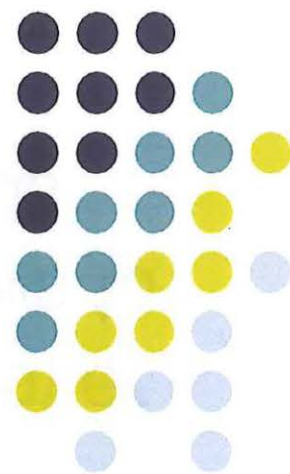


CITY AND COUNTY OF SAN FRANCISCO BOARD OF SUPERVISORS

Disclosure Responsibilities of Board Members under Federal Securities Laws





Introduction

- Presentation will provide training and cover the applicability of federal securities laws to Board Members when authorizing bonds
- What you will learn:

Applicable Securities Law

- What's the Law

Official Statement

- What it is
- City's Document

Discharge Your Duty

- Review and Approve OS, or
- Reasonable Reliance



Securities Law Overview

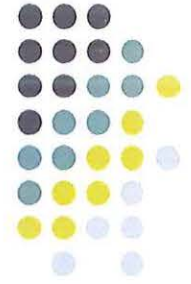
- Disclosure Contexts
- Disclosure Standards
- SEC and Private Litigation

SEC Jurisdiction in Municipal Securities Arena



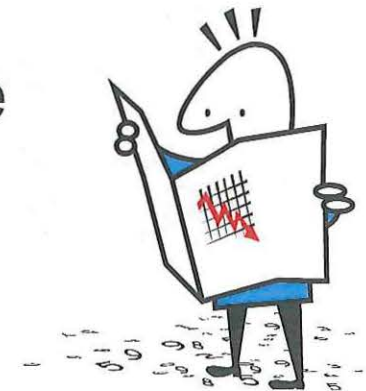
- No securities registration
- Antifraud provisions apply
- Regulate municipal securities brokers and dealers (Rule 15c2-12)





Disclosure Contexts

- Primary
 - Preliminary and final Official Statements (our focus today)
- Secondary
 - Rule 15c2-12 Continuing Disclosure Agreements
 - Voluntary Filings
 - Investor Information Webpage
- Communications “reasonably expected to reach investors”

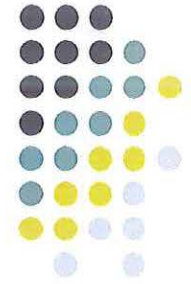




Disclosure Standard

- Rule 10b-5

“unlawful for any person . . . 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 the light of the circumstances under which they were made, not misleading”



Disclosure Standard (cont.)

- Material

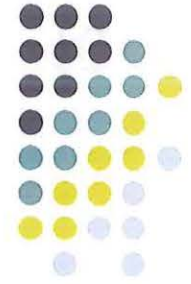
“substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable [investor].”



Litigation

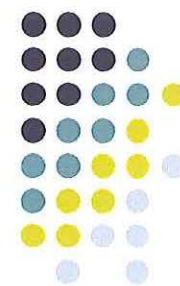
- SEC
 - administrative
 - civil
 - criminal (referral to Department of Justice)
- Private Plaintiff





Rule 10b-5 SEC Action

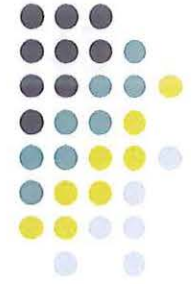
- a materially misleading misstatement or omission
- made or omitted with scienter (fraudulent intent or recklessness)
- in connection with the purchase or sale of a security



Rule 10b-5 Private Action

- 3 SEC elements
plus
- damages
- reliance on misleading disclosure





SEC Enforcement Actions

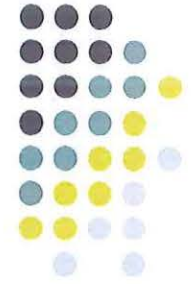
- The governmental issuer (i.e., the City)
- Individual Board Members
- Governmental officials and employees
- Third parties (e.g., underwriters, financial advisors, bond counsel, disclosure counsel)
- SEC can also bring an action under Section 17 of 33 Act: (a)(1) - fraudulent intent or recklessness; (a)(2) or (a)(3) - negligence



Guidance for Board Members



- Potential liability of City for materially misleading disclosure in any of the contexts we discussed
 - Official Statements
 - filings with EMMA (contractual and voluntary)
 - broadly, any communications “reasonably expected to reach investors”
- But SEC guidance for Board Members limited to Official Statements
 - Orange County Report

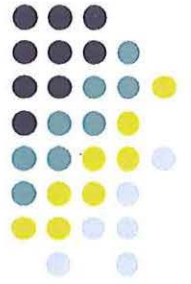


Orange County Report (1996)

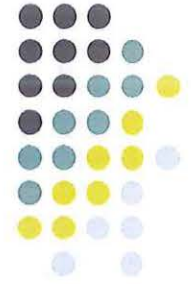
- Nature of misleading disclosure:

concerned false and misleading statements in the offer and sale of over \$2.1 billion of municipal securities over 1993 and 1994 involving investment pool strategy, the risks of their investment strategy and investment results; Orange County's reliance on the investment results for the County's financial condition

Orange County Report (1996)

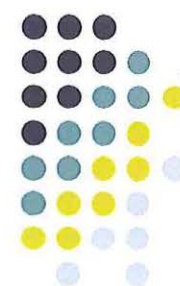


- “a public official may not authorize disclosure that the official knows to be false”
- “nor may a public official authorize disclosure while recklessly disregarding facts that indicate that there is a risk that the disclosure may be misleading”



Orange County Report (1996)

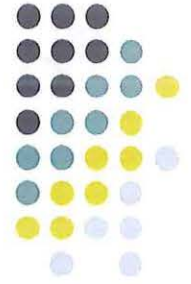
- *What is “acting recklessly”?*
 - public official has knowledge of facts bringing into question the issuer’s ability to repay the securities
 - fails to take steps appropriate under the circumstances to prevent the dissemination of materially false or misleading information regarding those facts



Orange County Report (1996)

- “such steps could have included becoming familiar with the disclosure documents and questioning the issuer’s officials, employees or other agents about the disclosure of those facts.”

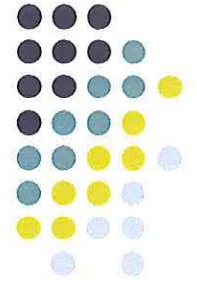




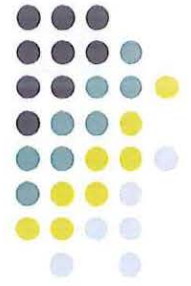
Board Responsibility

- If there are material adverse financial trends of which you are aware (or objectively should have been aware), issuer should reasonably investigate that trend

Recent Municipal Securities Enforcement Cases



- Town of Ramapo, New York
- Westlands Water District (Fresno, CA)
- City of Miami
- Port Authority of New York and New Jersey



Significance of Recent Enforcement Actions

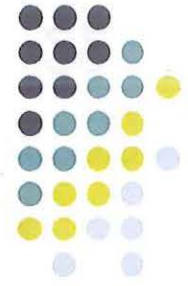
- Holding individuals liable, and seeking both personal financial penalties and industry bars from the municipal finance business
- Imposing significant fines on municipal issuers (not simply disgorgement)
- Corresponding criminal conviction in connection with municipal bond offerings and possible jail term for public official (Ramapo)
- Bringing first jury trial against a municipality and public official for securities law violations (Miami)
- Requiring a municipal issuer to admit wrongdoing in an SEC enforcement action (Port Authority)

Takeaways from Recent Enforcement Action



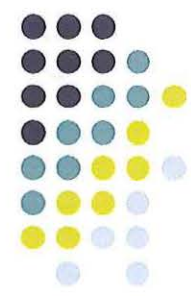
- Theme in several of the enforcement actions: don't try to hide low fund balances or weak revenues
- No payment defaults experienced in any of the bond issues
- Written Disclosure Controls and Procedures important to have in place

Why Disclosure Controls and Training?

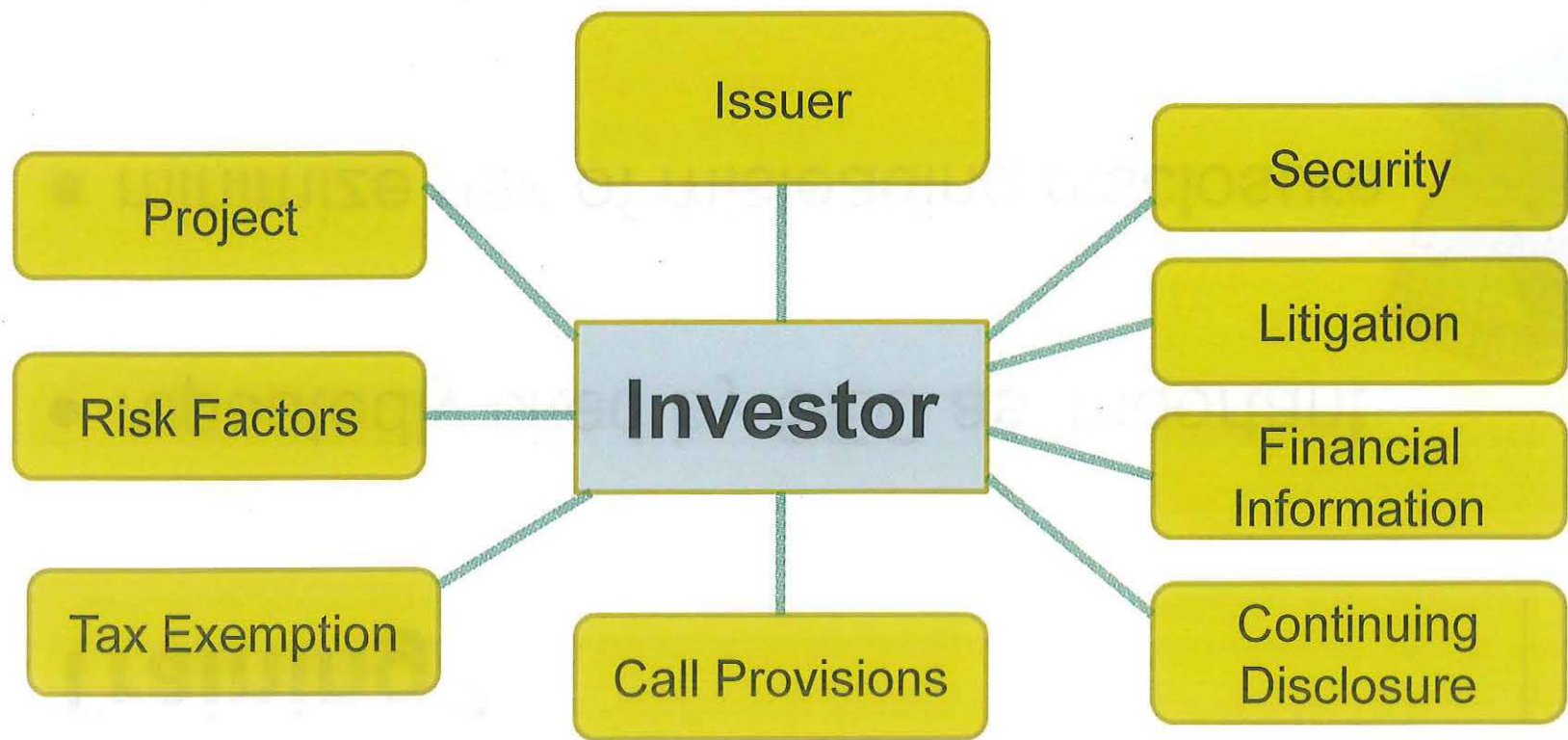


- repeatedly cited by SEC as important
- minimize risk of misleading disclosure
- help to defend against charge of negligence or recklessness





Official Statement

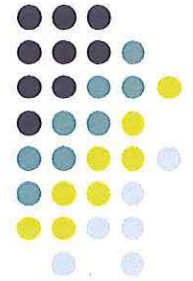




Official Statement Observations

- **Observation 1:** Investors/SEC have exquisite *20/20 hindsight!*
- **Observation 2:** To disclose or not to disclose
- see observation 1
- SEC can impose civil penalties and make criminal referrals to DOJ

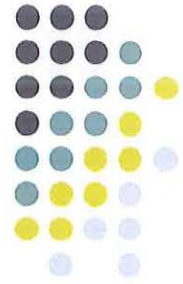




Official Statement

Two Approaches:

- Approve the Text
- Authorize Staff to Prepare and Approve (“Reasonable Reliance”)



Official Statement Approval

Basic Inquiries:

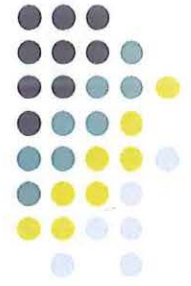
- What is the purpose of the bond issue?
- What is the source of payment of the bonds?
- What are the risks that the source of payment may be insufficient to repay the bonds?
- Are there any factors that could pose a material risk to issuer's financial position?

Official Statement Approval (cont.)



- Do I have knowledge of any other events that would affect the deliberation of a reasonable investor?
- Have such risks and events been brought to the attention of our staff, disclosure counsel, bond counsel and other professionals?
- Have such risks and events been disclosed, and if not what is the rationale for the non-disclosure?

Official Statement Approval (cont.)



- Have we contractually agreed to provide continuing disclosure with respect to this bond issue, and if we have, who is responsible and what are the procedures for preparing and distributing the information?
- In reviewing the “relevant portions” of the OS, are there any “red flags” that should be brought to the attention of the financing team and/or for which I as a Board member would like a further explanation?

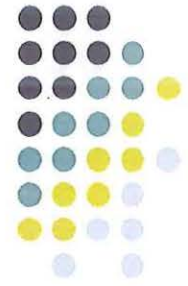
Authorize Staff to Prepare and Approve OS



Can't I simply rely on staff and professionals?

1. Do we have written disclosure controls and processes? If we do, am I satisfied that the processes followed in preparing the disclosure document have been reasonably designed to produce accurate and reliable information?
2. Do I have a reasonable basis to have confidence in the integrity and competence of finance professionals ?

Authorize Staff to Prepare and Approve OS (cont.)



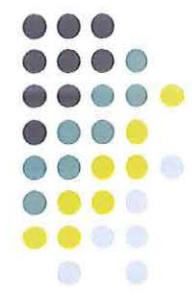
3. Do I know anything that would cause me to question the accuracy of the disclosure or that would indicate that there is a risk that those disclosures may be misleading?
4. With reference to the disclosure documents, do I know of any potentially material issues or “red flags” that should be brought to the attention of management or for which I would like further explanation?





City's Disclosure Controls

- Written Disclosure Policies and Procedures
- Disclosure Training
- Establishment of Disclosure Practice Working Group, incl. Director of Public Finance
- Engagement of General Disclosure Counsel
- Deputy City Attorney for Disclosure



The End

