



National Association of State Auditors, Comptrollers and Treasurers

November 15, 2012

Mary L. Schapiro, Chairwoman
Members of the Commission
U.S. Securities and Exchange Commission
SEC Headquarters
100 F Street, NE, Room 10700
Washington, DC 20549

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Dear Chairwoman Shapiro and Members of the Commission:

On behalf of the National Association of State Auditors, Comptrollers and Treasurers, I am writing in response to the recent report issued by the U.S. Securities and Exchange Commission on the municipal securities market. We share the Commission's belief that an efficient and well-informed municipal market is critical. NASACT and other state government organizations were major supporters of establishing the Municipal Securities Rulemaking Board's Electronic Municipal Market Access (EMMA) System, and we continue to support EMMA and to promote other voluntary efforts to improve disclosure.

In its report, the Commission makes a series of recommendations aimed at fulfilling its mission of protecting investors while also addressing the concerns of market participants. We commend the Commission for its extensive overview and study of the market and share the Commission's view that improvements in transparency and disclosure can enhance the current function of the municipal securities market.

We believe, however, that further improvements to the market can be achieved without statutory changes. To this end, NASACT has established a group to specifically work on enhanced disclosure. We will be exploring various avenues that states can take to make information more quickly and more readily available to the investor community. We also believe that in these times of unprecedented federal deficits and reductions in government, any new costs must address a compelling need. We oppose intervention by Congress, the Commission or any other federal entity that would impose federal oversight on municipal issuers and attempt to treat governmental entities like private sector corporations or that would impose new costs on all levels of government.

We also remain adamantly opposed to any federal actions that would erode states' authority over their financial reporting and diminish the independence of the states' designated standard setter, the Governmental Accounting Standards Board (GASB). Specifically, we strongly object to the Commission's recommendations that it be granted additional statutory authority over municipal issuer disclosure, including designating a state or local government's accounting standard setter and controlling the form and content of an issuer's financial statements. We believe that these recommendations violate states' rights and the basic premise of federalism.

Disclosure and financial reporting are very important aspects of assuring accountability and transparency in our markets, and we fully support voluntary efforts to further those objectives. We believe there are many ways that the Commission and other important market participants can work together to achieve better and more robust disclosure in the marketplace without federal legislation or regulation, and we look forward to participating in those initiatives.

The following pages contain comments that specifically address several of the Commission's recommendations contained in the July 2012 report.

Respectfully,

Martin J. Benison
NASACT President

**Comments from NASACT on the SEC's
"Report on the Municipal Market," dated July 31, 2012**

Authorize the Commission to require that municipal issuers prepare and disseminate official statements and disclosure during the outstanding term of the securities, including timeframes, frequency for such dissemination and minimum disclosure requirements, including financial statements and other financial and operating information, and provide tools to enforce such requirements.

The Commission reasons that its limited authority over issuers has hindered its ability to effectively improve disclosures and practices in the municipal securities market; therefore, the Commission recommends that it be given greater statutory authority directly over issuers.

We oppose the Commission's involvement in setting standards for the financial and operating information of state and local governments and believe that voluntary initiatives already underway can, and are, making significant improvements to disclosure practices. NASACT and many other state and local organizations were a major supporter of the creation of a disclosure database (originally under the auspices of the Municipal Advisory Council of Texas and now known as the Municipal Securities Rulemaking Board's Electronic Municipal Market Access [EMMA] system). EMMA has become an invaluable resource for investors, and we support continued voluntary enhancements to EMMA that would improve disclosure in the marketplace. We believe that enhancements such as the addition of URL links to an entity's investor relations page or to important financial information have given the investor efficient access to a myriad of information already made available by governments. Additionally, we believe that best practices, such as those established by the Government Finance Officers Association (GFOA) and favorably referred to in the Commission's report, are an effective way to encourage governments to produce more timely financial statements and make other interim financial information more readily available to investors.

Market participants continually work toward better disclosure and often seek to address areas of specific concern to the Commission. For example, a wide array of market participants came together in a recent effort sponsored by the National Association of Bond Lawyers (NABL) to address pension disclosure. NABL's Municipal Market Task Force on Public Pension Disclosure developed considerations for issuers and bond council in preparing disclosure of pension funding obligations in official statements. The task force proved that various participants in the municipal arena could work together to achieve an agreed-upon set of considerations that will bring additional information to the marketplace.

We commend the Commission for recognizing that a one-size-fits-all approach to disclosure is simply not feasible or desired, but we remain concerned about the Commission's reference to timeliness of financial information in its recommendation. As we have relayed to Commissioner Elisse Walter and other Commission staff in a meeting on March 10, 2010, and in a subsequent conference call on May 25, 2011, there are fundamental and significant differences between public and private sector financial reporting that make meeting corporate-like disclosure standards infeasible. Some of these differences include:

- Multiple sets of financial statements – State and local governments prepare entity-wide financial statements and fund-level statements. Differences between the two sets of financial statements must be reconciled. Private sector financial statements generally only contain entity-wide, or consolidated, financial statements.

- Multiple bases of accounting – Typical state and local government financial statements contain at least three different bases of accounting: accrual, modified accrual, and budgetary. Private sector statements, by contrast, generally contain only one basis of accounting: accrual.
- Materiality levels – Government auditors generally use lower materiality levels, which results in more testing (time) due to requirements in *Government Auditing Standards* and the use of “opinion units” prescribed by audit guidance issued by the American Institute of Certified Public Accountants. Auditors of private sector companies generally assess materiality at entity-wide or consolidated levels, which generally results in a much higher threshold for materiality.
- Component units – Governments are required to include certain component units (e.g., colleges and universities) in the comprehensive annual financial report (CAFR). In addition, component units have component units (e.g., a medical foundation of a university hospital). Completing the audits of the financial statements of all component units and incorporating the data into the state’s CAFR takes a significant amount of time and is often the source of delays. Any changes to the legal status of component units would require legislative action in most cases. This type of structure simply does not exist in the typical corporate model.

While we agree that improvements in the timeliness of financial statements can be made, preparing financial statements in 30 or 60 days, similar to the private sector, is simply not realistic or possible for governments given the differences described above. NASACT is currently exploring how unaudited cash-based or budget-based financial information can be provided on government websites to provide more timely information to investors. Specifically, the following four items could provide more timely financial information to investors:

1. Budget-to-actual operations, showing major categories of revenues and expenditures, for the general fund and major governmental and enterprise funds, year-to-date, and an explanation of the major variances.
2. Cash receipts and cash disbursements in the general fund and major governmental and enterprise funds, year-to-date, compared to the previous fiscal year.
3. Balances and changes in long-term and short-term debt, year-to-date.
4. Significant events (e.g., a major change in tax laws that would have a substantial effect on financial condition, etc.).

Efforts are already underway in some states to develop web pages geared specifically toward educating investors and that contain much of the suggested information. We support such initiatives and encourage all governments to provide information that would be helpful to current or future municipal bondholders.

Amend the municipal securities exemptions in the Securities Act and Exchange Act to eliminate the availability of such exemptions to conduit borrowers who are not municipal entities under Section 3(a)(2) of the Securities Act, without differentiation based on the size of the financing due to the continuing availability of other exemptions, including those available for small businesses, private offerings, and non-profit entities that take into account different types of offerings and issuers.

If, as the SEC report points out, the majority of defaults in the municipal securities market are in conduit revenue bonds issued for non-governmental purposes, and it is these same issuers that have provided substantially less continuing information, then we propose that the SEC focus on

the conduit borrowers. We agree with the market participants who thought that the same registration requirements and disclosure standards that apply to other non-governmental issuers selling securities directly in the corporate securities market should apply to non-governmental conduit borrowers.

Authorize the Commission to establish the form and content of financial statements for municipal issuers who issue municipal securities, including the authority to recognize the standards of a designated private-sector body as generally accepted for purposes of the federal securities laws, and provide the Commission with attendant authority over such private-sector body.

The Commission is specifically seeking authority to establish the form and content of financial statements used in municipal securities offerings, establish standards, and designate a private-sector body as the GAAP standard setter for municipal issuer financial statements. NASACT **strongly objects** to this recommendation and finds it particularly disturbing, as it is a direct infringement of states' rights. The content and scope of disclosed financial information varies substantially among the types of issuers, types of issues, and sources of repayment. It is the role of the states, not the federal government to set the form and content of financial statements.

Further, governments have an important responsibility to be accountable to the taxpayers for the use of their resources. Public accountability is a significantly different objective than is found in the business environment, and the need for accounting standards that reflect the unique nature of government is widely recognized and one of the primary reasons that the states have statutory and/or regulatory authority to promulgate accounting standards within their respective jurisdictions. The states delegated that authority to the Government Accounting Standards Board (GASB) in 1984; however, the authority to set accounting standards still resides with the states.

GASB was specifically established by 10 national state and local government associations to meet the goal of having a national and independent standard-setter that is focused on the needs of the state and local financial statement users. Any federal authority over the GASB is a violation of federalism, and we **adamantly oppose** any attempt by the federal government, including Congress, to override or interfere with GASB's independent standard-setting process.

Authorize the Commission, as it deems appropriate, to require municipal securities issuers to have their financial statements audited, whether by an independent auditor or a state auditor.

While audited financial statements are a reasonable expectation of investors, and we encourage municipal securities issuers to have their financial statements audited, such a requirement should remain part of a state's financial framework and should not be dictated by the federal government.

Provide a safe harbor from private liability for forward-looking statements of repeat municipal issuers who are subject to and current in their ongoing disclosure obligations that satisfy certain conditions, including appropriate risk disclosure relating to such forward-looking statements, and if projections are provided, disclosure of significant assumptions underlying such projections.

In some circumstances, forward-looking information can be useful to an investor; however, some governments have notated a legal risk in providing such information to the public. Changes in leadership, revenue sources driven by the economy, natural disasters and dollars controlled by changing elected officials are just a few of the reasons for uncertainty in forward-looking information. It is imperative that the user understand the nature of the information and the potential risks of relying on such uncertain information. Therefore, we generally support initiatives that protect the government from risks inherent in providing forward-looking information to the public.

Permit the Internal Revenue Service to share with the Commission information that it obtains from returns, audits, and examinations related to municipal securities offerings in appropriate instances and with the necessary associated safeguards, particularly in instances of suspected securities fraud.

While we support efforts to address securities fraud, we cannot support this recommendation without more specifics as to how the information would be shared and utilized.

To provide a mechanism to enforce compliance with continuing disclosure agreements and other obligations of municipal issuers to protect municipal securities bondholders, authorize the Commission to require trustees or other entities to enforce the terms of continuing disclosure agreements.

We oppose federal authority over state and local governments. We believe that the existing requirement that underwriters enter into continuing disclosure agreements with the issuer and the continued voluntary improvements in compliance being achieved through best practices and other initiatives can address compliance issues without the additional regulation of municipal issuers.

The Commission could host market participants, regulators, and academics at an annual conference on the municipal securities markets.

We are very supportive of efforts to enhance knowledge and share ideas and best practices. The Municipal Securities Rulemaking Board hosts an industry bi-annual roundtable where market participants discuss current developments in the municipal securities market. We have found this roundtable to be an appropriate venue to explore issues of common concern and to discuss possible solutions. Such initiatives are an effective way for market participants and regulators to understand every side of an issue in a more collaborative atmosphere.

The Commission could consider issuing updated interpretive guidance regarding disclosure obligations of municipal securities issuers and others.

The Commission has used its interpretive guidance as a tool to provide market participants with further clarification of the SEC's views on disclosure of municipal market participants in meeting their responsibilities under the antifraud provisions of the federal securities laws. As the guidance has not been updated since 1994, it would make sense for the Commission to review the existing guidance and consider updates to areas that the Commission believes warrant further attention.

The Commission could consider amendments to Exchange Act Rule 15c2-12 to further improve the disclosures made regarding municipal securities.

The Commission and other market participants have identified a number of areas where they believe improvements could be made in disclosure with respect to both primary and secondary offerings. The Commission's report suggests amendments to Rule 15c2-12 in the following manner:

- Amend the definition of final official statement to include required disclosure about the terms of the offering, including the plan of distribution, any retail order period, and the price to be paid for the municipal securities in the initial issuance;
- Mandate more specific types of disclosures in municipal securities official statements and ongoing disclosures, including event disclosures relating to issuance of new debt (whether or not subject to Rule 15c2-12 and whether or not arising as a result of a municipal securities issuance), primary offering disclosures relating to risks of the municipal securities, and disclosures about underlying obligors (regardless of the existence of credit enhancement or insurance);
- Provide a method to address noncompliance issues regarding continuing disclosure undertakings, including possibly by adding conditions that would require that issuers have disclosure policies and procedures in place regarding their disclosure obligations, including those arising under continuing disclosure undertakings;
- Consider modifications regarding application of the rule to demand securities and underwritten municipal fund securities offerings; and
- Improve the accessibility of disclosures, including the use of shortened or summary official statements and increased use of websites.

We do not have any comments at this time concerning the recommended amendments to 15c2-12, but we will participate in the due process if such changes are proposed. In addition, we will closely monitor any SEC activity that would impose greater disclosure requirements on state and local governments.

The Commission should continue to work with the MSRB to strengthen its rules and further enhance EMMA.

We continue to support EMMA as a vital source of comprehensive source of information on municipal securities and support voluntary enhancements that would bring more transparency to the marketplace. Specific changes to MSRB rules would warrant additional review and consideration.

Municipal market participants should follow and encourage others to follow existing industry best practices and expand and develop additional best practices guidelines in a number of areas to enhance disclosures and disclosure practices in the municipal securities market.

We are very supportive of industry best practices which enhance disclosure and disclosure practices in the marketplace. As noted in the report, the Commission recognizes that there are a number of groups that have developed industry best practices and voluntary disclosure guidelines to improve the level and quality of disclosure. For example, NASACT encourages states to share the most promising practices on NASACT's website including information regarding quarterly disclosure of unaudited financial information. Additionally, NASACT provides a number of opportunities for members to discuss financial reporting throughout the year. GFOA also hosts a very robust best practice, policy, and certificate and award program that guides issuers in developing financial reporting and disclosure policies and practices.

NASACT continues to explore avenues for states to publish more timely CAFRs. In addition, NASACT recently established a group to further determine the barriers that exist for governments to provide unaudited financial information to the public and will continue seeking to overcome barriers so that states can develop more robust investor websites and resources.