

HAWKINS ADVISORY

SEC Statement on Disclosure by Municipal Issuers Regarding the Impact of COVID-19

Introduction

On May 4, 2020, the Chairman of the Securities and Exchange Commission (the “SEC”) and the Director of the Office of Municipal Securities of the SEC released a public statement (the “SEC Statement”)¹ directed to issuers of municipal securities regarding disclosures about the impact of the novel coronavirus (“COVID-19”) on their financial and operating conditions. Such statement was intended to parallel prior guidance on this issue provided by the SEC for registered companies.² “Municipal issuers,” as used in the SEC Statement and this Advisory, also includes “obligated persons” as defined in SEC Rule 15c2-12.

The SEC Statement provides guidance on voluntary disclosure relating to the COVID-19 pandemic, but it “does not alter or amend applicable law and has no legal force or effect.” The SEC Statement does not impose any new legal obligations on any person. The SEC Statement requests “that municipal issuers provide investors with as much information about their current financial and operating condition as is reasonably practicable” and encourages “municipal issuers to provide investors with forward-looking information regarding the potential future impact of COVID-19 on their financial and operating conditions.”

Analysis

An Official Statement (or similar offering document) prepared under current circumstances will likely describe the impact of COVID-19 on a municipal issuer’s financial and operating conditions. However, in most instances, the fiscal impact of COVID-19 on a municipal issuer would not, in and of itself, require an event filing under a standard continuing disclosure agreement (“CDA”). As such, secondary market disclosure about the impact of COVID-19 on an issuer’s financial and operating conditions would be voluntary.

As the COVID-19 pandemic has progressed, municipal issuers have described with varying degrees of detail the current and potential future impact of COVID-19 on their financial and operating conditions in Official Statements and voluntary postings on the Electronic Municipal Market Access

(“EMMA”) system maintained by the Municipal Securities Rulemaking Board (“MSRB”). Since the beginning of 2020, issuers have filed more than 4,500 primary market and continuing disclosures relating to COVID-19 on EMMA.³

The SEC Statement recommends that the disclosure on financial and operating conditions, whether in an Official Statement, a filing made pursuant to a CDA, or a voluntary filing, be accompanied by meaningful cautionary language describing relevant facts or assumptions affecting the reasonableness of reliance on and the materiality of the information provided. Such disclosure may also caution how certain information may be incomplete or unaudited.

The SEC Statement reminds municipal issuers that they should ensure the information disclosed in a voluntary COVID-19-related filing is consistent with publicly available releases of the same information in other contexts (such as budgetary materials or statements made by officials of the municipal issuer). Certain municipal issuers, as the SEC Statement notes, “routinely prepare reports for governance purposes that may be significant sources of current information.” The SEC Statement suggests that such municipal issuers consider making these reports more readily accessible to investors, as they may “provide powerful insight into local, regional, and sector-specific strategies to fight and recover from COVID-19.”

The SEC Statement encourages the inclusion of specific detail as to the issuer’s assessment of COVID-19-related matters in forward-looking statements, noting that “[w]e would not expect good faith attempts to provide appropriately framed current and/or forward-looking information to be second guessed by the SEC.” While statutory safe harbors for forward-looking statements applicable to corporate issuers are not available for municipal issuers, the SEC Statement references an analogous judicially developed doctrine, the “bespeaks-caution” doctrine. Under such doctrine, municipal issuers may be afforded protection from claims based upon economic projections, estimates of future performance, and similar forward-looking statements if these are accompanied by meaningful, specific cautionary language that adequately discloses the risks bearing upon the reasonableness of reliance upon such statements.

¹ Public Statement – “The Importance of Disclosure for our Municipal Markets” (May 4, 2020), available at <https://www.sec.gov/news/public-statement/statement-clayton-olsen-2020-05-04>.

² Public Statement by the Chairman and the Director, Division of Corporation Finance – “The Importance of Disclosure – For Investors, Markets and Our Fight Against COVID-19” (April 8, 2020), available at <https://www.sec.gov/news/public-statement/statement-clayton-hinman>, and CF Disclosure Guidance: Topic No. 9 – “Coronavirus (COVID-19)” (March 25, 2020), available at <https://www.sec.gov/corpfin/coronavirus-covid-19>.

³ The MSRB is monitoring the impact of COVID-19 on municipal market participants and market activity. See <http://www.msrb.org/News-and-Events/COVID-19-Information.aspx>. As part of such information, the MSRB publishes summaries of primary market disclosures and continuing disclosures submitted to EMMA to assist market participants, policymakers, and the general public with identifying disclosures made by issuers of municipal securities that reference COVID-19.

SEC Statement's Examples of Disclosure

The SEC Statement sets forth examples of information that may be material or useful to investors and the marketplace when describing the impact of COVID-19 on a municipal issuer's financial and operating conditions, whether in an Official Statement, a filing made pursuant to a CDA, or a voluntary filing. This information includes:

- Information and the municipal issuer's assessment regarding the current and future impact of COVID-19 on its operations and financial condition
- Information regarding sources of liquidity, including
 - Cash on hand
 - Access to reserves or other funds (and to what extent such access is limited)
 - Access to liquidity facilities and any material terms thereof (such as lines of credit for debt service payments or operating expenses or similar facilities rather than standby bond purchase agreements)
 - Whether current liquidity is expected to be adequate to fund essential services and make timely debt service payments
- Information regarding availability of federal, state, or local aid, including the timing and material terms of any such aid
- Reports prepared for other governmental purposes

Further Considerations

In addition to these subjects, we suggest the following matters be considered when preparing disclosure of the impact of COVID-19 on a municipal issuer's financial and operating conditions:

- Have COVID-19-related circumstances such as remote work arrangements adversely affected the issuer's ability to maintain operations, including financial reporting systems, internal control over financial reporting and disclosure controls and procedures? What challenges does the issuer anticipate in its ability to maintain these systems and controls? Will the issuer's operations be materially impacted by any constraints or other impacts on its human capital resources and productivity? Have travel restrictions had a material impact on the issuer's operations?
- How does the issuer expect COVID-19 to impact its future operating results and near and long-term financial condition?
- Does the issuer expect to receive (or has the issuer received) any funding from the state or federal

government relating to the impacts of COVID-19? Is the issuer aware of any additional legislation, at the local, state, or federal level, or executive orders, enacted or issued in connection with COVID-19, that may materially affect its finances or operations?

- Has the issuer's cost of or access to capital and funding sources, such as revolving credit facilities or other sources, changed, or may it be reasonably likely to change?
- Does the issuer have any concern or uncertainty regarding its ability to pay debt service when due on any of its financial obligations? Does the issuer expect the COVID-19 pandemic to result in the default of any material contractual or financial obligation? If so, what is the nature of the obligation and what is the extent of such default?
- Does the issuer have any concern or uncertainty regarding its ability to access the debt markets, including with respect to its commercial paper or other short-term financing arrangements, or with respect to any terms of swap providers, including the valuation of collateral, and counterparty or customer risk? Is there uncertainty about the issuer's ongoing ability to comply with the covenants in its financial contracts and other agreements?
- If germane to the issuer's credit, is the issuer aware of an effect that COVID-19 may have on (i) the collection of property taxes or assessed values (e.g., relocation, closure, of a major property owner, significant property owner delinquencies, material assessment appeals, blanket assessment reductions, or property tax extensions), or (ii) income taxes, sales taxes, or any other key revenue sources?

Conclusion

The SEC Statement provides a useful guide for municipal issuers to develop effective disclosures on the current and projected impacts of COVID-19 on their financial and operating conditions. As issuers continue to monitor and assess the effects of the COVID-19 pandemic, the full fiscal impact on such issuers may change significantly in the coming months, particularly as budgets are considered for upcoming fiscal years (in many instances beginning July 1 or October 1). A voluntary filing may not be necessary or appropriate for some issuers; for others, it may be useful to make regular voluntary filings as circumstances change. We caution that any COVID-19-related disclosure should include appropriate disclaimers indicating that the information included is subject to change without notice, may be affected by future events and actions that may be outside the control of the issuer and that the issuer does not undertake to supplement the filing or disclosure for future events or circumstances.

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