what causes it to issue a request for information whether it is formal or informal? One source is massive letters as I've mentioned, they also review official statements themselves, they look at pressure points, so if there is an issuer that is in some financial distress, is having some difficulty and that is recorded in the press, the SEC will often follow up on that. My experience for example of how the folks in the municipal securities enforcement unit are all avid readers of the bond to buyer publication and they get a lot of their information of what they should be investigating from the publication. When they commence an investigation it may be just an informal inquiry, it may be a formal investigation. The principal difference is that when it is in the informal inquiry stage, they do not have subpoena power. They are requesting that you respond voluntarily. But, as I mentioned,

they can convert that to a formal investigation reasonably quickly. During the Bush administration for a well, that became more difficult. The SEC commission had to approve the Commandments commencement of a formal investigation. Under the Obama administration that has been pushed in, so that through several layers there probably a handful of people in every regional office who have authority to commence a formal investigation. So, the staff attorney who you may have contacted you about an informal investigation literally only has to walk down the hall and get a signature in order to convert it to a formal investigation. (inaudible). The only difference is that whether it is an informal or formal investigation may inform the judgment as to whether you have a disclosure obligation. Also, it will likely mean an instance of a formal investigation in addition to document request they are also seeking testimony under oath and it will feel more like litigation in many respects just responding to a request for information.

After the conclusion of a formal investigation if the SEC staff believes there's been a violation of federal securities laws it will issue with it calls a Wells notice of what they tentatively found in what they believe should happen but it will give you an opportunity to make a submission in response to a Wells notice to explain from your perspective wider has been no federal securities law violation and in order for an administrative proceeding to impose penalties on you, or a civil litigation to impose penalties on US has to be approved by the commission and the commission will look at the Wells submission of the issuer if there has been no violation as well as the steps click to view. I will tell you that when a Wells notice has gone out the commission is nine times out of 10 if not more going to follow the staff's recommendation. If they don't they will go to an administrative (inaudible) why don't I stop there and turn it over to Frank and he can help explain further having to deal with the circumstances avoid dealing with the circumstances and hopefully never have to deal with an attorney of my specialty.

>> Thank you, George. I think that George had on a key point, the idea is to (inaudible) wise not been subject to and received any of these inquiry letters, so the hope is to at least give you some idea as to best practices and things that districts can do proactively to mitigate the possibility and to hopefully ensure that you do not receive these letters. I think the general practice thus far is that letters have been going to board members and going to their homes, the actual place of residence in so for some districts that we work with, that creates some angst at the staff level but with the policies in place I think we feel this is just an example of things that districts can do to perhaps ensure that this doesn't happen to your district.

On the first slide maybe summarize what I explained earlier in following the points that Don and George have made. The idea here is to perhaps get a policy in place that allows for practice management and approach. One of the things we've seen districts do is to sort of raise the level of awareness to a board level and actually treat this almost as if it were a budget report, an annual report to your board and so some of the things you see on this page, this may be for reaching that this is for district actually did receive one of the inquiry letters and so they wanted to but maybe an additional letter of do diligence on behalf of the district with regard to continuing disclosure. That included the board approved policy, policy stated that the board was aware and would follow a best practices approach ensuring that all future obligations would be met under the continuing disclosure requirements. An annual report actually presented to the board prior to filing Lynn mentioned on average the

dates when these reports are due, the annual reports are due March 1, March 31, April 1, within the window. So perhaps earlier in the calendar year having report dated the board prior to submission to EMMA to provide, designate staff so that there could be training and Don and George had mentioned to provide adequate staff training, these rules are not locked in stone, obviously they change and move with the times. So providing updates and training and having designated staff who at least in the point person for the district with regard to information when it comes to bond counsel, financial adviser or underwriter. Come and of course we will get to this point in a moment, having the right people in place to ensure that the reports are filed. For some districts a sufficient staff resources may be there to file the reports but I think on average different multitasked that you have the and running the school district and keeping the doors open a lot of time it's hard to recall and know exactly for example when a bond insurance has been downgraded or perhaps when accounting policy with regard to investment strategy has changed. A lot of districts I think the general practice is to employ a third-party to file these reports for you and that can take many forms and we will get to that in a moment. The idea here is not to scare you and create additional work for you a truly is within the context of your building program our operational budget. As George had said, there are inquiries today, what does the future hold? I do recall working with a compliance officer whose view was the SEC has spent millions and millions of dollars building the EMMA system they dedicated a significant amount of time and resources, their focus today initially was information gathering but the fear and concern is that their ultimate goal is to get to a state where fines and penalties are sort of Mark a common occurrence. And so we want to avoid that. And I mentioned before where this influence is you is your ability to access capital markets another is the jelly bond passed last week or perhaps a tearing and to meet and operational deficit regardless of what particular bond is of complaints once you have the Scarlet letter that you failed to comply and it's been for a number of reasons that does impact your ability to sell bonds.

We have seen not just anecdotally we have seen recently some investors that actually passed and decided not to participate in a bond sale simply over concerns regarding districts continuing disclosure policy and history. One of the things that was mentioned is the role of five years and generally speaking what you have to discloses your continued disclosure complaints over a five-year window. So going back to annual reports that would start with fiscal 2006, seven. If you've been linked, if you failed a file with, if there's any reason why the district has not been in compliance these are the types of things investors are not, they are paying attention to because as I mentioned earlier given some of the concerns occurring not just in California but nationwide with some municipalities there is a desire and a need to have access to current and update district information and although most of your general obligation bonds ours secured by property taxes Don had made the point that there is a secondary market. There are bonds are traded company may sell a bond today from a new election about three months from now, to three years from now investors are still going to treat your bones and they make those decisions on your financial information regardless of the credit, GRS ERP so there's a desire and need to have the information out there and just to reiterate what I said this impacts base or general fund.

So an example of a policy. This would be again a policy that seeks to address and really sure that a firm approach will be adhered to by the district. So as we mentioned earlier designation as they continued disclosure officer. District generally to CBO, could be someone from your fiscal department, but regardless of whether you employ a

third-party to file we do think it is a best practice to have someone on district staff at least designated as the point person for the district. An annual report to the board, item be, again stating that the district desire to receive the reports prior to submission to EMMA. I did see, the dissemination agent. Many times once you sell the bonds and if you do a general obligation bond you will have a paying or fiscal agent. I think the general practice has been to simply designate the paying fiscal agent does your dissemination agent. However a lot of districts may be misinterpreted or were not aware of what the service would be. Usually what they will do is they will file your report when they send it to them so the onus of responsibility is still in the district. I think Clinton would agree in most people in the financial consulting site would agree that it's probably a better idea to have someone who specializes in the business serving as dissemination agent because that person is going to be able to make you aware and notify you if there's any material that may be out of your control and speaking with rereading upgrade or downgrade the rating agencies decide universally to change their rating scale that would qualify as a material effect. Any fiscal are paying agent, they are not going to be aware of that and they will not be in a position to notify you so I think it's a better idea to have someone who specializes and has the expertise. Then, his training sessions the district reasonably says they have someone in place to adequately respond to and be aware of any changes in requirements under their continued disclosure obligations.

On the next slide this is a sample, can we change to the next slide? This is an example of an assessment. When you talk to continued disclosure you need to understand that it isn't just applicable to about. It is applicable to every bond outstanding as defined by your individual maturities or actual bonds. The common terminology is I choose a number, that is how bonds are identified in the marketplace. The obligation is just to file for series a, it is to file for every (choosit) that is (inaudible) scheduled majority of the bombs, this is an example of the schedule district that was out of complaints and I'm certainly not going to read through the trophies but you do have to have an inventory inventory of all the bonds I think this is where having a professional dissemination will help because they will have thank you slips and he will know which bond to file for, going back to the window, EMMA they became operational on July 1, 2009 prior to EMMA reports were filed on what they called and answers, which stands for the national repository systems from which districts in municipalities could file their continuing disclosure reports, common landing spot for these reports, so prior to July 1, 2009 reports can be filed with Bloomberg. New CDs filed but filed late the duty was actually March 31, and you can actually see reading through some of the red highlighted lines under the current five-year status there's a series of failures whether it was filed late with Bloomberg, and in some instances not filed at all and incidences not filing until well after the point. Another thing I do want to highlight is I think some districts may have been under the impression that you only need to file and get current when you need to sell a bond. There was mentioned earlier. That is no longer the case. You need to be in compliance and current regardless of whether you are selling a bond or not. It would be good to get inventory to get a sense of where you are today should you decide to sell a bond in the future you can showing corrective step in trying to get up-to-date. But the status quo of getting current at the time of a bond sale no longer applies and I think that's what you see with this district here. They were filing reports in 2012 finally in 2012 reports do a couple years earlier. I think the point here is make sure you full assessment is being done fiscal level, paying an agent, or if you have played a third-party to make sure your consultant is giving you all of the data and information on all of your bonds.

And so as Don had mentioned, the equivalent to a prospectus or and offering statement and medicinal world is only called a preliminary official statement. There has always been a section called continuing disclosure in which the district will certify it's been assigned to continued disclosure certificate. It's going to file an annual report and depending on whether the district was compliant or not I would say prior to the current regulatory environment a simple statement to the effect of, in the past the district has failed to file but is now current, that was the status quo. I think everyone on the phone at least on the panel site would agree that that is no longer passes the smell test. So I think what we have shown here is an example of specific identification of reports that were failed or late. So we want to identify not just the fact that the district failed to file, but the actual years. Then you see here in the second body, the second paragraph the district also acknowledging to the community that the district has put the best practices in place in the summarizes what I said earlier. The last section I think the investors do want to see some acknowledgment from the district that a third-party will at least be engaged. He does not have to be someone who is only going to do dissemination services. Again financial advisors are generally a logical choice. But, to have somebody in place that the investor can be confident will ensure that all of your notices are file. Again, the investors understand as well you have many tasks running a school district. Continued disclosure may not be in the top three and of the list but they do want to see somebody who recognizes the importance and makes the district aware of the requirements.

So I just wanted to give you again a sort of practical, and maybe a mark day-to-day perspective of continued disclosure. This policy probably is far-reaching, but it was in response to one of those inquiry letters. No prejudice here to say that you need to administer all of these policies but I think some variation of it would be recommended if only for the fact if you did get a letter today that doesn't mean that you will not get one tomorrow and should you decide to sell bonds in the future I do think it's probably the district's best interest to have this in place so that moving forward you can show a product of supported management your obligations. So that essentially covers my section.

>> Great Frank, thanks. We did have a couple questions and George I think they are from you and we have a respect, request that you speak loudly and clearly is hard to understand, the first question would be what kind of repercussions could be expected of the agency represents that they have failed to comply on and am NOS or later document about later is found to have actually failed to comply with the disclosure requirement at some point of time in the past?

>> First I will try to speak more loudly. So there could be arrange outcomes. The first time that the district or issuer has had such a violation is quite possible that a consent can be negotiated in which the issuer acknowledges that it has committed a violation. And agrees not to do it again and agrees to put certain procedures and policies and practices in place to protect against it. In the future. One of the ways that the SEC agree to that sort of consent in a wide variety of low-level violations it was that it likes to have the hammer, so that if there is a second violation against the background of that sort of consent and agree, then it would drop the hammer more seriously. But the other sorts of violations included visitation of monetary penalties both on the district and on individuals. So there

are for example officials of the city of San Diego who, several years ago were personally required to pay several finds in the range of it. By individual, but ranges $5-$50,000, and that is not money that can be reimbursed by the school district. We don't have insurance for that. And typically there's a lot of legal fields before you get there as well. Legal fees. So I think these sorts of violations of the first instance it's going to be something more akin to a concept of green, more serious to the subject of misrepresentations, I think more serious penalties can be expected in the way of civil fines. The state of New Jersey had a violation, obviously it is a bigger entity, not a school district, but they were municipal securities, and again across the state of New Jersey a lot of money to settle with the SEC.

>> Okay the second question I think also goes to you George, does Dodd Frank allow for administrative procedure sections to be placed on issuers, or does the underwriter DOB party liable for nondisclosure violations

>> not allows them to be disclosed on the issuers as well as employers, employees representatives, officials of the issuer because those are conducted pursuant to the antifraud procedures. The antifraud provisions I should say in the securities

>> okay, great. I'm not getting any more questions so if you have another question, please submit it. But I think in summary what we wanted to convey to you is the disclosure is a very important way to communicate the bond market and that the SEC is looking at it more closely now so it is time to review your disclosure submission and review your practices. Maybe it is time to put into place suggest continuing disclosure policies if you don't have the staff on hand to make sure that the disclosure is taken care of properly, make sure that you engage a third-party or have somebody look it over. Let's see. We do have one more question. Let's see. We have had investors increasingly we have had investors can contact us directly to as questions outside of the continued disclosure process. In order to not give the appearance of insider information, can you recommend what we should say to them? Don, is that something you want to answer?

>> Yeah I think that is what is beyond the scope of this presentation. So I don't know if we want to get into that now, but generally want to make sure that when you're making any kind of statements, that you are in compliance with the antifraud provisions. But also, you do not want to be making statements to some individuals in the condo market generally, some I think the details of that is beyond the scope so whoever has that question, we could discuss it off-line if they want to send the e-mail.

>> Okay thanks with that if we don't have more questions I will turn it back over to Mark Campbell for a few my words and remind you that CDIAC will be putting on the website the 2010 material even reference card.

>> All right when, thanks for limiting me to a few more words that's good. I promise not to take them all up. I do want to recognize and reread the comments of the speakers on the importance of this topic and the fact that it does relate specifically not only to the financing team that to the issuers themselves and at that point cannot be made more strongly. Then our speakers did. I want to refer people to the website where the sites will be posted

very shortly. As well as the transcript. It takes a little while to complete the transcript so that may be delayed but you will have the opportunity to revisit the slides and the audio portion in a written format. With that, the last opportunity to submit any questions. If you do have questions subsequent to the webinar after we do close, go ahead and submit them to CDIAC_education@Treas.CA.gov and we can refer those to our speakers to handle and beyond that I want to thank Lynn, Don, George and Frank for an excellent presentation, thank you to all of the participants who were online today. Finally I'll mention we did have a webinar scheduled for next week addressing capital appreciation bonds. To make sure that you know, we have postponement, and we will pick a date in the near future to conduct that webinar. With that I think we will close. Thank you again, to all the speakers and participants.