

# Protecting Your District's Ability to Sell Bonds or Other Debt

*If your district is bound by continuing disclosure requirements, it's imperative that you comply with SEC requirements.*

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**D**oes your school district have more than \$10 million in tax-exempt debt, inclusive of all outstanding bonds, certificates of participation, and other public debt issues with durations of more than nine months? If so, it must comply with the contractual requirements entered into under Securities and Exchange Commission (SEC) rules.

District administrators and finance staff are responsible for providing required information to investors for debt issued since 1995. Unfortunately, many districts may not be fully aware of what they need to report. Developing policies and procedures to file the necessary information is critical.

In the past, municipal investments were considered risk free, but that changed in the wake of municipal bankruptcies, such as those in New York City and Orange County, California. Additionally, holders of securities have shifted from large institutions to individuals and trusts.

In response, beginning in 1995, new rules required districts to contractually commit to continuing

disclosure requirements when they issued debt. However, there were no real consequences for noncompliance. In the current economy, with state and local governments facing financial stresses, providing transparency to investors through continuing disclosures has become more important. Now, noncompliance can result in severe sanctions.

The most serious consequence of noncompliance is the possibility that a district may be unable to issue new debt when it wants to. Under SEC rules, bond underwriters are required to verify that (1) the borrowing district is in compliance with the requirements for continuing disclosure stated in lending contracts and (2) they have reasonable belief that the district will continue to be in compliance before issuing new debt. If the district is noncompliant, underwriters may be prohibited from participating in a district's new debt issues.

## Two Elements of Compliance

Each debt contract requires the submission of annual financial reports and data by specified dates and the filing of notices of specified reportable events (if one occurs). The reports and events must be posted to the Municipal Securities Rulemaking Board's Electronic Municipal Market Access (EMMA) Website ([www.emma.msrb.org](http://www.emma.msrb.org)). EMMA is an electronic library of official statements and other reports that provides the public with free access to municipal finance data.

**Annual financial reports.** Each debt issuance contract lists the specific reports and information that must be disclosed on an ongoing basis. At a minimum, this list includes the annual audit report conforming to the Governmental Accounting Standards Board's rules.

Bond issues may also require annual filings of assessed valuations, tax delinquency factors, and other information not in the audit report. Some contracts may call for more frequent supplementary reporting, such as quarterly reports. Districts are required to file these

reports in a searchable pdf format by the deadlines in the agreements.

The district should establish a schedule and a procedure to ensure that the required filings are posted on time to the EMMA website. The district may use a dissemination agent to assist in these filings, but the preparation of the reports and their content are the district's responsibility.

Not filing the required documents is noncompliance. The first step to reverse the course is to file the delinquent reports on the EMMA website going back five years. You must also file a notice on the EMMA website indicating the delay in filing. Based on the circumstances, other critical steps may be necessary so consult the district's financial adviser before proceeding.

**Reportable events.** Reportable events are the irregular, infrequent occurrences listed in the contract of which the SEC has determined investors should be promptly informed. (For a legal description of reportable events, visit [www.vlsllp.com/ASBO](http://www.vlsllp.com/ASBO).) When a reportable event occurs, investors need to know, because payments on a debt issue may be disrupted or the value of the debt issue in trading markets may be affected.

Over time, the list of reportable events has expanded and has become more stringent. The SEC's updated requirements for issues after December 1, 2010, increased the number of reportable events from 11 to 14. Additionally, 6 of the former events must now be reported even if they are considered immaterial. The new standard requires events to be filed within 10 days of occurrence rather than "as soon as possible," as specified in the previous rule.

## Identifying Reportable Events

The process for event reporting can be challenging at first, and the district may be wise to seek professional assistance. The process includes implementing a strategy to identify the potential reportable events for each of the district's outstanding debt issues, establishing necessary communication links, and managing risk exposure.

Create an inventory of the district's contractual continuing disclosure requirements for each outstanding debt issue. Current industry practice is to include the full SEC-prescribed list in each debt contract even though one or more of the listed items may not apply to the particular debt instrument that the contract covers.

Because of the expansive technical language used in these contracts, the district may need to employ a professional who is familiar with tax-exempt debt instruments to interpret, categorize, and clarify the list. Then, district staff must gain an understanding of what events to watch for since the district has ultimate responsibility for reporting any occurrences.

Contracted advisers can help staff understand the list, but they are generally not in a position to know

when a reportable event has occurred. The responsibility for identifying and reporting events remains with the district.

## Establishing Communication Links

After the list of potentially reportable events has been clarified, districts will probably find that many of the potential events could occur without triggering staff's immediate attention. Some events are external to the district, such as changes in the district's or the bond insurer's financial ratings. Others are internal but may not be visible to key staff because of the segregation of duties within the district.

Create or improve communication links between the official(s) designated for identifying and reporting events and important outside sources. Critical links include those between the school district and

- Agents holding funds or reserves (probably the most important link).
- The bond's registrar, to ensure that the district is immediately informed of any delays or problems regarding bond payments.
- Other outside parties, to ensure timely notices of changes in the district's or bond insurer's ratings, and so forth.

## Managing Risk Exposure

A key consideration in managing risk is to report events in compliance with the SEC's fraud law. This law requires reporting to be "both accurate and complete." Districts should consult bond or legal counsel when considering postings. Counsel can help identify clarifications and disclaimers that should be included in any required posting.

## Reasonable Assurance

The first step the district should take is to verify that annual reporting and event filings from the last five years are up-to-date. The SEC's December 1, 2010, rule amendments warn that underwriters may be prohibited from buying bonds from districts that have been non-compliant several times during the last five years.

In addition, the district should establish policies for meeting requirements in order to ensure future compliance. The policy should designate the official(s) responsible for reporting and should provide for the periodic review and updating of procedures. Continuing education for staff is important both for addressing changes in SEC and industry rules and operations and for continuity in district compliance beyond the tenure of current staff.

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