

## Electronic Disclosure: 2017 Update

### INTRODUCTION

The California Debt and Investment Advisory Commission (CDIAC) conducted its first review of Electronic Disclosure in 2002. At the time, electronic dissemination of disclosure documents was not the primary method by which issuers fulfilled their disclosure obligations. Since CDIAC's initial report, the development of investor webpages and the Municipal Securities Rulemaking Board's (MSRB) Electronic Municipal Market Access (EMMA) repository have changed how information is disclosed to the market. This issue brief updates the information in CDIAC's *The Role and Use of Repositories in the Disclosure Process for Municipal Securities* (2000) and *Electronic Disclosure* (2002) on electronic disclosure filing and addresses recent trends in electronic disclosure.<sup>1</sup>

### DISCLOSURE REQUIREMENTS UNDER FEDERAL SECURITIES LAWS

The Securities and Exchange Commission (SEC) is a regulatory agency with responsibility for administering the federal securities law. The SEC enforces federal securities

laws to provide protection for investors to ensure that they have access to disclosure of material information and to see that the securities markets operate fairly and honestly.<sup>2</sup> Whenever an issuer releases information which may reasonably be expected to reach investors, it is said to be "speaking to the market" and whenever an issuer speaks to the market those statements are subject to regulation under two anti-fraud provisions of federal securities law. The anti-fraud provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934 prohibit issuers from making material misstatements or material omissions of facts in the offering documents provided to investors.<sup>4</sup>

**INITIAL DISCLOSURE.** Initial disclosure documents consist primarily of preliminary official statements (POSs) and official statements (OSs), as required by Rule 15c2-12.<sup>5</sup> The POS and the OS are the issuer's official statement to the market; that is, the statements about itself upon which it intends others to rely, including statements about its financial and operating data, the securities, sources of repayment and any factors that affect the issuer's ability to meet its debt service. The purpose of the POS and the OS is to provide potential investors with all of the information they would need to decide whether to purchase the securities.

**CONTINUING DISCLOSURE.** Issuers are also obligated to provide continuing disclosure throughout the life of a bond or other security. Continuing disclosure agreements (CDAs), entered into at the time of bond issuance and included with closing transcripts, identify the issuers ongoing disclosure requirements.<sup>6</sup> Rule 15c2-12 prohibits underwriters from purchasing and selling securities unless they obtain reasonable assurances from issuers that they will provide continuing disclosure.<sup>7</sup> Continuing disclosure is comprised of annual reports and material events notices. The annual report consists of information about the issuer's financial condition and operating data. Material events notices are filed as specified events occur, as delineated in Rule 15c2-12.

**VOLUNTARY DISCLOSURE, INVESTOR RELATIONS WEBSITES.** Issuers of municipal securities must provide disclosure as stated in their CDA and required by federal securities laws, but they may also voluntarily provide additional information.<sup>8</sup> To do so, some issuers have developed investor relations webpages to present pertinent information related to their outstanding debt or financial position. Regardless of the medium through which disclosure is made, whether EMMA or a website, it is important for issuers to remember that they are

<sup>1</sup> *The Role and Use of Repositories in the Disclosure Process for Municipal Securities*, CDIAC, November 2000; *The Role and Use of Repositories for Municipal Securities Disclosure*, CDIAC, February 2002.

<sup>2</sup> *The Fundamentals of Municipal Bonds*, The Bond Market Association, Fifth Edition, p.18.

<sup>3</sup> Martha Mahan Haines, SEC, Office of Municipal Securities, Speech Before the Michigan Municipal Finance Officers Association, September 19, 2000, <https://www.sec.gov/news/speech/spch400.htm>

<sup>4</sup> Anti-fraud provisions consist of the Securities Act of 1933, Section 17(a), 15 U.S.C. § 78q-1 and the Securities and Exchange Act of 1934, Rule 10b, 15 U.S.C. § 78j.

<sup>5</sup> 17 C.F.R. § 240.15c2-12.

<sup>6</sup> Government Finance Officers Association, *Debt 101 (Volume 2) – Responsibilities After Bond Issuance*, <https://www.gfoa.org/materials/debt-101>

<sup>7</sup> See *supra* note 3, 17 C.F.R. § 240.15c2-12. Underwriters obtain reasonable assurance through a covenant in the OS known as a Continuing Disclosure Agreement (CDA) or Continuing Disclosure Certificate (CDC).

responsible for the accuracy of their statements made to the market.<sup>9</sup>

The content of the webpage should be tailored to a broader audience than investors. This may include other stakeholders such as insurers and credit enhancers, rating agencies, trustees, liquidity providers, counterparties, members of the issuer's debt financing team, and members of the public. The webpage may include information available on EMMA, including POSs, OSs, and continuing disclosure filings as well as supplementary information, such as interim or pre-audit financial reports and data, even where it is unaudited. This information affords stakeholders a more thorough appreciation of the issuer's financial condition, but the information should be clearly delineated as unaudited. Webpages may also include Independent Registered Municipal Advisor (IRMA) letters, for issuers utilizing the Municipal Advisor Rule's (MA Rule) IRMA Exemption.<sup>10</sup>

An issuer's website should be organized, with investor and stakeholder information displayed on a specific and clearly delineated webpage. Information on that webpage can be arranged so that documents posted in connection with the sale of bonds are clearly identified as such and align easily with information posted on EMMA or information direct-mailed to investors. Issuers may need to obtain permission before posting documents provided to it by third parties. Issuers should carefully consider whether the convenience to investors outweighs the

risk to the issuer including posting a third-party's documentation on its website.

Issuers may realize many benefits as a result of maintaining an investor relations webpage. Timely and comprehensive disclosure may lead to increased liquidity and efficiency and may lower the issuer's borrowing costs.<sup>11</sup> The use of a webpage, together with EMMA where appropriate, may enable the issuer to release information to all investors simultaneously, more quickly, and to a broader audience of interested parties. It may also assist in developing more consistent responses to investor inquiries. Although there are significant benefits to an investor relations webpage, issuers should evaluate all possible disadvantages, such as the time, effort, and cost of designing, periodically reviewing, and maintaining a website. Service providers are developing user-friendly solutions that make disclosure easier and faster.

The issuer should institute a formal process for reviewing and approving information and documents posted on the website, and internal controls should ensure that only complete, accurate, and current information is posted.<sup>12</sup> The site should be periodically reviewed and updated with current reports and information. Any outdated information should be marked as such or placed in an archive. Issuers should also consider including terms of use for the site or a pop-up window or landing page that prompts users to acknowledge the terms of use before they access the site.<sup>13</sup>

Finally, an issuer's investor relations webpage should be the product of a broad-based program. A successful investor relations program will include: (1) a designated and publicized point of contact for investors and stakeholders, (2) an administrative process for determining what information should be disclosed and with what frequency, and (3) appropriate policies and procedures, such as policies requiring periodic review and revision of the webpage by issuer personnel.<sup>14</sup> It is particularly important that issuers coordinate the information disbursed through their webpage and any social media platforms they utilize. Issuers should not share information via social media that does not appear on the webpage.<sup>15</sup> A successful investor relations program consists of a coordinated and efficient dispersal of disclosures and other pertinent information.

#### NEW TRENDS IN ELECTRONIC DISCLOSURE

The SEC has demonstrated a heightened interest in the municipal market leading to an increase in enforcement actions and settlements. In 2010, the SEC announced a new specialized Municipal Securities and Public Pensions unit which has brought greater scrutiny to the municipal market.<sup>16</sup> Since 2013, the SEC has pursued an unprecedented number of enforcement actions against municipal market participants, including issuers. A significant number of these deal with fraudulent, misleading, or insufficient disclosure. One example is the enforcement action against the City of Har-

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<sup>8</sup> Statements from issuers that fall outside of proscribed initial and continuing disclosure requirements may still be subject to federal securities anti-fraud provisions. Issuers should discuss with legal counsel the content and form of information on the website in order to limit exposure to liability under the securities laws. See, e.g., *SEC Interpretation: Use of Electronic Media*, SEC, May 2000, available at <https://www.sec.gov/rules/interp/34-42728.htm>.

<sup>9</sup> SEC Interpretation: Use of Electronic Media, Press Release No. 33-7856 <https://www.sec.gov/rules/interp/34-42728.htm#seciib1>

<sup>10</sup> For more information on the MA Rule and IRMA Exemption, see Issuer Application of the Municipal Advisor Rule's IRMA Exemption, CDIAC, July 2016, available at <http://www.treasurer.ca.gov/cdiac/publications/irma.pdf>.

<sup>11</sup> See MacNaught, Colin, *Enhanced Disclosure Provides an Opportunity for Governments*, Government Finance Review, June 2016, available at <http://www.gfoa.org/sites/default/files/GFR061638.pdf>.

<sup>12</sup> See also *Using Technology for Disclosure*, GFOA, September 2015, <http://www.gfoa.org/using-technology-disclosure>.

<sup>13</sup> *Id.*

<sup>14</sup> *Maintaining an Investors Relations Program*, Government Finance Officers Association (GFOA), October 2010, available at <http://gfoa.org/maintaining-investor-relations-program>.

<sup>15</sup> See *Using Technology for Disclosure*, *supra* note 13.

<sup>16</sup> *SEC Names New Specialized Unit Chiefs and Head of New Office of Market Intelligence*, Press Release, Jan. 13, 2010, available at <https://www.sec.gov/news/press/2010/2010-5.htm>.

risburg in which the SEC charged the city with misleading public statements about its financial condition.<sup>17</sup> The public statements were financial documents, such as an annual budget and mid-year fiscal report, as well as a State of the City address that was posted to its website. In the absence of formally filed disclosure documents, investors were forced to rely on these public reports and statements posted electronically to the issuer's website. This enforcement action emphasizes the importance of meeting formal disclosure requirements and carefully monitoring an investor relations webpage.

Additionally, the SEC instigated the Municipalities Continuing Disclosure Cooperation Initiative (MCDC Initiative) in early 2014.<sup>18</sup> Under the MCDC Initiative, issuers and underwriters self-reported violations of the federal securities laws in connection with material misstatements or omissions in meeting their continuing disclosure obligations. The MCDC Initiative spanned violations occurring within the last five years, and issuers assessing whether to self-report were able to limit their review to disclosure documents electronically filed to EMMA. The results of the MCDC Initiative revealed some unique challenges issuers faced in meeting their disclosure obligations through electronic means. For example, the SEC cited failure to file documents properly on EMMA and failure to properly cross-reference continuing disclosure documents to the original debt issue as violations of securities regulations. Other violations included

filing to an incorrect location or with a third party that, in turn, failed to file on time.<sup>19</sup>

There are significant benefits to electronic disclosure, including the greater ease and speed with which issuers can share their information, and the broader accessibility of that information. However, issuers must remain diligent in confirming that documents are timely and properly filed. Even when using a third party to meet disclosure obligations, issuers should routinely evaluate their EMMA webpage to ensure that all requisite documents are present, in final form, and correctly linked. Issuers can take advantage of some technological tools such as electronic tickler systems, developed to assist issuers in complying with their continuing disclosure obligations. Tickler systems are set up by users to send automatic reminders of important dates and deadlines.

Disclosure practices have evolved as issuers utilize investor relations webpages and EMMA to disseminate information to the market. Public agencies are now regular users of social media and Twitter to communicate with their constituents. With this new trend in communication, public agencies may want to consider addressing this form of communication in their debt management/disclosure policies. While there are no formal best practices at this time, it was noted earlier in this brief that issuers should not share disclosure related information via social media that does not appear on the issuer's webpage. As social media and Twitter

are used more frequently to announce the availability of financial statements, budget documents and government body actions, guidance will be needed for issuers to ensure they employ comprehensive disclosure practices.

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<sup>17</sup> *SEC Charges City of Harrisburg for Fraudulent Public Statements*, SEC Press Release, May 6, 2013, <https://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171514194>.

<sup>18</sup> *SEC Launches Enforcement Cooperation Initiative for Municipal Issuers and Underwriters*, March 10, 2014, available at <https://www.sec.gov/News/PressRelease/Detail/PressRelease/1370541090828>; see also *Municipalities Continuing Disclosure Cooperation Initiative*, SEC, <https://www.sec.gov/divisions/enforce/municipalities-continuing-disclosure-cooperation-initiative.shtml>.

<sup>19</sup> *SEC Charges 71 Municipal Issuers in Muni Bond Disclosure Initiative*, August 24, 2016, <https://www.sec.gov/news/pressrelease/2016-166.html>.