Muni News: SEC Adopts Rule 15c2-12 Amendments, Adding Two New Notice Events

On August 20, 2018, the Securities and Exchange Commission (the "SEC" or "Commission") adopted a final rule amending Rule 15c2-12 under the Exchange Act of 1934 (the municipal securities disclosure rule that requires an underwriter to determine, prior to purchasing bonds, that an issuer and/or other obligated person has undertaken to provide continuing disclosure to bondholders in the form of annual financial information and notice of certain listed events via emma.msrb.org).

The final rule follows proposed amendments that were published in March 2017, with some modifications. The proposed amendments were the subject of numerous comments, including four comment letters submitted by the National Association of Bond Lawyers. The adopting release responds to a number of the comments and is available here.

The final rule adopted by the SEC amends the existing list of 14 events that may trigger notice to bondholders. The final rule adds two additional notice events as follows (emphasis added):

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

Once the final rule takes effect in 2019, underwriters will be required to determine that an issuer and/or other obligated person has undertaken to provide notice, within 10 business days, of the incurrence of a material financial obligation (such as a bank loan or direct purchase obligation) as well as 10 business days' notice of certain agreements and events involving financial obligations.

The final rule also adds a definition of "financial obligation" for these purposes:

> "The term financial obligation means a (i) debt obligation; (ii) derivative instrument entered into in connection with, or pledged as security or a source of payment for, an existing or planned debt obligation; or (iii) guarantee of (i) or (ii). The term financial obligation shall not include municipal securities as to which a final official statement has been provided to the Municipal Securities Rulemaking Board consistent with this rule."

The final rule includes a narrower definition of the term "financial obligation" as compared to the March 2017 proposed amendments. The final rule focuses on "debt, debt-like, and debt-related obligations"[1] and not on the "ordinary financial and operating liabilities incurred in the normal course of an issuer's or obligated person's business…."[2]

Notably, the final rule deletes the term "lease" from the proposed definition of financial obligation. Although the term lease is deleted from the definition of financial obligation, the adopting release notes that "the term 'debt obligation' generally should be considered to include lease arrangements entered into by issuers and obligated persons that operate as vehicles to borrow money."[3]

In addition, the final rule deletes the phrase "monetary obligation resulting from a judicial, administrative, or arbitration proceeding" from the proposed definition of financial obligation and narrows the language regarding derivative instruments (to derivatives related to debt) and guarantees (to guarantees of debt or debt-related derivatives) that constitute financial obligations.

The final rule does not define or provide any new guidance on materiality, deferring instead to existing case law: "the Commission continues to believe that materiality determinations should be based on whether the information would be important to the total mix of information made available to the reasonable investor."[4]

The final rule also allows more transition time than did the proposed amendments. The final rule applies to continuing disclosure undertakings entered into on and after the compliance date (180 days following publication of the final rule in the Federal Register). Existing continuing disclosure undertakings are not affected by the final rule.

To prepare for the compliance date, we will be working with clients to prepare draft continuing disclosure undertakings in connection with new bond issues subject to Rule 15c2-12 that include the additional event notices (15) and (16) as well as the new definition of financial obligation. In addition, issuers and other obligated persons should review their continuing disclosure policies and procedures to identify any changes needed to ensure compliance with future undertakings subject to the amended rule.

[1] SEC Release No. 34-83885 (August 20, 2018), at 29.
[2] Id. at 39.
[3] Id. at 43.
[4] Id. at 24.

If you have any questions on these securities law topics of interest to state and municipal bond issuers, please contact any of our public finance attorneys.

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Dated: August 21, 2018

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