

CDIAC

**CALIFORNIA
DEBT AND
INVESTMENT
ADVISORY
COMMISSION**

SESSION TWO: INITIAL DISCLOSURE

James Wawrzyniak, Jr., Shareholder, Jones Hall

Brian Wong, Debt Manager, City of Sacramento

JH

JONES HALL
www.joneshall.com

City of
SACRAMENTO

INTRODUCTION

- **Overview of initial disclosure policies and practices**
 - ❖ Types of initial disclosure documents and goals when drafting
 - ❖ Participants involved with initial disclosure documents
 - ❖ Requirements under federal securities laws – Rule 10b-5 and Rule 15c2-12
 - ❖ Policies and practices for drafting Preliminary Official Statements
- **City of Sacramento Case Study**
 - ❖ Preparation of the Preliminary Official Statement
 - ❖ Takeaways and Lessons Learned

TYPES OF INITIAL DISCLOSURE DOCUMENTS

- **Preliminary Official Statement (“POS”)** – Used for public offering of securities.
- Private Placement Memorandum or Other Disclosures.
- CDIAC Reports of Preliminary and Final Sale.
- **Not** focusing on Continuing Disclosure, which occurs after the primary issuance of the securities.

GOALS OF INITIAL DISCLOSURE DOCUMENTS

- Legal considerations
 - ❖ Issuer subject to anti-fraud provisions of the federal securities laws.
 - ❖ Underwriter subject to regulatory obligations under federal securities laws, including Rule 15c2-12.
- Credit considerations
 - ❖ Accurately describing security and source of repayment.
 - ❖ Telling the story regarding the issuer and the security.
 - ❖ Ratings, credit enhancements, etc.

PARTICIPANTS

- What is the role of the Local Agency Issuer?
- What is the role of Disclosure Counsel?
- What is the role of the Underwriter?
- What is the role of Bond Counsel?
- What is the role of the Financial Advisor/Municipal Advisor?



Audience Polling

Detailed Directions in Program

Link: *b.Socrative.com/login/student*

Room Name: *CDIAC*

Questions

1. What type of financing transaction(s) have you participated in? (Select all that apply)
2. For public offering transactions, what role did you serve?
3. When was the financing completed?

FEDERAL SECURITIES LAWS

- Securities Act of 1933 – Two requirements
 - ❖ Registration requirement – municipal securities are exempt.
 - ❖ Antifraud requirement – municipal securities are not exempt.
- Securities Act of 1933 – Two standards of antifraud responsibility:
 - ❖ Negligence (§ 17(a))
 - ❖ Recklessness (§ 10(b) – Rule 10b-5)

FEDERAL SECURITIES LAWS

- What are the disclosure requirements stemming from the Federal Securities Laws?
 - ❖ SEC Rule 10b-5
 - ❖ SEC Rule 15c2-12
- Promulgated by the Securities and Exchange Commission (SEC) – based on the SEC’s authority to regulate the purchase and sale of securities.
- Imposes on Issuers initial-disclosure requirements and continuing-disclosure obligations that apply post-issuance.

SEC RULE 10b-5

- **Rule 10b-5:** Unlawful for any person engaged with the purchase or sale of a security to “make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading”
- “**Materiality**” is not defined. Depends on facts and circumstances and usually looked at in hindsight; reasonable investor standard:
“[w]hether or not there is a substantial likelihood that a reasonable investor or prospective investor would consider the information important in deciding whether or not to invest” (*Basic Inc. v. Levinson* (1988) 485 U.S. 224)

SEC RULE 15c2-12

- **Rule 15c2-12** places certain requirements on underwriters of publicly offered municipal securities.
 - ❖ **Directly** governs underwriters but not municipal issuers (except for 10b-5 liability).
 - ❖ **Indirectly** governs municipal issuers engaged in public offerings because underwriters must obtain “deemed final” official statements from issuers *and* must ensure that issuers have undertaken in a written agreement to provide information to the MSRB as required by Rule 15c2-12.
- Recently amended to add two new Listed Event items related to “financial obligations”.

MCDC INITIATIVE / ENFORCEMENT ACTIONS

- Over past several years, there has been a marked increase in SEC activity in the municipal market.
 - ❖ Enforcement actions related to non-compliance with Rule 15c2-12 continuing disclosure undertakings.
 - ❖ Municipalities Continuing Disclosure Cooperation (“**MCDC**”) Initiative.
 - Settlements with self-reporting underwriters (2015).
 - Settlements with self-reporting issuers (2016).
 - Actions against issuers that did not self-report – Beaumont.
- Compliance with continuing disclosure undertakings likely to remain focus of SEC and other regulators.
- Current trend to tighten rules and increase enforcement.

CA Government Code 5852.1

- Effective Jan. 1, 2018, the governing body that authorizes the issuance of bonds—e.g., city council, board of supervisors—must obtain and disclose the following information in a meeting open to the public:
 - Estimated true interest cost of the bonds.
 - Estimated finance charge of the bonds (i.e., total amount paid to for the services of external financing-team members).
 - Estimated amount of project proceeds (net of reserves or capitalized interest).
 - Estimated total debt service (principal and interest) to be paid over the life of the bonds.

WHAT IS AN OFFICIAL STATEMENT?

- The POS is the offering document to investors (like corporate prospectus).
- No "line item" list of required items to be included (unlike corporate prospectus).
- Cover, main body, and all appendices are collectively the “Official Statement.”
- **It is the issuer’s document:** the issuer must take ownership for accuracy and completeness of the information presented.
- Should contain all “material” information regarding the bonds, so investors can make informed decisions.

PREPARING AN OFFICIAL STATEMENT

- **What is the basic structure of an Official Statement?**
 - ❖ Cover and introduction.
 - ❖ Security and source of repayment.
 - ❖ Key credit tables, information about the issuer, bonds, source of repayment.
 - ❖ Improvements being financed (new money); bonds to be refunded (refunding).
 - ❖ Risk Factors.
 - ❖ Federal tax and other legal matters, including form of bond opinion and summary of legal documents.
 - ❖ Continuing disclosure compliance and form of new undertaking.
 - ❖ Demographic and statistical information; DTC information.

PREPARING AN OFFICIAL STATEMENT (Cont'd)

- **What are the sources of Information?**
 - ❖ Prior POS's for similar types of bonds, notes, etc. – need to update!
 - ❖ POS's prepared by other issuers of similar types of bonds, notes, etc.
 - ❖ Publicly available sources regarding issuer demographics, risk factors, DTC.
 - ❖ Federal tax law for the tax matters and form of opinion.
 - ❖ Outside third-party reviewer for continuing-disclosure compliance.
 - ❖ Rule 15c2-12 for the form of the continuing-disclosure undertaking.
- **Who are the participants/contributors of Information?**
 - ❖ Issuer – disclosure coordinator, subject-matter experts.
 - ❖ Disclosure counsel, bond counsel, underwriter, etc.

PREPARING AN OFFICIAL STATEMENT (Cont'd)

- **What are some examples of Material Information?**
 - ❖ Bond terms, security and source(s) of repayment, ratings, bond insurance.
 - ❖ Risks of non-repayment, ability to incur additional debt.
 - ❖ Federal tax treatment and material litigation.
 - ❖ Prior continuing-disclosure compliance.
- **What are examples of different types of bonds/security?**
 - ❖ Utility Bonds – Customers, net revenues, debt-service coverage.
 - ❖ CFD Bonds – Developer’s anticipated build-out, financing, top owners.
 - ❖ General Fund COPs – General fund cash flows, PERS, OPEB, continuity of issuer’s leadership.

ADOPTING POLICIES FOR INITIAL DISCLOSURE

- Adopt or Update a Disclosure Policy, whether Stand-Alone or Part of Debt Management Policy Required by SB 1029 (Cal. Gov. Code, § 8855).
 - ❖ Designate a disclosure coordinator—the person in charge of disclosure.
 - ❖ Describe the process for updating disclosure documents by subject- matter experts, governing body review, and approval procedures.
 - ❖ Follow the disclosure policy or explicitly state reason for waiver.
 - ❖ Review and revise policy over time as needed, given internal changes to staff or outside input and focus (e.g., continuing-disclosure compliance).

ADOPTING POLICIES FOR INITIAL DISCLOSURE

(Cont'd.)

- Provide Periodic Training
 - ❖ Staff training at conferences or at office with disclosure counsel, etc.
 - ❖ Governing body training by staff, disclosure counsel, etc.
 - ❖ Understand role of dissemination agent and capabilities.

CITY OF SACRAMENTO POLICIES

- Debt Management Policy:
 - Identifies authority and responsibility.
 - When the issuance of debt would be appropriate.
 - Debt issuance and structure.
 - Debt administration.
- Policies and Procedures for Use of Special Assessment and Mello-Roos Community Facilities District Financing for Public Facilities.
- Supplemental Policy on Disclosure:
 - Identifies authority and responsibility.
 - Identifies reportable events under SEC Rule 15c2-12.

CITY OF SACRAMENTO CASE STUDY

- \$283.3mm issuance of revenue bonds to finance the renovation of the Convention Center Complex, followed by \$50.5 million issuance of revenue bonds to finance a second convention center ballroom.
- Initial discussion started in 2010-11 and culminated in issuance of bonds in November 2018 and August 2019.
- Scope of project increased from compliance with ADA lawsuit (\$15-20mm) up to full renovation of three facilities of the Convention Center Complex.

Sacramento Convention Center (rendering)



Community Center Theater (rendering)



Memorial Auditorium



CITY OF SACRAMENTO CASE STUDY (Cont'd)

How where the two POS's prepared for these financings?

- ❖ Disclosure Coordinator: Debt Manager is in charge of disclosure, including collection and dissemination of information to/from all participants.
- ❖ City participants: City Treasurer's Office, City Manager's Office, City Attorney's Office, Convention & Cultural Services (CCS), Finance Department, Public Works, Community Development Department, and Utilities Department.
- ❖ Other participants: Lead underwriter, co-underwriters, underwriter's counsel, bond counsel, disclosure counsel, municipal advisor, hotel tax consultant, Sacramento Hotel Association, Visit Sacramento (trade organization), marketing and outreach consultant, special district formation consultant, and litigation counsel.
- ❖ Goal/Objective: Development of the POS focused on three areas: project components, security structure/flow of funds, and projected cashflow and coverage.

CITY OF SACRAMENTO CASE STUDY (Cont'd)

Additional Details

- ❖ Policies and Procedures – how do they inform the POS drafting?
- ❖ Due Diligence – how do you involve all necessary staff, including behind-the-scenes staff, such as engineering and real estate?
- ❖ Presentation to the City Council – how do you ensure City Councilmembers realizes their obligations under the federal securities laws and questions related to disclosure are elicited?
- ❖ Continuing Disclosure – how does the drafting/structure of the POS translate into ongoing continuing disclosure obligations?

CITY OF SACRAMENTO CASE STUDY (Cont'd)

Conclusion

- ❖ What are the takeaways from the case study transactions?
- ❖ What makes good disclosure?
- ❖ Lessons learned/pitfalls to avoid?



Audience Polling

Detailed Directions in Program

Link: *b.Socrative.com/login/student*

Room Name: *CDIAC*

Questions

1. Who has participated in a complex project involving multiple internal and external stakeholders?
2. Who served as the project manager to ensure the project was successfully completed?

TAKE-AWAYS FOR INITIAL DISCLOSURE DOCUMENTS

- Understand what is “material” for particular credit.
- Highlight important or different information up front and repeat.
- Consider whether you have a “story” bond or more straightforward credit.
- Be consistent – tell same stories to governing body in budget documents, to investors in POS, and to rating agency in credit presentation.
- Start from prior POS – but review everything – and update throughout.

TAKE-AWAYS FOR INITIAL DISCLOSURE

DOCUMENTS (Cont'd).

- Involve all members of the team; they each have different viewpoints and expertise.
- There are no “stupid questions” – if you have a question, others probably will too.

CONTACT INFORMATION

**James A. Wawrzyniak,
Jr., *Shareholder***
Jones Hall

Email:

jwawrzyniak@joneshall.com

Telephone: (415) 391-5780

**Brian Wong,
*Debt Manager***
City of Sacramento

Email:

bwong@cityofsacramento.org

Telephone: (916) 808-5811

