



San Diego County Water Authority

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June 11, 2016

Randy Record and
Members of the Board of Directors
Metropolitan Water District of Southern California
P.O. Box 54153
Los Angeles, CA 90065-0153

MEMBER AGENCIES

Carlsbad
Municipal Water District
City of Del Mar
City of Escondido
City of National City
City of Oceanside
City of Poway
City of San Diego
Fallbrook
Public Utility District
Helix Water District
Lakeside Water District
Olivenhain
Municipal Water District
Otay Water District
Padre Dam
Municipal Water District
Camp Pendleton
Marine Corps Base
Rainbow
Municipal Water District
Ramona
Municipal Water District
Rincon del Diablo
Municipal Water District
San Dieguito Water District
Santa Fe Irrigation District
South Bay Irrigation District
Vallecitos Water District
Valley Center
Municipal Water District
Vista Irrigation District
Yuima
Municipal Water District
OTHER
REPRESENTATIVE
County of San Diego

RE: Board Memo 8-2: Approve and Authorize Appendix A for use in the issuance and remarketing of Metropolitan's bonds - **REQUEST TO TABLE OR IN ALTERNATIVE, OPPOSE**

Dear Chairman Record and Members of the Board:

Since Board Memo 8-3, authorizing the issuance of up to \$175 million of Subordinate Water Revenue Bonds, has been pulled from this month's board agenda, this letter will address only Board Memo 8-2, relating to proposed changes in MWD's procedures for board review of bond offering statements in connection with sale of municipal bonds. We will provide detailed comments on the *Board Distribution 5/31/16 Draft Appendix A*, prior to the proposed bond sale being brought back to the Board of Directors for approval. We request that board action approving the "biannual" generic Appendix A attached to Board Memo 8-2 be tabled pending the proposed financing being brought back to the Board.

Board Memo 8-2 describes a *material change* in MWD's longstanding practice of providing a draft Appendix A for board review *each time bonds are proposed to be sold, or remarketed*, prior to finalizing bond offering statements that include Appendix A. According to Board Memo 8-2, MWD staff now plans to limit the Board to a "biannual" review of Appendix A.ⁱ

Copies of the "updated" Disclosure Procedures dated June 1, 2016 and the prior, undated procedures are included as Attachments 1 and 2 to this letter, respectively, so that the Board may see the proposed changes, in particular, the addition of a new paragraph 2, "Preparation of Disclosure Documents related to Debt."ⁱⁱ We OPPOSE this new policy and procedure; in fact, we believe federal law relating to the individual fiduciary responsibilities every MWD Board member has in connection with the sale of MWD bonds cannot be "trumped" by a MWD Board vote, let alone a new procedure developed by staff.

Our staff has provided us with a helpful article we are also taking the liberty of attaching for the

benefit of our fellow MWD Board members, *Disclosure Obligations of Municipal Issuers: The SEC Enforcement Perspective*.ⁱⁱⁱ Among other things, the article notes:

- The SEC will hold public officials personally accountable and seek enforcement sanctions when it determines that an issuer has failed to disclose material information in violation of the federal securities laws.
- While it is important for a municipal issuer to demonstrate that it has written policies and procedures designed to ensure that material information is disclosed, compliance with such a disclosure checklist is not "the goal unto itself." Rather, it is essential that there are substantive discussions relating to the larger issues facing the agency including disclosure of "bad news."
- While it is important to retain qualified professional advisors, the SEC requires that public officials read and understand the representations being made in offering statements before they vote to approve them.

In short, we believe the changes staff has made to MWD's disclosure procedures are moving in the wrong direction; rather than enhancing review, the changes would reduce the opportunities for, and level of Board review associated with the issuance and sale of bonds.^{iv} We recommend that the staff bring back a complete report on MWD's disclosure procedures, including recommendations by its professional advisors, so that the Board can weigh in on what the process should be before it is finalized.

The Water Authority has expressed a number of concerns about the disclosures in MWD's Draft Appendix A for many years. That alone is a good reason to enhance, not diminish the MWD Board's review. It is important that we express our concerns, and it is important for the rest of the MWD Board to be aware of those concerns, whether or not individual board members agree that additional or different disclosures should be made. Recent SEC actions and other news involving the Westlands Water District also suggest that greater, rather than lesser Board oversight is not only beneficial, but essential.

We appreciate your consideration of these issues and look forward to the discussion at next week's board meeting. We hope the Board will table this item and have a full discussion; if not, we must OPPOSE the action for the reasons stated above.

Sincerely,



Michael T. Hogan
Director



Keith Lewinger
Director



Fern Steiner
Director



Yen C. Tu
Director

Attachments:

1. MWD "Disclosure Procedures" dated June 1, 2016
2. MWD "Disclosure Procedures" undated
3. Disclosure Obligations of Municipal Issuers: The SEC Enforcement Perspective, May 2008, prepared by K&L|Gates

ⁱ Attachment 1 and Board Memo 8-2 say different things about what updates staff would provide to the board between biannual updates. The Disclosure Procedures (Attachment 1), which presumably are provided to the SEC and investors, states that "interim" updates will be provided to the Board, described as being those that are needed to "capture key shifts in Metropolitan's financial cycle" (page 2, paragraph 2(b)). Board Memo 8-2 states that "material updates" will be provided for bond sales occurring between the proposed biannual reviews. Without trying to interpret what the language means in either context, we believe the only correct approach is to provide the entire Draft Appendix A to directors as staff has historically done.

ⁱⁱ Staff is also recommending changes relating to the voluntary disclosure of bank loans (Attachment 1, paragraph 6 compared to Attachment 2, paragraph 5), for which an explanation should be provided.

ⁱⁱⁱ There is a wealth of information available about the SEC's continuing focus on the municipal securities market; however, this 2008 article provides an excellent overview of the issues and remains current.

^{iv} No matter what the outcome of the board vote on Board Memo 8-2, the Water Authority's representatives request that staff continue to provide copies of the Draft Appendix A prior to each and every proposed bond sale and remarketing.



THE METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA
DISCLOSURE PROCEDURES
INCLUDING
COMPLIANCE WITH SEC RULE 15c2-12
Dated: June 1, 2016

Metropolitan is committed to providing comprehensive and timely disclosure of its financial condition and relevant events to its members, bondholders and other participants in financial transactions, the rating agencies and the municipal finance industry. To that end, and to assure continuing compliance with SEC Rule 15c2-12, Metropolitan has formally assembled disclosure procedures in this document. The purpose of these Disclosure Procedures is to set forth internal processes, procedures and controls for the preparation of Disclosure Documents. Notwithstanding the foregoing, failure to comply with these Disclosure Procedures shall not create any presumption that Metropolitan's disclosure is inadequate. Further, the failure to comply with these Disclosure Procedures shall not affect the authorization or the validity or enforceability of any bonds, notes or other indebtedness that are otherwise issued by Metropolitan in accordance with law.

1. External Communications. The Deputy General Manager for External Affairs is responsible for speaking with the media on behalf of Metropolitan. All communications on financial matters shall be coordinated with the Office of the Chief Financial Officer.
2. Preparation of Disclosure Documents related to Debt. Public debt issuances generally involve the preparation of two offering documents (e.g., official statements), one in preliminary form and one in final form. In some instances, only one offering document in final form is prepared for a debt issuance. Metropolitan may be required to supplement or amend the offering statement at any time between the time of posting of the preliminary offering document until 25 days after the "end of the underwriting period" (usually the closing date for the bond issuance). In addition, offering documents are periodically prepared for remarketings of outstanding debt.

The standard for accuracy in disclosure documents is that there shall be no untrue statement of material fact and no omission of a statement necessary to make the statements made, in light of the circumstances under which they were made, not misleading. All participants in the process should keep this standard in mind at all times when preparing or reviewing any Disclosure Document. References in these Disclosure Policies to accuracy or material accuracy refer to this standard. Any questions about this standard should be directed to the Office of the General Counsel.

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- (a) Offering Statements – Bond Counsel prepares the preliminary\final offering statement; the General Counsel and the CFO’s Office prepare Appendix A (see (b) below); the Controller’s Office provides the most recent Auditors Report and Basic Financial Statements (typically found in Appendix B) and the CFOs office oversees the preparation of The Selected Demographic and Economic Information for Metropolitan’s Service Area (typically found in Appendix E). Co-Bond counsel, underwriters, underwriter’s counsel and Metropolitan’s financial advisor review the documents, provide comments and sign off, before posting to EMMA.
- (b) Appendix A – Appendix A is updated biannually, unless additional updates are needed, to capture key shifts in Metropolitan’s financial cycle, for example following the close of the fiscal year and after closure of the semi-annual accounting period. The General Counsel prepares Appendix A with assistance from the CFOs Office, who prepares the financial sections. Finance, Water Resource Management, Water System Operations, Engineering Services and Human Resources staffs provide information and updates to the Office of the General Counsel to update Appendix A. Metropolitan’s Office of the General Auditor reviews and agrees tables, statistics and financial data. Bond counsel, underwriters, underwriters counsel and Metropolitan’s financial advisor review Appendix A and provide comments. Before posting to EMMA, a draft of Appendix A is provided to senior officers and group managers, with oversight and responsibility for areas discussed in Appendix A, for review and signoff and to the Board for review and approval. Interim updates to Appendix A between biannual updates are provided to the Board for review and comment and to those senior officers and group managers with responsibility for the updates, for signoff. In addition, underwriters, underwriters counsel and bond counsel must sign off before posting to EMMA.
3. Annual Report Procedures. Metropolitan’s Continuing Disclosure Undertakings (CDU) require filing of annual financial information reports with respect to each fiscal year of Metropolitan by no later than 180 days after the end of the respective fiscal year (or no later than **December 27** each year), to the Municipal Securities Rulemaking Board’s Electronic Municipal Market Access system (EMMA). Both Water Revenue Bonds and General Obligation Bonds are subject to filing requirements.

Annual financial information reports are prepared under the supervision of the Office of the Chief Financial Officer. The Legal Department prepares the draft report for review and completion by the Office of the Chief Financial Officer. Financial statements are provided by the Controller. The financial information required by the CDUs to be included in the annual financial information reports is on file with the Office of the Chief Financial Officer (ATTACHMENT A), along with the sources for such information.

4. Amendments to CDU. If an amendment changes the type of financial information or operating data provided in the CDU, the first annual financial information provided thereafter shall include

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a narrative explanation of the reasons for the amendment and the impact of the change. (see CDU §4.2c) If amendment changes accounting principles followed in preparing financial statements, the annual financial information for the year in which the change is made shall present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles. Such comparison shall include a qualitative and quantitative discussion of the differences in the accounting principles and the impact of the change in accounting principles on the presentation of the financial information. Notice of such amendment shall be posted on EMMA. (see CDU §4.2d)

5. Event Notice Requirements. Metropolitan will provide, or cause to be provided, to EMMA, notice for all listed events, as required by CDUs (see table below). For bonds issued **on or after December 1, 2010**, notices must be filed within ten business days of occurrence. For bonds issued **before December 1, 2010**, notices must be filed “in a timely manner.” Metropolitan will strive to provide notice within ten business days of occurrence, regardless of the date of issuance of the bonds.

The Office of the Chief Financial Officer is responsible for monitoring these events and providing event notices, as required. Event notices are prepared under the supervision of the Office of the Chief Financial Officer. The Legal Department prepares the draft report for review by the Office of the Chief Financial Officer.

For events that must be only be disclosed if material, a materiality determination will be made by the Office of the Chief Financial Officer, with advice from the executive officer(s) with oversight and management authority for the subject matter, and with advice and concurrence by the Legal Department (which may consult outside bond counsel).

The table below shows the events that require notice filings and the sources for such information. *Notice of the types of events in italics below are not required for bonds issued before December 1, 2010, but may be provided.*

Event	Materiality Determination Required?
Principal and interest payment delinquencies	n/a
Non-payment related defaults, if material	n/a
Unscheduled draws on debt service reserves reflecting financial difficulty	n/a
Unscheduled draws on credit enhancements reflecting financial difficulty	n/a
Substitution of credit or liquidity providers, or their failure to perform	n/a
Adverse tax opinions, the issuance by the IRS of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701 TEB) or other material notices of determination with respect to the tax status of the security or other material events affecting the tax status of the security	n/a (for adverse tax opinions and the issuance by the IRS of proposed or final determination of taxability)
Modifications to rights of security holders, if material	

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Event	Responsibility for Determining Materiality
Bond calls, if material, and tender offers	n/a (for tender offers)
Defeasances	n/a
Release, substitution, or sale of property securing repayment of the securities, if material	yes
Rating changes	n/a
<i>Bankruptcy, insolvency, receivership or similar event of Metropolitan</i>	n/a
<i>The consummation of a merger, consolidation, or acquisition involving Metropolitan or the sale of all or substantially all of the assets of Metropolitan, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material</i>	yes
<i>Appointment of a successor or additional trustee or the change of name of a trustee, if material</i>	yes
Failure to provide in a timely manner notice to provide required annual financial information by the date specified in the CDU	n/a

6. Voluntary Disclosure of Bank Loans.

With the happening of the following events, Metropolitan will assess and decide upon a course of action including those listed below.

Event:

- Revolving credit agreements
- Bank loans for the purpose of paying purchase price, principal of or interest on water revenue bonds
- Draws
- Substitution of lender or replacement of agreement
- Material amendments
- Extension or renewal
- Expiration, suspension or termination

Action:

- Posting of an event notice to EMMA, either to all outstanding bonds, or to those affected
- Posting of redacted document or notice by Metropolitan to Financial Information-Financial Reports page of Metropolitan's Website or EMMA
- Posting of redacted document or notice by banks to EMMA
- Posting of an updated disclosure to EMMA disclosing the named event

The Office of the Chief Financial Officer is responsible for monitoring these events and providing event notices and updated disclosure, as required. Metropolitan's Legal Department prepares draft notices for review by the Office of the Chief Financial Officer, in consultation with bond counsel, as required.

7. [RESERVED]

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8. Web Posting Procedures. The following documents are posted on Metropolitan’s Finance web page, as soon as is practicable after publishing, and updated as more recent information becomes available.

Document/Information	Responsibility for Preparing and Posting
Latest Official Statement—Water Revenue Bonds	Office of the Chief Financial Officer (CFO)
Latest Official Statement—General Obligation Bonds	Office of the CFO
Annual audited financial statements	Office of the Controller
Quarterly financial statements	Office of the Controller
CAFR	
Budget	Budget and Rates Section
Water rates	Budget and Rates Section
Monthly Treasurer’s report	Treasury and Debt Management Section
Quarterly swap report	Treasury and Debt Management Section

9. Request for Documents. Requests for copies of Finance documents are routed through the Office of the Chief Financial Officer and must be coordinated with the Legal Department for compliance with the Public Records Act.

ATTACHMENT A

<u>Financial Information to be Included in Annual Financial Information Reports</u> <u>(as required under CDUs)</u>	
<u>Required Document/Information</u>	<u>Source of Information</u>
Draft CDU Report	CDUs Rev Bonds: S:\FINANCE FOLDERS\Disclosure\2010 filing Rev bonds.docx GO Bonds: S:\FINANCE FOLDERS\Disclosure\2010 filing GO bonds.docx
List of outstanding bonds subject to CDU	App A, Treasurer or Controller
<p>Annual Financial Information:</p> <p>WATER REVENUE BONDS</p> <ul style="list-style-type: none"> • the table under “OPERATING REVENUES, DEBT SERVICE AND INVESTMENT PORTFOLIO – Debt Service Requirements” in the forepart of the OS; • under “METROPOLITAN’S WATER SUPPLY” in App. A, the table “Metropolitan’s Water Storage Capacity and Water in Storage”; • under “METROPOLITAN REVENUES” in App. A, the tables “Summary of Receipts by Source”, “Summary of Water Sold and Water Sales”, “Summary of Water Rates”, and “Ten Largest Water Customers”; the water standby charge for the fiscal year; revenues for the fiscal year resulting from wheeling and exchange transactions; and the total power revenues for the fiscal year; • under “METROPOLITAN REVENUES – Investment of Moneys in Funds and Accounts” in Appendix A to the Official Statement, the total market value of all Metropolitan funds, earnings on investments and the minimum month-end balance of Metropolitan’s investment portfolio; • under “METROPOLITAN EXPENDITURES” in App. A, the table “Summary of Expenditures”; outstanding indebtedness (including revenue bonds, subordinate revenue obligations, variable rate and swap obligations, other revenue obligations and general obligation bonds), the payment obligation under the State Water Contract, a description of other long term commitments, and the information described under the sub-caption “Defined Benefit Pension Plan”; • under “HISTORICAL AND PROJECTED REVENUES AND EXPENSES” in App. A, historical revenues and expenses for the then immediately past fiscal year, as presented in the table “Historical and Projected Revenues and Expenses”; • under “MANAGEMENT’S DISCUSSION OF HISTORICAL AND PROJECTED REVENUES AND EXPENSES” in App. A to the Official Statement, the percentage of operation and maintenance expenses to total costs; • under “POWER SOURCES AND COSTS” in App. A to the Official Statement, the expenses for electric power, for so long as such information shall be deemed to be material by Metropolitan; • and (B) the information regarding amendments to this Undertaking required pursuant to Sections 4.2(c) and (d) of this Undertaking. Annual Financial Information shall include Audited Financial Statements, if available, or Unaudited Financial Statements. 	<p>Rev. Bond Official Statement and App A, containing information for applicable fiscal year</p> <p>If no OS has been issued since prior July 1, expand report to provide the required information (see Annual Information supplement for GO Bonds listed below)</p>

List of financial information required by Metropolitan’s Continuing Disclosure Undertakings to be included in annual financial information reports.
Filed with the Office of the Chief Financial Officer – June 1, 2016

ATTACHMENT A

<u>Financial Information to be Included in Annual Financial Information Reports</u> <u>(as required under CDUs)</u>	
<u>Required Document/Information</u>	<u>Source of Information</u>
<p><u>Annual Financial Information:</u></p> <p>GENERAL OBLIGATION BONDS</p> <ul style="list-style-type: none"> • under “METROPOLITAN TAX REVENUES” in the forepart of the OS, the tables entitled “Summary of Property Tax Levies”, “Summary of Assessed Valuations and Tax Rates”, “Assessed Valuation Within Metropolitan’s Service Area (By Counties)” and “Debt Service Requirements for General Obligation Bonds”; • under “METROPOLITAN REVENUES” in App. A, the tables entitled “Summary of Receipts by Source”, “Summary of Water Sold and Water Sales”, “Summary of Water Rates”, and “Ten Largest Water Customers”; the water standby charge for the fiscal year; revenues for the fiscal year resulting from wheeling and exchange transactions; the total power revenues for the fiscal year; and the unrestricted reserve balances available to Metropolitan for the fiscal year; • under “METROPOLITAN REVENUES – Investment of Moneys in Funds and Accounts” in Appendix A to the Official Statement, the total market value of all Metropolitan funds, earnings on investments and the minimum month-end balance of Metropolitan’s investment portfolio • under “METROPOLITAN EXPENDITURES” in App. A, the table entitled “Summary of Expenditures”; outstanding indebtedness (including revenue bonds, subordinate revenue obligations, variable rate and swap obligations, other revenue obligations and general obligation bonds), the payment obligation under the State Water Contract, a description of other long term commitments, and the information described under the sub-caption “Defined Benefit Pension Plan”; • under “HISTORICAL AND PROJECTED REVENUES AND EXPENSES” in App. A, historical revenues and expenses for the then immediately past fiscal year, as presented in the table entitled “Historical and Projected Revenues and Expenses”; • under “MANAGEMENT’S DISCUSSION OF HISTORICAL AND PROJECTED REVENUES AND EXPENSES” in App. A, the percentage of operation and maintenance expenses to total costs; • under “POWER SOURCES AND COSTS” in App. A, the expenses for electric power, for so long as such information shall be deemed to be material by Metropolitan 	<p>GO Bond Official Statement and App A, containing information for applicable fiscal year</p> <p>If no GO Bond OS has been issued since prior July 1, use Rev. Bond Official Statement and App A, containing information for applicable fiscal year, and statistical tables from CAFR See S:\FINANCE FOLDERS\Disclosure\2008 filing GO bonds.docx, and S:\FINANCE FOLDERS\Disclosure\2008 filing GO bonds\2008 Annual Financial Info Supp GO.docx</p> <p>If no OS has been issued since prior July 1, expand report to provide the required information</p>
<p>ANY AMENDMENT TO CDU</p> <p>If amendment changes the type of financial information or operating data, include a narrative explanation of the reasons for the amendment and the impact of the change. (see CDU §4.2c)</p> <p>If amendment changes accounting principles, present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles (see CDU §4.2d)</p>	<p>Legal—determine if CDU has been amended</p> <p>Controller, Auditor—provide notice of any changes in accounting principles</p>
<p>ANNUAL FINANCIAL STATEMENTS</p> <p>Audited financial statements must be filed, if available. If not, unaudited annual financial statements must be filed with the annual report and audited statements must be filed when available</p>	<p>Controller</p>

List of financial information required by Metropolitan’s Continuing Disclosure Undertakings to be included in annual financial information reports.
Filed with the Office of the Chief Financial Officer – June 1, 2016



THE METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA
DISCLOSURE PROCEDURES
FOR
COMPLIANCE WITH SEC RULE 15c2-12

Metropolitan is committed to providing comprehensive and timely disclosure of its financial condition and relevant events to its members, bondholders and other participants in financial transactions, the rating agencies and the municipal finance industry. To that end, and to assure continuing compliance with SEC Rule 15c2-12, Metropolitan has formally assembled disclosure procedures in the following document.

1. External Communications. The Deputy General Manager for External Affairs is responsible for speaking with the media on behalf of Metropolitan. All communications on financial matters shall be coordinated with the Office of the Chief Financial Officer.
2. Annual Report Procedures. Metropolitan's Continuing Disclosure Undertakings (CDU) require filing of annual financial information reports with respect to each fiscal year of Metropolitan by no later than 180 days after the end of the respective fiscal year (or no later than **December 27** each year), to the Municipal Securities Rulemaking Board's Electronic Municipal Market Access system (EMMA). Both Water Revenue Bonds and General Obligation Bonds are subject to filing requirements.

Annual financial information reports are prepared under the supervision of the Office of the Chief Financial Officer. The Legal Department prepares the draft report for review and completion by the Office of the Chief Financial Officer. Financial statements are provided by the Controller. The financial information required by the CDUs to be included in the annual financial information reports is on file with the Office of the Chief Financial Officer, along with the sources for such information.

3. Event Notice Requirements. Metropolitan will provide, or cause to be provided, to EMMA, notice for all listed events, as required by CDUs (see table below). For bonds issued **on or after December 1, 2010**, notices must be filed within ten business days of occurrence. For bonds issued **before December 1, 2010**, notices must be filed "in a timely manner." Metropolitan will strive to provide notice within ten business days of occurrence, regardless of the date of issuance of the bonds.

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The Office of the Chief Financial Officer is responsible for monitoring these events and providing event notices, as required. Event notices are prepared under the supervision of the Office of the Chief Financial Officer. The Legal Department prepares the draft report for review by the Office of the Chief Financial Officer.

For events that must be only be disclosed if material, a materiality determination will be made by the Office of the Chief Financial Officer, with advice from the executive officer(s) with oversight and management authority for the subject matter, and with advice and concurrence by the Legal Department (which may consult outside bond counsel).

The table below shows the events that require notice filings and the sources for such information. *Notice of the types of events in italics below are not required for bonds issued before December 1, 2010, but may be provided.*

Event	Materiality Determination Required?
Principal and interest payment delinquencies	n/a
Non-payment related defaults, if material	n/a
Unscheduled draws on debt service reserves reflecting financial difficulty	n/a
Unscheduled draws on credit enhancements reflecting financial difficulty	n/a
Substitution of credit or liquidity providers, or their failure to perform	n/a
Adverse tax opinions, the issuance by the IRS of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701 TEB) or other material notices of determination with respect to the tax status of the security or other material events affecting the tax status of the security	n/a (for adverse tax opinions and the issuance by the IRS of proposed or final determination of taxability)
Modifications to rights of security holders, if material	

Event	Responsibility for Determining Materiality
Bond calls, if material, and tender offers	n/a (for tender offers)
Defeasances	n/a
Release, substitution, or sale of property securing repayment of the securities, if material	yes
Rating changes	n/a
<i>Bankruptcy, insolvency, receivership or similar event of Metropolitan</i>	n/a
<i>The consummation of a merger, consolidation, or acquisition involving Metropolitan or the sale of all or substantially all of the assets of Metropolitan, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material</i>	yes
<i>Appointment of a successor or additional trustee or the change of name of a trustee, if material</i>	yes
Failure to provide in a timely manner notice to provide required annual financial information by the date specified in the CDU	n/a

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4. Amendments to CDU. If an amendment changes the type of financial information or operating data provided in the CDU, the first annual financial information provided thereafter shall include a narrative explanation of the reasons for the amendment and the impact of the change. (see CDU §4.2c) If amendment changes accounting principles followed in preparing financial statements, the annual financial information for the year in which the change is made shall present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles. Such comparison shall include a qualitative and quantitative discussion of the differences in the accounting principles and the impact of the change in accounting principles on the presentation of the financial information. Notice of such amendment shall be posted on EMMA. (see CDU §4.2d)
5. Voluntary Disclosure of Bank Loans. Metropolitan will voluntarily post redacted copies of its revolving credit agreement(s) and any other bank loans for the purpose of paying the purchase price, principal of or interest on water revenue bonds on EMMA. In addition, Metropolitan will voluntarily provide notice of the following events with respect to such agreement(s) and loans:
- Draws
 - Substitution of lender or replacement of agreement
 - Material amendments
 - Extension or renewal
 - Expiration, suspension or termination

The Office of the Chief Financial Officer is responsible for monitoring these events and providing event notices, as required. Event notices are prepared under the supervision of the Office of the Chief Financial Officer. The Legal Department prepares the draft notice for review by the Office of the Chief Financial Officer.

6. Web Posting Procedures. The following documents are posted on Metropolitan's Finance web page, as soon as is practicable after publishing, and updated as more recent information becomes available.

Document/Information	Responsibility for Monitoring	Responsibility for Posting
Latest Official Statement—Water Revenue Bonds	Office of the Chief Financial Officer	Office of the CFO
Latest Official Statement—General Obligation Bonds	Financial Officer (CFO)	Office of the CFO
Annual audited financial statements	Office of the CFO	Office of the CFO
Quarterly financial statements	Office of the CFO	Office of the CFO
CAFR	Office of the CFO	Office of the CFO
Budget	Office of the CFO	Office of the CFO

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Document/Information	Responsibility for Monitoring	Responsibility for Posting
Water rates	Office of the CFO	Office of the CFO
Monthly Treasurer's report	Treasurer	Treasurer
Monthly swap report	Office of the CFO	Office of the CFO

7. Request for Documents. Requests for copies of Finance documents are routed through the Office of the Chief Financial Officer and must be coordinated with the Legal Department for compliance with the Public Records Act.

<u>Financial Information to be Included in Annual Financial Information Reports</u> <u>(as required under CDUs)</u>	
<u>Required Document/Information</u>	<u>Source of Information</u>
Draft CDU Report	CDUs Rev Bonds: S:\FINANCE FOLDERS\Disclosure\2010 filing Rev bonds.docx GO Bonds: S:\FINANCE FOLDERS\Disclosure\2010 filing GO bonds.docx
List of outstanding bonds subject to CDU	App A, Treasurer or Controller
<p>Annual Financial Information:</p> <p>WATER REVENUE BONDS</p> <ul style="list-style-type: none"> • the table under “OPERATING REVENUES, DEBT SERVICE AND INVESTMENT PORTFOLIO – Debt Service Requirements” in the forepart of the OS; • under “METROPOLITAN’S WATER SUPPLY” in App. A, the table “Metropolitan’s Water Storage Capacity and Water in Storage”; • under “METROPOLITAN REVENUES” in App. A, the tables “Summary of Receipts by Source”, “Summary of Water Sold and Water Sales”, “Summary of Water Rates”, and “Ten Largest Water Customers”; the water standby charge for the fiscal year; revenues for the fiscal year resulting from wheeling and exchange transactions; and the total power revenues for the fiscal year; • under “METROPOLITAN REVENUES – Investment of Moneys in Funds and Accounts” in Appendix A to the Official Statement, the total market value of all Metropolitan funds, earnings on investments and the minimum month-end balance of Metropolitan’s investment portfolio; • under “METROPOLITAN EXPENDITURES” in App. A, the table “Summary of Expenditures”; outstanding indebtedness (including revenue bonds, subordinate revenue obligations, variable rate and swap obligations, other revenue obligations and general obligation bonds), the payment obligation under the State Water Contract, a description of other long term commitments, and the information described under the sub-caption “Defined Benefit Pension Plan”; • under “HISTORICAL AND PROJECTED REVENUES AND EXPENSES” in App. A, historical revenues and expenses for the then immediately past fiscal year, as presented in the table “Historical and Projected Revenues and Expenses”; • under “MANAGEMENT’S DISCUSSION OF HISTORICAL AND PROJECTED REVENUES AND EXPENSES” in App. A to the Official Statement, the percentage of operation and maintenance expenses to total costs; • under “POWER SOURCES AND COSTS” in App. A to the Official Statement, the expenses for electric power, for so long as such information shall be deemed to be material by Metropolitan; • and (B) the information regarding amendments to this Undertaking required pursuant to Sections 4.2(c) and (d) of this Undertaking. Annual Financial Information shall include Audited Financial Statements, if available, or Unaudited Financial Statements. 	<p>Rev. Bond Official Statement and App A, containing information for applicable fiscal year</p> <p>If no OS has been issued since prior July 1, expand report to provide the required information (see Annual Information supplement for GO Bonds listed below)</p>

List of financial information required by Metropolitan’s Continuing Disclosure Undertakings
to be included in annual financial information reports.
Filed with the Office of the Chief Financial Officer – December 14, 2015

<u>Financial Information to be Included in Annual Financial Information Reports</u> <u>(as required under CDUs)</u>	
<u>Required Document/Information</u>	<u>Source of Information</u>
<p><u>Annual Financial Information:</u></p> <p>GENERAL OBLIGATION BONDS</p> <ul style="list-style-type: none"> • under “METROPOLITAN TAX REVENUES” in the forepart of the OS, the tables entitled “Summary of Property Tax Levies”, “Summary of Assessed Valuations and Tax Rates”, “Assessed Valuation Within Metropolitan’s Service Area (By Counties)” and “Debt Service Requirements for General Obligation Bonds”; • under “METROPOLITAN REVENUES” in App. A, the tables entitled “Summary of Receipts by Source”, “Summary of Water Sold and Water Sales”, “Summary of Water Rates”, and “Ten Largest Water Customers”; the water standby charge for the fiscal year; revenues for the fiscal year resulting from wheeling and exchange transactions; the total power revenues for the fiscal year; and the unrestricted reserve balances available to Metropolitan for the fiscal year; • under “METROPOLITAN REVENUES – Investment of Moneys in Funds and Accounts” in Appendix A to the Official Statement, the total market value of all Metropolitan funds, earnings on investments and the minimum month-end balance of Metropolitan’s investment portfolio • under “METROPOLITAN EXPENDITURES” in App. A, the table entitled “Summary of Expenditures”; outstanding indebtedness (including revenue bonds, subordinate revenue obligations, variable rate and swap obligations, other revenue obligations and general obligation bonds), the payment obligation under the State Water Contract, a description of other long term commitments, and the information described under the sub-caption “Defined Benefit Pension Plan”; • under “HISTORICAL AND PROJECTED REVENUES AND EXPENSES” in App. A, historical revenues and expenses for the then immediately past fiscal year, as presented in the table entitled “Historical and Projected Revenues and Expenses”; • under “MANAGEMENT’S DISCUSSION OF HISTORICAL AND PROJECTED REVENUES AND EXPENSES” in App. A, the percentage of operation and maintenance expenses to total costs; • under “POWER SOURCES AND COSTS” in App. A, the expenses for electric power, for so long as such information shall be deemed to be material by Metropolitan 	<p>GO Bond Official Statement and App A, containing information for applicable fiscal year</p> <p>If no GO Bond OS has been issued since prior July 1, use Rev. Bond Official Statement and App A, containing information for applicable fiscal year, and statistical tables from CAFR See S:\FINANCE FOLDERS\Disclosure\2008 filing GO bonds.docx, and S:\FINANCE FOLDERS\Disclosure\2008 filing GO bonds\2008 Annual Financial Info Supp GO.docx</p> <p>If no OS has been issued since prior July 1, expand report to provide the required information</p>
<p>ANY AMENDMENT TO CDU</p> <p>If amendment changes the type of financial information or operating data, include a narrative explanation of the reasons for the amendment and the impact of the change. (see CDU §4.2c)</p> <p>If amendment changes accounting principles, present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles (see CDU §4.2d)</p>	<p>Legal—determine if CDU has been amended</p> <p>Controller, Auditor—provide notice of any changes in accounting principles</p>
<p>ANNUAL FINANCIAL STATEMENTS</p> <p>Audited financial statements must be filed, if available. If not, unaudited annual financial statements must be filed with the annual report and audited statements must be filed when available</p>	<p>Controller</p>

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Filed with the Office of the Chief Financial Officer – December 14, 2015



May 2008

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DISCLOSURE OBLIGATIONS OF MUNICIPAL ISSUERS: THE SEC ENFORCEMENT PERSPECTIVE

The Securities and Exchange Commission's Division of Enforcement is scrutinizing the municipal marketplace to a degree not seen since the mid-1990's. With \$2.5 trillion of municipal securities outstanding – two-thirds held directly or indirectly by individual investors – SEC Chairman Christopher Cox has identified “ferreting out fraud in the municipal bond market and punishing its perpetrators” as an enforcement priority for 2008.¹ Municipal securities are the focus of one of four “working groups” recently formed within the SEC's Enforcement Division to coordinate investigative efforts nationwide.²

One key component of the SEC's renewed focus on municipal securities is the disclosure obligations of municipal issuers. In a White Paper submitted in July 2007 to the leaders of the Senate Banking Committee and the House Committee on Financial Services, the SEC staff noted its concern over “continued disclosure weaknesses” in municipal securities offerings notwithstanding the SEC's past public statements and enforcement actions.³ The SEC's recent action seeking antifraud injunctions and financial penalties against five former San Diego city officials for failing to disclose the city's under funding of pension liabilities and its growing financial crisis relating to pension and retiree health benefits⁴ illustrates that the SEC is prepared to hold individuals personally accountable and seek tough enforcement sanctions when the agency determines that state and local issuers have failed to disclose material information in violation of the federal securities laws.

This article discusses the disclosure obligations of municipal issuers from the perspective of SEC enforcement practice. Part I reviews the statutory bases in the federal securities laws for SEC enforcement actions against municipal issuers and officials. Because the SEC does not have regulatory jurisdiction over municipal securities, the focus of enforcement investigations is always on potential antifraud violations. Part II reviews developments in the SEC's enforcement program against municipal issuers and officials from the mid-1990's to the present. Part III describes the current environment of heightened scrutiny and the SEC's continuing concerns with certain disclosure practices of municipal issuers. Part IV suggests practical steps that issuers can follow to help minimize the possibility that they will

- 1 Christopher Cox, Chairman, U.S. SEC, “The SEC Agenda for 2008: Remarks to the ‘SEC Speaks in 2008’ Program of the Practicing Law Institute” (Feb. 8, 2008), *available at* <http://www.sec.gov/news/speech/2008/spch020808cc.htm>.
- 2 The other three are built around sub-prime lending, options backdating, and hedge funds. Linda Chatman Thomsen, Director, Division of Enforcement, U.S. SEC, “Regulatory Keynote Address — Outlook From the SEC,” Second Annual Capital Markets Summit, U.S. Chamber of Commerce (Mar. 26, 2008), *available at* <http://www.sec.gov/news/speech/2008/spch032608lct.htm>. (“Thomsen Speech; Outlook From the SEC”)
- 3 “Disclosure and Accounting Practices in the Municipal Securities Market” at 1, 10, *available at* <http://www.sec.gov/news/press/2007/2007-148.htm> (“SEC White Paper”).
- 4 *SEC v. Michael T. Uberuaga, et al.*, Civil Action No. 08 CV 0625 DMS (LSP) (S.D. Cal.) (filed April 7, 2008), SEC Litigation Release No. 20522, *available at* <http://www.sec.gov/litigation/litreleases/2008/lr20522.htm>.

become subject to an enforcement investigation or that the SEC will find any violations should an investigation of the issuer's disclosures be undertaken.

With respect to corporate issuers, the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley")⁵ mandated disclosure controls for SEC periodic reports, including requirements for so-called disclosure controls and procedures, internal control over financial reporting, and officer certifications. As will be seen below, it appears that the SEC is increasingly looking to elements of the Sarbanes-Oxley model as a framework for evaluating disclosure practices among municipal issuers. Thus, in any future enforcement investigation, it will be imperative for a municipal issuer to be able to demonstrate to the SEC staff that the issuer implemented written policies and procedures that were appropriate to the issuer and were reasonably designed to ensure that material information concerning the issuer and its securities was accumulated, processed, summarized, and reported in a timely fashion in offering documents, continuing disclosures and other public statements that could affect investors.

I. Background: Applicable Law

In contrast with corporate issuers, the SEC's regulatory authority over disclosures by issuers of municipal securities is circumscribed by statute.⁶ Because municipal securities are "exempt" securities under both the Securities Act of 1933 ("Securities Act") and the Securities Exchange Act of 1934 ("Exchange Act"), they are not subject to the Securities Act registration requirements, and issuers of municipal securities are not subject to the Exchange Act periodic reporting requirements that are applicable to public companies.⁷

However, the SEC's authority reaches to municipal issuers and their officials through the operation of the antifraud provisions of the federal securities laws – Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5. The antifraud provisions prohibit "any person," including issuers of municipal securities, from making a false or misleading statement of material fact, or omitting to state material

facts that are necessary to make statements made not misleading, in connection with the offer, purchase, or sale of any security.⁸ A fact is deemed to be material for purposes of the federal securities laws if there is a substantial likelihood that a reasonable investor would consider it important in making an investment decision.⁹

Thus, in any enforcement investigation involving an offering of municipal securities, the stakes are immediately elevated for the issuer and its personnel. Unlike investigations of disclosures by public companies, or relating to regulated entities such as brokers, dealers, and investment advisers, the SEC's limited authority over municipal issuers means that any potential enforcement action necessarily will sound in fraud. There is no other statutory or regulatory basis on which an action can be brought and, therefore, a potential settlement reached.

Within this limitation, however, an important distinction is made between fraud actions based on negligent conduct and those based on scienter. Under Sections 17(a)(2) and (3) of the Securities Act, which prohibit material misstatements or omissions and fraudulent transactions, practices, or courses of business in the offer or sale of securities, the SEC need only prove that a defendant or respondent acted negligently.¹⁰ However, Section 17(a)(1) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 require the SEC to show that the defendant or respondent acted with scienter,¹¹ defined as "a mental state embracing intent to deceive, manipulate, or defraud."¹² The courts generally permit scienter to be proven by evidence of conduct that was reckless in the face of a known danger of misleading.¹³ Thus, depending on the facts

5 Pub. L. No. 107-202 (2002).

6 "Municipal securities" include all bonds, notes, and other debt securities issued by state and local governments and their respective agencies and instrumentalities. SEC White Paper at 1.

7 SEC White Paper at 3.

8 Statement of the Commission Regarding Disclosure Obligations of Municipal Securities Issuers and Others, SEC Release Nos. 33-7049, 34-33741, 1994 SEC LEXIS 700 at *9 (March 9, 1994) ("1994 Interpretive Release").

9 *E.g.*, *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1987).

10 *Aaron v. SEC*, 446 U.S. 680, 685, n.5 (1980).

11 *Aaron v. SEC*, 446 U.S. at 701-702.

12 *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.12 (1976).

13 Recklessness is generally defined as "a highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so 'obvious that the actor must have been aware of it.'" *E.g.*, *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1569 (9th Cir.

and circumstances of the particular case, the SEC can pursue an enforcement action against a municipal issuer or its officials based on a theory of either negligent,¹⁴ reckless,¹⁵ or intentional misstatements or omissions.

Further, in any enforcement investigation, the SEC's scrutiny will not be limited to representations in the official statement or preliminary official statement for an offering. Whenever an issuer of municipal securities "releases information to the public that is reasonably expected to reach investors and the trading markets, those disclosures are subject to the antifraud provisions."¹⁶ Thus, for example, the SEC's actions against the City of San Diego and the former city officials cited misleading disclosures not only in official statements and preliminary official statements, but also in the city's continuing disclosures filed with nationally recognized municipal securities information repositories pursuant to Rule 15c2-12 under the Exchange Act, and in presentations to credit rating agencies.¹⁷

II. SEC Pronouncements and Enforcement Actions Relating to Municipal Disclosures

Reforms in the municipal securities market became a focus of SEC rule making, interpretive guidance, and enforcement activity during the 1990's under former Chairman Arthur Levitt, Jr. The SEC's 1994 Statement Regarding Disclosure Obligations of Municipal Securities Issuers and Others cited continuing concerns with the adequacy of disclosure

both in primary offerings of municipal securities and in the secondary market.¹⁸ Among the areas where the SEC determined that improvement was needed was the disclosure in primary offerings of financial and operating information concerning issuers, including known conditions that could significantly affect an issuer's financial condition in the future.¹⁹

The SEC has repeatedly made clear that the obligation to ensure adequate disclosure rests primarily with the municipal issuer itself and its officials, notwithstanding the participation of outside professionals such as underwriters, bond counsel, and issuer's counsel in an offering.²⁰ As the Director of the SEC's Enforcement Division recently stated, "[T]he buck stops with municipalities and their officials."²¹

For example, following the 1994 bankruptcy of Orange County, California as a result of substantial losses in the county's investment pools – the largest municipal bankruptcy in history – the SEC issued a Report of Investigation under Section 21(a) of the Exchange Act that prominently criticized the individual members of the county's board of supervisors for failing to ensure that bond offering documents disclosed increasing budgetary pressures and the county's dependence on interest income from the investment pools. Although the supervisors believed they could rely on the financial advisers, bond counsel, and underwriters that assisted with the offerings, the SEC took the supervisors to task because they "never questioned the professionals regarding the disclosure in the Official Statements, despite their knowledge of facts calling into question the County's ability to repay the securities."²² The

1990) (*quoting Sundstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977)).

14 *E.g.*, *In re The Massachusetts Turnpike Authority and James J. Kerasiotes*, SEC Release No. 33-8260, 2003 SEC LEXIS 1792 (July 31, 2003); *In re Dauphin County General Authority*, SEC Release No. 33-8415, 2004 SEC LEXIS 886 (Apr. 26, 2004).

15 *E.g.*, *In re The City of Miami, Florida*, SEC Release Nos. 33-8213, 34-47552, 2003 SEC LEXIS 676 (Mar. 21, 2003); *In re City of San Diego, California*, SEC Release Nos. 33-8751, 34-54745, 2006 SEC LEXIS 2608 (Nov. 14, 2006); *SEC v. Michael T. Uberuaga, et al.*, *supra*. In the case of individuals, the SEC can also pursue secondary theories of liability; i.e., that the individual "caused" or "aided and abetted" the issuer's primary violations.

16 1994 Interpretive Release at *50.

17 *City of San Diego, California, supra*; *SEC v. Michael T. Uberuaga, et al.*

18 1994 Interpretive Release at *12-*13.

19 1994 Interpretive Release at *31-*34.

20 *E.g.*, *Municipal Securities Disclosure*, SEC Release No. 34-26985, 1989 SEC LEXIS 1173 at *71 n. 84 (June 28, 1989).

21 Linda Chatman Thomsen, Director, Division of Enforcement, U.S. SEC, "Lessons Learned from San Diego," AICPA National Conference on Current SEC and PCAOB Developments (Dec. 11, 2007), *available at* <http://www.sec.gov/news/speech/2007/spch121107lct.htm> ("Thomsen Speech; Lessons Learned from San Diego").

22 Report of Investigation in the Matter of County of Orange, California as it Relates to the Conduct of the Members of the Board of Supervisors, SEC Release No. 34-36761, 1996 SEC LEXIS 132 at *22 (Jan. 24, 1996).

SEC's report concluded with a clear warning to public officials:

In addition to the responsibilities imposed on issuers of municipal securities, the antifraud provisions of the federal securities laws impose responsibilities on a public official who authorizes the offer and sale of securities. A public official who approves the issuance of securities and related disclosure documents may not authorize disclosure that the public official knows to be materially false or misleading; nor may the public official authorize disclosure while recklessly disregarding facts that indicate that there is a risk that the disclosure may be misleading. When, for example, a public official has knowledge of facts bringing into question the issuer's ability to repay the securities, it is reckless for that official to approve disclosure to investors without taking steps appropriate under the circumstances to prevent the dissemination of materially false or misleading information regarding those facts. In this matter, such steps could have included becoming familiar with the disclosure documents and questioning the issuer's officials, employees or other agents about the disclosure of those facts.

... Based on the Supervisors' significant knowledge relating to the County's finances, they should have understood the materiality of that information to the County's ability to repay the municipal securities. The Supervisors therefore had a duty to take steps appropriate under the circumstances to assure accurate disclosure was made to investors regarding this material information. The Supervisors, however, failed to take appropriate steps. For example, while the Supervisors believed that they could rely on the County's officials, employees or other agents with respect to these offerings, they never questioned these officials, employees or other agents regarding the disclosure of this information; nor did they become familiar with the disclosure regarding the County's financial condition. Had they taken such or similar steps, it should have been apparent to each Supervisor, in light of his or her knowledge, that the disclosure regarding the County's financial condition may have been materially false or misleading.

Consequently, the Supervisors failed to assure appropriate disclosure of these matters by authorizing and approving the dissemination of misleading disclosure documents. This failure denied investors the fair and accurate disclosure required under the federal securities laws.²³

A so-called "Section 21(a) Report" is not an SEC enforcement action and does not impose any sanctions.²⁴ The SEC on occasion issues a Section 21(a) Report under circumstances where the Commission wants to publicize its views concerning certain conduct, but, because novel legal issues are involved or for other reasons, determines in its discretion not to pursue an enforcement action. However, Section 21(a) Reports are exceedingly rare; only eight have been issued since 1996. Far more typically, the SEC's response to violations is to file an enforcement action (either an administrative proceeding at the agency or a civil injunctive action in federal court).²⁵ Thus, the Orange County Section 21(a) Report was a "shot across the bow" for municipal officials, and should not be interpreted as suggesting that similar conduct in other cases will also receive the benefit of Section 21(a) treatment. To the contrary, the recent enforcement action against San Diego's former officials illustrates the seriousness with which the SEC is likely treat evidence of disclosure violations by municipal officials in the future.

In enforcement actions subsequent to the Orange County Report, the SEC has returned time and again to the theme that municipalities and their officials are responsible for the content of disclosures in connection with offerings of municipal securities. For example, in administrative orders entered against the City of Miami, Florida and the former City Manager related to

²³ *Id.* at *29-*31.

²⁴ Section 21(a) of the Exchange Act authorizes the SEC, in its discretion, to conduct investigations and to "publish information concerning any ... violations,..." 15 U.S.C. §78u(a)(1).

²⁵ In enforcement actions filed in connection with the Orange County matter, the SEC charged the former county Treasurer, the Assistant Treasurer, the county, and the board of supervisors as a body with violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 for various disclosure failures in bond offerings relating to the risks of the county's investment pools and the county's reliance on the pools.

several bond offerings, the SEC found that the city and the official committed fraud by failing to disclose that the city's financial condition was deteriorating and that the city might not be able to meet its operating expenses and debt service requirements. In support of its finding of scienter, the SEC emphasized that "Miami's officials ignored the City's disclosure responsibilities":

...[I]n the face of obvious indicators to the contrary, Miami was at least reckless in misstating that its FY 1995 budget was balanced, down playing its cash flow crisis, failing to disclose that Miami needed to issue debt to resolve its crisis, and misrepresenting that there were no material changes in its financial condition. Miami's officials ignored the City's disclosure responsibilities. [The former City Manager] admitted that he was not familiar with Miami's disclosure requirements and dismissed the importance of the bond offering documents....²⁶

The SEC gave short shrift to the city's effort to pass the blame for disclosure failures to the outside professionals who worked on city bond offerings:

Miami further asserts that the City relied on Deloitte, and other professionals who participated in the bond offerings, to advise the City on its disclosure in the Official Statements. Primary responsibility for the accuracy of information filed with the Commission and disseminated among investors rests upon the municipality. A city does not discharge this obligation by the employment of independent public accountants or other professionals. As we have repeatedly emphasized, issuers of municipal securities "are primarily responsible for the content of their disclosure documents and may be held liable under the federal securities laws for misleading disclosure."²⁷ Municipal issuers have an affirmative obligation to know the contents of their securities disclosure documents, including their financial statements.²⁷

In an order against the Dauphin County General Authority, the SEC emphasized that the Authority's reliance on a bevy of professional advisers did not absolve the Authority from liability under the federal

securities laws when an official statement that the Authority authorized was found to be materially misleading.²⁸ The Authority issued unsecured bonds to finance the purchase of an office building. Lease and parking revenues from the building provided the sole source of funds to repay the bonds. Although the Authority knew at the time it authorized the preliminary official statement that the tenant that provided more than 60 percent of the building's revenues had determined to vacate the building, this fact was not specifically disclosed. Instead, the official statement merely included general cautionary language to the effect that the leases would expire before the bonds matured, and there was no commitment from the tenants to renew them. In a later enforcement action against the bonds' underwriter, the D.C. Circuit Court of Appeals likened this disclosure to "someone who warns his hiking companion to walk slowly because there *might* be a ditch ahead when he *knows* with near certainty that the Grand Canyon lies one foot away."²⁹

The SEC's order recognized that the Authority retained a financial adviser, bond counsel, and underwriter to assist with the offering, and that the Authority "trusted its professional advisors...to use their professional knowledge and expertise in ensuring that ... all documents, including the Official Statement, were complete, accurate, and contained all necessary disclosures."³⁰ The SEC further acknowledged that none of the advisors discussed with the Authority the need to disclose the departure of the building's major tenant. Notwithstanding these circumstances, the SEC found that the Authority violated the negligence-based antifraud provisions of the Securities Act (Sections 17(a)(2) and (3)) because "[i]ssuers of municipal securities are primarily responsible for the content of their disclosure documents."³¹

The SEC specifically criticized the members of the Authority for not reading the preliminary official statement before they voted to approve it. Even though the case was settled on a non-scienter basis, the SEC

²⁶ *In re The City of Miami, Florida*, SEC Release Nos. 33-8213, 34-47552, 2003 SEC LEXIS 676 at *35 (Mar. 21, 2003) (citations omitted).

²⁷ *Id.* at *36.

²⁸ *In re Dauphin County General Authority*, SEC Release No. 33-8415, 2004 SEC LEXIS 886 (Apr. 26, 2004).

²⁹ *Dolphin & Bradbury, Inc. v. SEC*, 512 F.3d 634, 640 (D.C. Cir. 2008).

³⁰ *Dauphin County General Authority*, 2004 SEC LEXIS 886 at *4.

³¹ *Id.* at 9.

cautioned that “Executing offering documents without first reading the documents to ascertain whether they were accurate may be reckless.”³²

The SEC’s view that municipal issuers may not abdicate their responsibility for offering disclosures to outside professionals was also at the core of the SEC’s order finding that the Neshannock Township School District violated the antifraud provisions by failing to disclose the actual use of proceeds and the consequent risk to the tax-exempt status of certain notes that the school district issued.³³ Under governing IRS regulations, the notes’ tax exemption depended on the school district meeting certain strict criteria concerning commitment of the note proceeds to capital improvement projects. Although these criteria were not satisfied (and the proceeds were not in fact used for such projects) the school district decided to proceed with the offering after discussions with the underwriter and bond counsel. Later, the school district had to enter into a settlement with the IRS to preserve the tax exemption for investors.

The SEC found that the school district’s misleading disclosures were made recklessly in violation of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5.³⁴ Further, as if to underscore the primary responsibility of issuers for disclosures, after a trial, the SEC only held the bond counsel who rendered the tax-exemption opinion liable for negligent violations (i.e., Sections 17(a)(2) and (3) of the Securities Act).³⁵

In connection with the offering, a school district official executed a “non-arbitrage” certificate drafted by the bond counsel that inaccurately represented that the IRS criteria were met. The official testified at the bond counsel’s trial that she signed the certificate “pretty

much having no idea what it meant.”³⁶ Chairman Cox has pointed to this official, as well as to the examples of the former Miami City Manager and the Dauphin County Authority, to drive home the point that “Too many municipal issuers – and in particular the members of their governing bodies – remain inadequately involved in disclosure.”³⁷

As noted above, in 2006 the SEC found that the City of San Diego violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 by failing to disclose in bond offering documents, in continuing disclosures, and in presentations to rating agencies that the city had been intentionally under funding its pension obligations, faced a near-term dramatic increase in unfunded pension liabilities and retire health benefits, and would have severe difficulties paying its obligations in the future. The Director of the SEC’s Enforcement Division has warned that “San Diego may not be unlike many other American cities, and accordingly there is some concern that San Diego may be a harbinger of things to come as other cities wrestle with their own burgeoning financial obligations.”³⁸

The SEC’s administrative order against the City of San Diego signified an important new approach to cases involving municipal issuers. As part of the settlement, the SEC required that the city retain an independent consultant to evaluate and make recommendations concerning the city’s policies, procedures, and internal controls relating to disclosures, the hiring of employees and outside experts for disclosure functions, and the implementation of training programs regarding disclosure obligations. The city is required to comply with the independent consultant’s recommendations or to adopt alternative measures designed to achieve the same objectives.³⁹

Such so-called “remedial undertakings” have been an integral part of SEC enforcement practice for

32 *Id.*

33 *In re Neshannock Township School District*, SEC Release Nos. 33-8411, 34-49600, 2004 SEC LEXIS 861 (April 22, 2004).

34 *Neshannock Township School District*, 2004 SEC LEXIS 861 at *9.

35 *In re Ira Weiss*, SEC Release Nos. 33-8641, 34-52875, 2005 SEC LEXIS 3107 (Dec. 2, 2005), *pet. for review denied*, 468 F.3d 849 (D.C. Cir. 2006). In a separate settlement, the SEC also found that the underwriter violated Sections 17(a), Section 10(b), and Rule 10b-5, and aided and abetted and caused the school district’s violations. *In re Ira Weiss and Andrew Shupe II*, SEC Release Nos. 33-8459 and 34-50235, 2004 SEC LEXIS 1839 (Aug. 24, 2004).

36 *In re Ira Weiss*, 2005 SEC LEXIS 3107 at *35.

37 Christopher Cox, Chairman, U.S. SEC, “Integrity in the Municipal Market” Town Hall, Los Angeles Biltmore Hotel (July 18, 2007), *available at* <http://www.sec.gov/news/speech/2007/spch071807cc.htm> (“Cox Speech: Integrity in the Municipal Market”).

38 Thomsen Speech; Outlook From the SEC, *supra*.

39 *In re City of San Diego, California*, SEC Release Nos. 33-8751, 34-54745, 2006 SEC LEXIS 2608 at *49 (Nov. 14, 2006).

many years in cases against regulated entities and public companies. As the name suggests, remedial undertakings are intended to remediate the causes or consequences of securities violations, and are limited only by the creativity of the enforcement staff. Often, as is illustrated by the San Diego case, undertakings require an entity to implement expensive, time consuming, and burdensome process reviews and reforms under the oversight of an independent third party expert whose fees are paid by the entity.

In actions against municipal issuers, the SEC has traditionally limited itself to issuing administrative cease-and-desist orders against future violations. The settlement with the City of San Diego marked the first time that the SEC has ordered remedial undertakings in an action against a municipality,⁴⁰ and suggests that the SEC is now prepared to seek costly enforcement remedies developed in other contexts in order to address disclosure violations in actions against municipal issuers.⁴¹ The best way for issuers to avoid such requirements is to proactively take steps to ensure that they have implemented appropriate disclosure controls and that their disclosures are fully compliant with the requirements of the federal securities laws.

III. Heightened Scrutiny and the SEC's Current Concerns; the Staff White Paper

The lesson the SEC has drawn from cases such as those against the City of Miami, the Dauphin County General Authority, the Neshannock Township School District, and the City of San Diego is that the “broader problem” is “the lack of disclosure controls, policies, and procedures for municipal issuers.”⁴² Thus, the SEC’s White Paper expressed the staff’s concerns that “regardless of size, issuers of municipal securities may lack policies and procedures adequate to ensure accurate and full disclosure in their offering documents and are not legally required to certify the accuracy

of their disclosures.”⁴³ The staff’s perspective on disclosures by municipal issuers has clearly been informed by its experience since 2002 under Section 302 of Sarbanes-Oxley and related SEC rules, which require that public companies maintain and regularly evaluate so-called “disclosure controls and procedures,” and that their principal executive and principal financial officers personally certify periodic reports filed with the SEC.⁴⁴

The staff’s White Paper concludes that the lack of such disclosure controls is a key reason for deficiencies in municipal disclosures:

Unlike in the corporate context, in which there are requirements for disclosure controls, evidence obtained in many enforcement actions suggests that issuer officials who vote to approve the use of disclosure documents often assume the accuracy of disclosure documents and approve them with little or no review. Furthermore, the staff has observed that issuer representatives often have limited involvement in the preparation of disclosure documents.⁴⁵

Thus, in a move reminiscent of the Sarbanes-Oxley model, the SEC’s White Paper proposed legislation “Ensuring that issuers of municipal securities establish policies and procedures for disclosure appropriate to the particular issuer.”⁴⁶

The White Paper also concluded that, despite “explicit” guidance provided in the Orange County Section 21(a) Report concerning the responsibility of municipal officials for disclosure in securities offerings, “this problem remains.”⁴⁷ Exacerbating the situation, outside professionals who assist in offerings frequently disclaim responsibility for disclosures or do not have full knowledge of the issuer’s circumstances:

In contrast to corporate securities offerings in which the issuer and its counsel prepare a company’s disclosure documents and filings, with input from the underwriter and its counsel,

⁴⁰ Thomsen Speech; Lessons Learned from San Diego, *supra*.

⁴¹ However, financial penalties against municipal issuers do not appear to be in the offing. Apart from the obvious issues regarding sovereignty that penalties would raise, Chairman Cox has recognized that a municipal issuer has no money of its own, and that any penalty would be paid by citizens through tax dollars. Cox Speech: Integrity in the Municipal Market, *supra*.

⁴² Cox Speech: Integrity in the Municipal Market, *supra*.

⁴³ *Id.* at 9.

⁴⁴ See Section 302 of the Sarbanes-Oxley Act of 2002, Pub. L. No. 107-202 (2002); Exchange Act Rules 13a-14, 13a-15, 15d-14, and 15d-15, 17 CFR §§240.13a-14, 13a-15, 15d-14, and 15d-15.

⁴⁵ SEC White Paper at 9.

⁴⁶ *d.* at 11.

⁴⁷ *Id.* at 10.

the offering documents for negotiated offerings of municipal securities are typically prepared by the underwriter and underwriter's counsel, who do not have an intimate knowledge of the issuer's affairs. In fact, issuers often are not represented by counsel with respect to the preparation of disclosure documents. The issuer's counsel, bond counsel, and other professionals who work on an offering are often hired on a transaction-by-transaction basis and therefore may lack the depth of factual knowledge derived from an ongoing relationship with an issuer. Often issuer's counsel is only occasionally engaged in municipal securities offerings and is heavily dependent on others about disclosure matters. Bond counsel often limit their practices exclusively to municipal securities and may lack the depth of knowledge of the federal securities laws obtained from representing clients in registration, periodic reporting, and other matters before the Commission. Furthermore, underwriters of municipal securities often disclaim responsibility for statements made in offering documents, which would not be permitted in a corporate bond offering.⁴⁸

For these reasons, the SEC's White Paper also proposed legislation to clarify the legal responsibilities of issuer officials and outside participants in offerings of municipal securities.

IV. Practical Guidance for Issuers of Municipal Securities

Against the backdrop of potential scrutiny from the SEC enforcement staff, there are at least three reasons why municipal issuers should consider reviewing their disclosure processes and making improvements in any deficient areas. First and foremost, enhanced disclosure controls may help ensure compliance with the federal securities laws and therefore minimize the chances that any questions might arise that could result in an SEC enforcement investigation. Second, in the event that an issuer's disclosures do become the subject of an investigation, the fact that the disclosures were subject to detailed controls and a comprehensive review process may help blunt any allegation that the issuer acted recklessly or negligently. Third, the SEC has traditionally viewed the presence of an effective compliance program as a mitigating factor in exercising its prosecutorial discretion as to whether to bring an

⁴⁸ *Id.* at 9-10 (footnotes omitted).

enforcement action against an entity and, if so, what sanctions to pursue. For example, in a recent case involving insider trading by a state agency that managed state pension funds, the SEC decided not to seek either a permanent injunction or a cease-and-desist order against future violations in part because, subsequent to the violations occurring, the agency engaged securities counsel and implemented a compliance program that counsel designed and recommended. Instead of commencing an enforcement action, the SEC issued a Section 21(a) Report (which, notably, criticized the agency for not having adequate policies and procedures in the first instance to ensure that the violations did not occur.)⁴⁹ Conversely, the lack of an effective compliance program may be viewed negatively in the agency's enforcement determinations.

There are a number of steps that municipal issuers should consider taking to help ensure that their disclosures comply with the requirements of the federal securities laws. First, as discussed above, the SEC now appears to view adherence to a suitable set of written disclosure policies and procedures as virtually a "must" for municipal issuers as it has been for public companies at least since the passage of Sarbanes-Oxley. Other helpful steps may include instituting formal and regular training for municipal employees in disclosure obligations; retaining disclosure counsel or issuer's counsel experienced in the federal securities laws as well as knowledgeable about the issuer; and taking steps to ensure the quality and reliability of audits of financial statements.

Each of these steps is discussed briefly below. However, this discussion is not meant to suggest that all such measures are required for all issuers. Even the SEC accepts that disclosure policies and procedures should be "appropriate for the particular issuer," and

⁴⁹ Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: The Retirement Systems of Alabama, SEC Release No. 34-57446, 2008 SEC LEXIS 513 (Mar. 6, 2008). *See also* Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions, SEC Release No. 34-44969, 2001 SEC LEXIS 2210 (Oct. 23, 2001) (noting that a company's adoption of internal controls and procedures designed to prevent a recurrence of misconduct in the future is a factor that the SEC will consider in determining whether and how much to credit a company in an enforcement matter).

may assume greater importance depending on the size and complexity of the issuer, and the frequency with which the issuer accesses the municipal securities marketplace.⁵⁰ Thus the following discussion is intended only to suggest the range and types of preventative measures that may assist municipal issuers in meeting their disclosure obligations laws, and thus avert, or at least successfully address, any inquiries from the SEC Enforcement Division.

Disclosure Policies and Procedures

As discussed above, SEC rules promulgated pursuant to Section 302 of Sarbanes-Oxley require SEC reporting companies to maintain, and management to periodically evaluate the effectiveness of, the company's "disclosure controls and procedures." Disclosure controls and procedures are defined as:

controls and other procedures of an issuer that are designed to ensure that information required to be disclosed by the issuer in the reports that it files or submits under the [Exchange] Act is recorded, processed, summarized, and reported, within the time periods specified in the Commission's rules and forms. Disclosure Controls and Procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the [Exchange] Act is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.⁵¹

A closely related concept under Section 404 of Sarbanes-Oxley and SEC rules is the requirement that management evaluate the effectiveness of the company's "internal control over financial reporting." While "disclosure controls and procedures" and "internal control over financial reporting" are distinct concepts under the federal securities laws, the SEC has stated that disclosure controls and procedures include those components of internal control over financial reporting that provide reasonable assurances that transactions are recorded as necessary to permit

preparation of financial statements in accordance with generally accepted accounting principles.⁵² Thus, disclosure controls and procedures include controls and procedures relating to both non-financial disclosures and financial reporting.

Although municipal issuers are exempt from SEC reporting requirements, the SEC's definition of disclosure controls and procedures provides a useful starting point for municipal issuers in designing their own controls. For example, the City of San Diego borrowed conceptually from the Exchange Act rules relating to disclosure controls and procedures when it adopted new "Securities Disclosure" provisions in the city's Administrative Code. These provisions require city officials, among other things, to implement written disclosure controls and procedures designed to ensure:

"(1) that information material to the City's proposed and outstanding securities is accumulated and communicated to senior City officials, including the City Manager, City Auditor and Comptroller, City Treasurer, City Attorney, and the City Council, as appropriate, to allow timely decisions regarding disclosure;

(2) that such information is recorded, processed, and summarized in a timely manner to enable the requisite senior City officials to certify the accuracy of disclosures made in connection with City financings;

(3) compliance with all applicable federal and state securities laws, including the disclosure of all material information with respect to the City's proposed and outstanding securities; and,

(4) the preservation of an audit trail regarding information reviewed or prepared in connection with such disclosures."⁵³

The SEC has stated that it will not require reporting companies to implement any particular types of disclosure controls and procedures. Instead, the SEC leaves it to each company to develop a process that is

⁵⁰ SEC White Paper at 11; Cox Speech: Integrity in the Municipal Market, *supra*.

⁵¹ Exchange Act Rules 13a-15(e) and 15d-15(e), 17 CFR §§240.13a-15(e), 15d-15(e).

⁵² Management's Report on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports, SEC Release Nos. 33-8238, 34-47986, IC-26068, 2003 SEC LEXIS 1380 at *62 (June 5, 2003).

⁵³ San Diego Municipal Code, Article 2, §22.4105 (added Oct. 11, 2004).

consistent with its business and internal management and supervisory practices.⁵⁴ However, corporate issuers have commonly incorporated into their disclosure controls and procedures a number of features that municipal issuers should consider. These include:

- A written statement of policy and procedure that sets forth the steps to be followed in the preparation and review of disclosure documents and clearly delineates the responsibilities of various persons and parts of the organization at each step;
- A process employing formalized and documented communications such as meetings, interviews of relevant personnel, or disclosure questionnaires that are intended to elicit or update material information from various parts of the organization and to identify potential disclosure questions or concerns;
- A committee or group comprised of senior personnel with relevant area or subject matter responsibilities (typically referred to in the corporate context as the “disclosure committee”), including in-house counsel (and assisted by outside counsel), charged with the responsibility to make determinations regarding disclosures, to carefully review disclosure documents to ensure that all appropriate disclosures are made, and to periodically evaluate the effectiveness of the issuer’s disclosure controls and procedures;⁵⁵
- “Sub-certifications” provided by officials with area or subject matter responsibilities to the senior officers attesting that the officials believe that the disclosure documents do not misrepresent any material facts or contain any material omissions with regard to their areas of responsibility; and
- A person or persons designated to coordinate the entire process.

The Director of the SEC’s Enforcement Division has cautioned municipal issuers that as they undertake such processes, they should also “keep the big picture in mind,” and not let the completion of a disclosure

⁵⁴ Certification of Disclosure in Companies’ Quarterly and Annual Reports, SEC Release Nos. 33-8124, 34-46427, IC-25722, 2002 SEC LEXIS 2240 at *30 (Aug. 28, 2002).

⁵⁵ The formation of a disclosure committee to consider materiality issues and make disclosure determinations is the only measure that the SEC has specifically recommended. *Id.*

checklist “become the goal unto itself.”⁵⁶ For example, she has advised that members of an issuer’s disclosure team have “brainstorming sessions” devoted to the larger issues facing the municipality, identify the financial problems and issues that the municipality is struggling with, conduct their own due diligence on these issues, and make sure to disclose “bad news.”⁵⁷

Training

Training of municipal personnel with regard to disclosure obligations goes hand-in-glove with the need to maintain appropriate disclosure controls and procedures. In any investigation of possible securities violations by officers or employees of an entity, the SEC enforcement staff routinely focuses on whether the entity provided adequate compliance training. Training should encompass disclosure and financial reporting requirements applicable to municipal issues under the federal securities laws and generally accepted accounting principles established by the Government Accounting Standards Board, as well as specific training on the roles and responsibilities of individuals in the disclosure process.⁵⁸

Further, senior personnel – including the issuer’s elected officials – should be included in the training.⁵⁹ The SEC made clear in the Orange County Section 21(a) Report, and reiterated in the staff’s White Paper last year, that elected officials risk personal liability if they approve an offering without taking steps to ensure the disclosure of negative material information of which they are aware.

Retention of Knowledgeable Counsel

In many cases, reliance on counsel can provide important evidence of good faith to rebut any charge that the issuer acted recklessly.⁶⁰ However, counsel should be experienced regarding disclosure obligations under the federal securities laws, and should be knowledgeable concerning the operations, finances, and risks facing the issuer. In the SEC’s settlement with the City of San Diego, one of the city’s remedial actions that the SEC credited was the hiring of new disclosure counsel for all future offerings, who would

⁵⁶ Thomsen Speech; Lessons Learned from San Diego, *supra*.

⁵⁷ *Id.*

⁵⁸ *Id.*

⁵⁹ *Id.*

⁶⁰ See *Howard v. SEC*, 376 F.3d 1136 (D.C. Cir. 2004).

have a better and more continuous knowledge of the city's financial affairs.⁶¹ Conversely, the staff's White Paper criticized instances where issuer's counsel lacks in-depth factual knowledge about an issuer because counsel is hired on a transaction-by-transaction basis.⁶²

Audit Issues

The SEC has criticized the practice of some municipal issuers of including audited financial statements in disclosure documents without obtaining the consent of the auditor – and, in some cases, without disclosing that consent was not obtained.⁶³ In granting consent, an auditor is required to review other information included in the disclosure document and to consider whether that information, or the manner of its presentation, is materially inconsistent with information, or the manner of its presentation, appearing in the financial statements.⁶⁴ Thus, the fact that audited financial

statements were included without the consent of the auditor may be material to investors.

The SEC has also cautioned municipal issuers to make sure that their independent auditors have the requisite technical skills, experience, and resources to conduct competent and rigorous audits. The Director of the Enforcement Division has pointed to the SEC's 2007 suit against San Diego's auditors – which included charges that the auditors did not have sufficient auditing proficiency, were not knowledgeable about the city, failed to obtain sufficient competent evidential matter, and failed to exercise due professional care – as a lesson for municipal issuers. Auditors should be hired based on their ability to do the job, and not based on factors such as political connections, going with the lowest bid, or the desire to give business to local firms.⁶⁵

Finally, municipal issuers may want to consider establishing an Audit Committee, along the lines of the corporate model, to provide specific oversight to accounting, auditing, and financial reporting processes. San Diego's decision to establish an Audit Committee was one of the voluntary remedial undertakings that the SEC credited in its settlement with the city.⁶⁶

61 *City of San Diego, California*, 2006 SEC LEXIS 2608 at *48.

62 SEC White Paper at 9.

63 SEC White Paper at 8; Cox Speech: Integrity in the Municipal Market, *supra*.

64 See Statement of Auditing Standards No. 8, *Other Information in Documents Containing Audited Financial Statements*; see also "Recommended Practice: Auditor Association with Financial Statements Included in Offering Statements or Posted on Web Sites," Government Finance Officers Association (2005 and 2006).

65 Thomsen Speech; Lessons Learned from San Diego, *supra*.

66 *City of San Diego, California*, 2006 SEC LEXIS 2608 at *48; see also San Diego Municipal Code, Article 2, Division 43

V. Conclusion

In public statements and enforcement orders over the past dozen years, the SEC has repeatedly stressed that issuers of municipal securities are primarily responsible for the content of their disclosures. Where disclosures violate the antifraud provisions of the federal securities laws, the SEC may seek tough sanctions against responsible individuals as well as try to impose costly and burdensome undertakings on municipalities such as requiring the retention of an independent consultant to review and make improvements to the municipality's disclosure processes. To promote compliance with disclosure obligations and minimize the risks of future SEC investigations, municipal issuers should consider taking proactive steps to review their disclosure processes and improve upon any deficiencies. Issuers should consider implementing disclosure controls and procedures, retaining counsel knowledgeable about the municipality's finances and risks, and adopting measures to ensuring the rigor and reliability of independent audits of their financial statements.

(added May 2, 2007).

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