

# Financial Services

Providing Strategic Legal Guidance to the Global Financial Services Industry

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## SEC Chairman Calls for Legal Bulletin on EMMA Disclosures

Is information posted on EMMA subject to greater scrutiny under the antifraud provisions of the federal securities laws than when posted only on an issuer's website?

That is the question raised by Securities and Exchange Commission Chairman Jay Clayton's introductory remarks to the SEC's Fixed Income Market Structure Advisory Committee on Monday, July 29. Chairman Clayton said that he had heard of issuers being advised that disclosing information through the Municipal Securities Rulemaking Board's EMMA municipal disclosure system triggered a "more rigorous liability standard for that information than disclosing the same information to investors through other means." Clayton said he had "significant questions about this advice" and whether it was correct as a matter of law and policy. He added that he would ask the SEC's Office of Municipal Securities to create a staff legal bulletin on the topic.

### BACKGROUND

The SEC's Rule 10b-5, which was promulgated in 1943 under the authority of Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act"), provides that it is unlawful "in connection with the purchase or sale" of a security "to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading." Section 17(a) of the Securities Act of 1933 (the "Securities Act") provides for similar misstatement or omission antifraud liability "in the offer or sale" of a security.

In 1975, both the Exchange Act and the Securities Act were amended in a number of ways. Among the changes was the so-called "Tower Amendment," which precludes the SEC and the MSRB from requiring filings, registration, or the provision of information by municipal issuers in connection with the sale of municipal securities. Also included in the 1975 amendments were changes that subjected municipal issuers to the antifraud provisions of Securities Act Section 17(a), Exchange Act Section 10(b) and SEC Rule 10b-5.



Prior to the promulgation of Rule 15c2-12 in 1989, issuers had no obligation to provide any sort of prospectus in connection with a public offering of municipal bonds; indeed, the Tower Amendment prevented the SEC from requiring such a thing. With Rule 15c2-12, the SEC used its ability to regulate securities broker-dealers to bring municipal securities disclosure to the primary market. The new rule required underwriters of municipal securities to obtain and review an “official statement” from the issuer containing the proposed terms of the securities and financial and operating data material to an evaluation of the offering and to send a copy of the official statement to any potential customer in the offering upon request.

In 1994, Rule 15c2-12 was amended to require not only primary market disclosure (the official statement) but also secondary market disclosure (so-called “continuing disclosure”). As with the original rule, the continuing disclosure provisions of Rule 15c2-12 achieve their aim through the regulation of broker-dealers rather than requiring or mandating issuer disclosure or registration, requiring underwriters to obtain from an issuer or obligated person a contractual undertaking to provide annual financial and operating information and to provide notices of certain material events to certain designated dissemination services. This requirement is similar to the reporting requirements for issuers under the Exchange Act, although the required disclosures are narrower in scope and the Rule recognizes a number of differences between municipal issuers and other types of issuers. The SEC has since expanded these continuing disclosure requirements to cover variable rate demand or tender obligations (which in earlier versions of the Rule were exempt) and has twice amended the rule to require disclosure of additional events. The SEC has also demonstrated more recent emphasis on continuing disclosure in its Municipalities Continuing Disclosure Cooperation Initiative (the “MCDC Initiative”), where more than 140 municipal issuers and other obligated persons were subject to Enforcement actions between 2014 and 2016.

After many years of experience and general dissatisfaction with private dissemination services, the MSRB created the EMMA website in 2008, and a year later the SEC designated EMMA as the official repository for municipal securities disclosures. The EMMA system is now widely regarded as an efficient, useful and easily accessible platform for disclosing and obtaining information about an issuer and its publicly traded securities. Particularly for issuers that do not maintain investor relations websites – which is the majority of them – EMMA is the first place investors look to for information.

## THE ISSUE

Do statements made through EMMA trigger a “more rigorous liability standard” than the same statements disclosed to investors through other means? It actually depends on a number of circumstances, including whether the statements are directed to investors and what is meant by “other means.” It is unlikely, however, that the SEC’s Division of Enforcement will focus on or distinguish between the mediums of dissemination as opposed to the content of the information provided.

It has long been recognized that a statement need not be directed specifically at investors to be subject to the antifraud provisions. Contemporaneously with its release of the proposed continuing disclosure amendments in 1994, the SEC issued a “Statement of the Commission Regarding Disclosure Obligations of Municipal Securities Issuers and Others” – known generally as the “interpretive release.” An expansive statement of the SEC’s view of municipal securities disclosure practices, the interpretive release contained two statements particularly relevant to this discussion. While municipal issuers are not required to comply with continuous reporting and disclosure practices required of public companies, when a municipal issuer does release information to the public “that is reasonably expected to reach investors and the trading markets, those disclosures are subject to the antifraud provisions.” Second, even if such statements are not published “for the purposes of informing the securities markets,” they may nonetheless give rise to antifraud liability under the Securities Act and the Exchange Act.



While statements made on EMMA, on an issuer's investor relations web page, in a press release, or on an issuer's general website, can all give rise to antifraud liability, a statement specifically directed to investors (such as through EMMA or on a specific investor relations page) may be more likely to be noticed or reviewed by investors and thus raise greater concern within the SEC's Division of Enforcement. This could be particularly true in the case of material omissions, which is the most typical concern for issuers. We can stipulate that very few issuers make false representations intentionally, whether on EMMA or otherwise, in connection with the purchase or sale of municipal securities. Municipal issuers sometimes face scrutiny, however, when they post completely accurate statements that are alleged to be incomplete for securities law purposes – *i.e.*, statements that omit to state other material facts necessary to make the otherwise accurate facts not misleading in light of the circumstances under which the statements are made.

The way in which a particular statement is published or otherwise communicated to investors can affect the degree to which additional statements are necessary to make the statement not misleading for securities law purposes. Issuers have many reasons to communicate, and by and large the constituents they intend to communicate with are not investors but rather the citizens and residents of their communities. It is not reasonable to expect that every statement published on an issuer's general government website be scrubbed by securities lawyers and examined in depth to ensure that it does not contain a material omission. Antifraud liability under the federal securities laws, however, ordinarily does not turn on where and how a statement is made or posted. Reasonable investors, as well as the SEC, are likely to expect that all statements, whether on EMMA or otherwise, are accurate and complete.

### LOOKING AHEAD

The SEC frequently receives requests from institutional investors and industry groups for more disclosure in the municipal market, and the SEC seems sympathetic to that view, even though the instances of defaults in the municipal market are quite low. At this point, the SEC, municipal investors, underwriters and even issuers appear to have largely coalesced behind EMMA as the site for disclosure of issuer information for investors.

Issuers, on the other hand, are often reluctant to post information on EMMA that is not legally or contractually required. Municipal issuers often do not have the resources to maintain a dedicated staff of securities disclosure professionals or to keep a securities lawyer on retainer to assist with secondary securities market disclosure issues including difficult questions of "materiality." Similarly, the accounting and other reporting systems of many municipal issuers are not set up to provide information as quickly or as completely as would typically be required in the corporate market, and for many municipal issuers, particularly small or infrequent issuers, requiring more sophisticated disclosure would impose a substantial burden on the issuers without clearly producing significant benefits. Nonetheless, those statements and other information that is posted on EMMA are unquestionably statements intended for the investment community, are not infrequently reviewed by the SEC, and need to be reviewed by the issuer with that in mind prior to such statements being posted.

The staff legal bulletin Chairman Clayton said he would request will likely clarify the SEC's view on the differences, if any, between communicating with investors through EMMA and communicating with investors through other means. Until such guidance is issued, however, municipal issuers and other obligated persons should assume that the SEC remains focused on continuing disclosure, as evidenced by the MCDC Initiative, and thus they should remain equally focused on the content and completeness of their disclosures.



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