



SECURITIES AND EXCHANGE COMMISSION ANNOUNCES NEW AMENDMENTS TO RULE 15c2-12

Pugh, Jones & Johnson, P.C. Newsletter

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On August 20, 2018, the Securities and Exchange Commission (the “Commission”) announced new amendments (the “Amendments”) to Rule 15c2-12 (the “Rule”).¹ The release of the final Amendments (the “Release”)² was published in the Federal Register on August 31, 2018.³

The Amendments add two items to the list of events an issuer or obligated person that is party to a continuing disclosure undertaking must provide notice of to the Municipal Securities Rulemaking Board on its EMMA system within ten days of their occurrence. The events are:

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

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¹ 17 CFR Section 240.15c2-12.

² SEC Release No. 34-83885.

³ 83 Fed. Reg. 44700.

In This Issue

- Financial Obligation
- Defaults and Similar Events
- “Material” and “Reflect Financial Difficulties”
- Timing and Content of Notices
- Effectiveness of the Amendments
- Compliance Actions for Issuers and Obligated Persons



FINANCIAL OBLIGATION

The Amendments provide that a “financial obligation” means: a (i) debt obligation; (ii) derivative instrument entered into in connection with, or pledged as security or a source of payment for, an existing or planned debt obligation; or (iii) guarantee of (i) or (ii). The Release provides that a financial obligation does not include ordinary financial and operating liabilities incurred in the normal course of an issuer’s or obligated person’s business. Rather, it is meant to focus on the types of obligations that could impact an issuer’s or obligated person’s liquidity, overall creditworthiness, or an existing security holder’s rights.

The Release indicates that the term “debt obligation” is intended to encompass short and long-term obligations of an issuer or an obligated person under an indenture, loan agreement or similar contract to be repaid over time, such as a direct purchase of municipal securities or a direct loan by a bank. The Release also indicates that a “debt obligation” is also intended to include leases that operate as vehicles to borrow money, citing as an example certificates of participation.

According to the Release, the type of derivative instruments intended to be covered by the Amendments are those entered into to hedge against the risks of a related debt obligation (including a debt obligation that is planned but not yet incurred), as opposed to those entered into to mitigate investment risk.

DEFAULTS AND SIMILAR EVENTS

The language of the Amendments uses the word “default” rather than “event of default.” As the Release indicates, the intent is to include defaults under the terms of an agreement in the more generic sense, rather than what may be formally defined as an event of default. The Release also states that the phrase “modification of terms” should also be considered broadly, and include written or verbal waivers of terms of an agreement.

“MATERIAL” AND “REFLECT FINANCIAL DIFFICULTIES”

In the Release the Commission declined to provide more precise definitions for these terms, noting that they have been used in the Rule since the 1994 amendments requiring the use of continuing disclosure undertakings. Application of either term will depend upon the specific facts and circumstances of each case.

TIMING AND CONTENT OF NOTICES

The Release provides guidance as to when a material financial obligation or agreement as to terms affecting security holders is “incurred” for purposes of the Rule. Whether or not a series of related transactions constitutes a single incurrence for notice purposes depends on the facts and circumstances of each case, but the Release suggests following the requirements for determining whether multiple series of bonds of an issuer constitute a single issue under the Internal Revenue Code.⁴

⁴ 26 CFR 1.150-1c.



In the case of a drawdown bond, the Release states that notice should be given when the terms of the bond become legally enforceable, rather than when draws are made. Likewise, notice of a derivative instrument should be provided when the instrument becomes legally enforceable.

According to the Release, notice of a material financial obligation should contain the material terms of the obligation, including the date of incurrence, principal amount, maturity, amortization and interest rate or method of computation.

EFFECTIVENESS OF THE AMENDMENTS

The Release states that the Amendments will become effective 180 days after their publication date, making them effective February 27, 2018. The effectiveness of the Amendments is applicable only to offerings that occur (which the Release assumes will be on the date the applicable continuing disclosure agreement is executed) after the effective date. In the event a preliminary official statement is distributed before the effective date for an offering expected to occur after the effective date, the Release advises that the form of continuing disclosure undertaking attached to such preliminary official statement reflect the Amendments.

The Release also clarifies that for any continuing disclosure agreement the reporting obligation with respect to material financial obligations and agreements as to terms affecting security holders is prospective, while the reporting obligation with respect to defaults and other similar events is retroactive. That is, for any continuing disclosure agreement executed after the effective date of the Amendments, the issuer or obligated person will be required to report only material financial obligations and agreements incurred after the effective date of the Amendments, but will be required to report defaults and other similar events occurring after the effective date of the Amendments with respect to all material financial obligations and agreements, even those incurred prior to the effective date of the Amendments.

COMPLIANCE ACTIONS FOR ISSUERS AND OBLIGATED PERSONS

To better comply with the Amendments, issuers and other obligated persons should consider taking the following steps before the effective date (and executing their first continuing disclosure agreement after such date):



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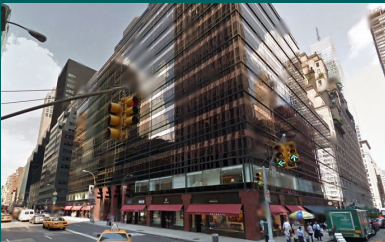
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- Cataloging all existing financial obligations;
- Compiling a database of all such financial obligations including the date of incurrence, principal amount, maturity, amortization, interest rate or method of computation, covenants, events of default, remedies for default and priority rights or other terms which could affect security holders of the issuer or obligated person;
- Determining those financial obligations considered to be material (whether by size or by terms);
- Updating their disclosure policies and procedures to incorporate mechanisms for (i) reporting to the designated disclosure official (or similar person) of (A) new financial obligations and (B) defaults, accelerations, termination events modifications or similar events with respect to old and new financial obligations, (ii) determining whether: (a) any of the items in (i)(A) are material (whether by size or by terms) and (b) any of the items in (i)(B) reflect financial difficulties of the issuer or obligated person, and (iii) timely filing all required notices with EMMA.

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