

# HAWKINS ADVISORY

## MSRB AMENDS RULE G-34(c) AND IMPLEMENTS NEW MARKET DISCLOSURE REQUIREMENTS

### Overview

The Municipal Securities Rulemaking Board (the “MSRB”) has announced that amendments to MSRB Rule G-34(c), relating to the collection and dissemination of market information with respect to variable rate securities (the “Amended Rule”),<sup>1</sup> will become effective on May 16, 2011 (the “Effective Date”), subject to a transition provision as described below. The Amended Rule requires certain brokers, dealers, and municipal securities dealers (collectively, “dealers”) to submit and file with the MSRB additional market information and certain documentation associated with municipal auction rate securities (“ARS”)<sup>2</sup> and variable rate demand obligations (“VRDOs”).<sup>3</sup> All documentation is to be submitted via the MSRB’s short-term obligation rate transparency system (the “SHORT System”).

A detailed overview of the Amended Rule and its implementation is provided in MSRB Notice 2010-31 as supplemented with respect to document submission by MSRB Notice 2011-17.

The objective of the Amended Rule is to add ARS bidding information and additional VRDO information to the information currently collected and disseminated and to provide the market with a centralized source of documents that define critical aspects of VRDO liquidity provisions and ARS auction procedures and interest rate setting mechanisms.<sup>4</sup> In the case of VRDOs, MSRB Notice 2011-17 explains that such critical items include, without limitation, (i) the “termination provisions” detailing circumstances when the obligation for a liquidity provider to provide liquidity is no longer applicable, (ii) the “notification period” that details the length of time that may lapse between a VRDO holder tendering a position in the security and a liquidity provider purchasing the tendered

security, and (iii) the “term out period” showing, if any, the time period that principal held with the liquidity provider (as a “bank bond”) would be amortized.

Dealers must submit new or amended versions of required documents within five business days after they are made available to the Program Dealer (defined below) or Remarketing Agent, as applicable. Dealers must also submit any renewals, amendments, or supplements to any of the required documents on an ongoing basis.

There will be a transition period of 90 business days for documents in effect prior to the Effective Date. For such documents, dealers have until September 22, 2011 to make the required submissions, and dealers must submit any future, subsequently amended or new versions of such documents within five business days of their receipt. Note that for VRDO documents (but not ARS documents) subject to the transition period, a dealer need only use its best efforts to obtain current versions of the required documents, but if such documents cannot be obtained, a dealer must keep a record detailing its efforts for three years under MSRB Rule G-8 (Books and Records) and file a notice with the SHORT System stating that the required documents could not be acquired.

### Applicable Dealers

Rule G-34(c), both before and after the amendments, applies to the following classes of dealers: (i) in the case of ARS, each broker, dealer, or municipal securities dealer that submits an order directly to an Auction Agent for its own account or on behalf of another account to buy, sell, or hold an ARS through the auction process (a “Program Dealer”) and (ii) in the case of VRDOs, each Remarketing Agent.

*continued*

<sup>1</sup> MSRB Notice 2011-17 (Feb. 23, 2011), available at <http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2011/2011-17.aspx> (“MSRB Notice 2011-17”). The Amended Rule was approved by the Securities and Exchange Commission in SEC Rel. No. 34-62755 (Aug. 20, 2010), available at <http://www.sec.gov/rules/sro/msrb/2010/34-62755.pdf>.

<sup>2</sup> The MSRB defines ARS as municipal securities in which the interest rate resets on a periodic basis under an auction process conducted by an agent responsible for conducting the auction process on behalf of the issuer or other obligated person with respect to such ARS (the “Auction Agent”) that receives orders from dealers. MSRB Rule G-34(c)(i).

<sup>3</sup> The MSRB defines VRDOs as securities in which the interest rate resets on a periodic basis with a frequency of up to and including every nine months, an investor has the option to put the issue back to the trustee, tender agent or other agent of the issuer or obligated person at any time, typically with specified advance notice, and a dealer acts as a remarketing agent (the “Remarketing Agent”) responsible for reselling to new investors securities that have been tendered for purchase by a holder. MSRB Rule G-34(c)(ii).

<sup>4</sup> MSRB Notice 2010-31 (Aug. 26, 2010), available at <http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2010/2010-31.aspx> (“MSRB Notice 2010-31”) and MSRB Notice 2011-17.

### Applicability of Current Rule

Rule G-34(c) currently requires Program Dealers and Remarketing Agents to report certain market information following ARS auctions or VRDO interest rate resets to the SHORT System by 6:30 p.m. Eastern Time on the day the auction or interest rate reset occurs.<sup>5</sup> The following disclosure requirements represent key identifying and descriptive market information that will remain in effect under, and be augmented by, the Amended Rule.

**ARS Auctions.** The market information required to be reported for an ARS auction includes (i) the CUSIP number; (ii) the interest rate produced by the auction process and whether the interest rate is a maximum rate, all hold rate, or rate set by auction; (iii) the identity of all Program Dealers that submitted orders (including hold orders); (iv) the date and time of the auction; (v) the length of time that the interest rate produced by the auction process is applicable; (vi) the minimum denomination; (vii) the minimum and maximum rates, if any, applicable at the time of the auction (or an indication that such rate or rates are not calculable at the time of auction); and (viii) the date and time the interest rate determined as a result of the auction process was communicated to Program Dealers.<sup>6</sup>

**VRDO Interest Rate Resets.** The market information required to be reported for VRDO interest rate resets includes (i) the CUSIP number; (ii) the interest rate and whether the interest rate is a maximum rate, set by formula or set by the Remarketing Agent; (iii) identity of the Remarketing Agent; (iv) date and time of the interest rate reset; (v) length of time that the interest rate is applicable; (vi) minimum denomination; (vii) the length of notification period; (viii) the minimum and maximum rates, if any, applicable at time of the interest rate reset (or an indication that such rate or rates are not calculable at the time of the interest rate reset); and (ix) the type and expiration date of each liquidity facility applicable to the VRDO.<sup>7</sup>

### Amended Rule

With the adoption of the Amended Rule, dealers will be required to make additional market disclosures, as well as certain document submissions.

**Additional Market Disclosures.** For ARS auctions, new market disclosures focus on key bidding details, including regarding how the interest rate was determined for an auction. Specifically, the Amended Rule requires Program Dealers to disclose the following:

- (i) interest rates and aggregate par amounts of orders to buy or sell at any interest rate, or to hold at a specific interest rate, and the aggregate par

amount of such orders that were successfully executed or held;

- (ii) interest rates, aggregate par amounts, and types of orders (buy, sell, or hold) by a Program Dealer for its own account and the aggregate par amounts of such orders, by type, that were executed; and

- (iii) interest rates, aggregate par amounts, and types of orders (buy, sell, or hold) by an issuer or conduit borrower for the subject ARS.<sup>8</sup>

For VRDO interest rate resets, Remarketing Agents will be required to disclose the effective date that the interest rate reset is applicable, as well as certain information available to the Remarketing Agent at the time of the interest rate reset, including the following:

- (i) the identity of the tender agent and liquidity provider (as well as identifying which VRDOs have issuers, conduit borrowers or affiliates providing “self liquidity” and the identity of the party providing such self-liquidity); and

- (ii) the par amount of the VRDO, if any, held by a liquidity provider (par amount held as “Bank Bonds”) or held by parties other than a liquidity provider, including the par amounts held by the Remarketing Agent and by investors.<sup>9</sup>

**Document Submissions.** Under the Amended Rule, Program Dealers and Remarketing Agents are required to submit certain documents to the SHORT System. Documents defining auction procedures and interest rate setting mechanisms must be submitted for ARS, while documents consisting of liquidity facilities, such as letters of credit, stand-by bond purchase agreements and any other documents that establish an obligation to provide liquidity, are to be submitted for VRDOs.

MSRB Notice 2011-17 contemplates that multiple documents may contain these key terms and the SHORT System will allow dealers to submit multiple documents in order to comply with the Amended Rule. For example, with respect to letters of credit composed of a reimbursement agreement and the letter of credit, both documents would need to be submitted to make clear that the collection of documents relates to the same letter of credit agreement. The Notice also explains that, under the Amended Rule, summaries of documents, such as those contained in official statements, will not satisfy the document submission requirements.<sup>10</sup>

<sup>5</sup> MSRB Rule G-34(c)(i)(A)(2) and MSRB Rule G-34(c)(ii)(A)(2).

<sup>6</sup> MSRB Rule G-34(c)(i)(A)(1)(a)-(h).

<sup>7</sup> MSRB Rule G-34(c)(ii)(A)(1)(a)-(i).

<sup>8</sup> MSRB Rule G-34(c)(i)(A)(1)(i)-(m).

<sup>9</sup> MSRB Rule G-34(c)(ii)(A)(1)(i)-(k).

<sup>10</sup> See MSRB Notice 2011-17.

In MSRB Notice 2011-17, the MSRB provides some guidance on the new document filing requirements for VRDO issues. As described above, in addition to letters of credit and stand-by bond purchase agreements, the Amended Rule creates a third category of documents that must be submitted for VRDO issues, namely “any other documents that establish an obligation to provide liquidity”, i.e. any documents constituting a liquidity facility other than letters of credit and stand-by bond purchase agreements. MSRB Notice 2011-17 explains that this category is intended to include VRDO liquidity facilities where an issuer, conduit borrower, or affiliate provides “self liquidity” and thus, for example, would require the filing of a financing agreement which obligates a conduit borrower to purchase tendered bonds which are not remarketed.

#### Other Considerations

There are certain other aspects of the Amended Rule that dealers will want to consider.

All submitted documents must be PDF files. Those documents entered into and produced prior to the Effective Date will not be required to be word-searchable.

A document that contains information that was not intended to be made public is not exempt from submission under the Amended Rule. However, dealers will be permitted to redact, on a limited basis, information intended to remain confidential in order to maintain internal security or the confidentiality of personal information, including fees, staff names and contact information for making a request to use a VRDO liquidity facility, as well as information that could be used in a fraudulent manner (such as VRDO liquidity facility bank routing or account numbers). Any redaction must be kept to a minimum and must not include information that would reasonably be assumed to be used by investors or other market participants in evaluating an ARS or VRDO.

#### About Hawkins Advisory

The Hawkins Advisory is intended to provide occasional general comments on new developments in Federal and State law and regulations which we believe might be of interest to our clients. Articles in the Hawkins Advisory should not be considered opinions of Hawkins Delafield & Wood LLP. The Hawkins Advisory is not intended to provide legal advice as a substitute for seeking professional counsel; readers should not under any circumstance act upon the information in this publication without seeking specific professional counsel. Hawkins Delafield & Wood LLP will be pleased to provide additional details regarding any article upon request.

This Hawkins Advisory is not intended or written to be used, and cannot be used, by a taxpayer for the purpose of avoiding penalties that the Internal Revenue Service may impose on the taxpayer.

Additional copies of this Hawkins Advisory may be obtained by contacting any attorney in the Firm.

##### New York

One Chase Manhattan Plaza  
New York, NY 10005  
Tel: (212) 820-9300

##### San Francisco

One Embarcadero Center, Suite 3820  
San Francisco, CA 94111  
Tel: (415) 486-4200

##### Newark

One Gateway Center, 24<sup>th</sup> Floor  
Newark, NJ 07102  
Tel: (973) 642-8584

##### Hartford

20 Church Street, Suite 700  
Hartford, CT 06103  
Tel: (860) 275-6260

##### Los Angeles

333 South Grand Avenue, Suite 3650  
Los Angeles, CA 90071  
Tel: (213) 236-9050

##### Sacramento

1415 L Street, Suite 1180  
Sacramento, CA 95814  
Tel: (916) 326-5200

##### Washington, D.C.

601 Thirteenth Street, N.W., Suite 800 South  
Washington, D.C. 20005  
Tel: (202) 682-1480

*Hawkins*  
DELAFIELD & WOOD LLP