American Bankers Association®

Cristeena Naser
Vice President
Center for Securities, Trust & Investments
202-663-5332
cnaser@aba.com

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VIA ELECTRONIC MAIL

Lisa Good, Executive Director
National Federation of Municipal Analysts
P.O. Box 14893
Pittsburgh, Pennsylvania 15234

Re: Recommended Best Practices in Disclosure for Direct Purchase Bonds, Bank Loans, and Other Bank-Borrower Agreements

Dear Ms. Good:

The American Bankers Association (ABA)[1] appreciates the opportunity to comment on the draft Recommended Best Practices in Disclosure for Direct Purchase Bonds, Bank Loans, and Other Bank-Borrower Agreements (RBP) published by the National Federation of Municipal Analysts (NFMA) to address what the NFMA sees as a deficiency in current practices in the disclosure of bank lending products (collectively, "bank loans"). ABA members regularly purchase municipal obligations directly from the obligors and extend the kinds of loans and other credit accommodations that are the subject of the RBP. In addition, many of our members provide services as regulated municipal securities dealers, either through separately identifiable departments in commercial banks or through broker-dealer affiliates of commercial banks.

The RBP advocates increased disclosure and transparency of bank loans in the municipal marketplace, and ABA generally supports that goal. That said, certain of our members defer to the relevant obligor in matters of bank loan disclosure, believing that disclosure is the purview of the obligor alone, while still other members affirmatively encourage obligors to post redacted bank loan documentation on the Municipal Securities Rulemaking Board's EMMA website to ensure transparency. ABA appreciates that constituents of the NFMA have an interest in the financing activities of municipal obligors. At the same time, we believe that disclosure and transparency of bank loans is achievable without prejudicing the interests of other constituents of the municipal marketplace, particularly the interests of the municipal entities and obligated persons (collectively, obligors) with whom ABA's and the NFMA's members do business.

As discussed more fully below, to the extent consistent with the wishes of the relevant obligor, ABA supports the prompt disclosure of bank loans following closing. We believe that advance disclosure and summary form disclosure are not required to achieve transparency and will plainly increase the transaction costs associated with bank loans, making them less attractive for municipal borrowers. Rather, a careful balancing of the interests of all constituents will engender good will among market participants and inspire the transparency advocated by the RBP.

[1] The American Bankers Association is the voice of the nation's $15 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $11 trillion in deposits and extend more than $8 trillion in loans.

DISCUSSION

1. Preliminary Considerations: Bank Rights as Lender vis à vis *Rights of Other Investors*

We respectfully urge the NFMA to consider more carefully its view on a bank's rights as a lender *vis à vis* those of other investors. The RBP states that the NFMA believes a bank's rights as an investor should be the same as the rights of investors in publicly offered parity debt. Although that may be appropriate to some degree, there are several good reasons why their respective rights need not be the same.

- Many banks extend bank loans as part of their ordinary commercial lending activities rather than making an "available-for-sale" investment.

- Banks are heavily regulated institutions that are required to engage in safe and sound lending practices, and must structure their loans to conform to regulatory rules and guidance.

- Whereas public market investments tend to be highly liquid, bank loans are generally held in a much less liquid form (*e.g.*, no offering statement, no public rating, physical form), evidencing the bank's intent to hold the loan to maturity rather than divest the asset in the event of a decline in credit quality.

- By the nature of bank loans (including the manner in which banks fund their commercial lending activities), the tenor of such loans is generally shorter than publicly offered fixed rate financings. That fundamental difference manifests itself in the credit and liquidity facilities that banks have historically provided to support variable rate demand obligations and commercial paper.

- In many—and likely most—cases where the disclosure and transparency of bank loans are relevant, the obligors are highly rated credits that, quite appropriately, have significant flexibility to issue additional debt and negotiate the terms under which it is issued.

Given the prominent role of commercial banks as the providers of funding in the municipal market, other constituents will be well served to appreciate the fundamental differences in the structure and tenor of financing provided by banks as contrasted with the securities purchased by long-term fixed rate investors. The respective roles and fundamental differences between bank financing and the securities held by long-term fixed rate investors have co-existed for decades in the public finance market. It thus should come as no surprise that the transition from bank-supported capital markets transactions to direct lending by banks would preserve those fundamental differences in the terms and provisions of bank loans as compared to those associated with securities held by long-term fixed rate investors.

The RBP emphasizes that bank loans change the obligor's debt profile. Although that is plainly true, as is the case with variable-rate demand obligations and commercial paper supported by bank facilities, bank loans in all cases must fit within the parameters of the obligor's additional debt and lien covenants that the existing debt holders have previously accepted. As a result, we are not convinced that a failure to disclose the additional debt and its terms in advance of a bank loan transaction will materially adversely affect existing debt holders (or, at a minimum, result in any adverse effect that they could not reasonably foresee at the time they purchased the related debt).

Furthermore, many of the potential risks of bank loans discussed in the RBP are not unique to bank loans but exist with respect to any short-term debt, regardless of the purchaser. For example, any short-term capital markets financing undertaken with the expectation of refinancing (rather than repaying) the debt upon maturity will include what the RBP calls "contingent liquidity risk" and "refinancing risk." Similarly, reduced security for existing bondholders will likely occur in connection with the issuance of any additional parity debt. Finally, there is no evidence that the transferability risk with respect to bank loans is any greater than that of publicly held debt. Most bank loans restrict the transferability of the loan for accounting reasons, and in any case there have been very few if any transfers of bank loans to date. An overwhelming number of our members report that they extend bank loans to municipal obligors with the intention to hold them to maturity, and in fact do hold them to maturity, making any increased transferability risk relative to publicly held debt theoretical at best. But even if bank loans are, in a departure from historical practice, transferred to other sophisticated investors, any such transfer is likely to be to another commercial bank and therefore would not result in a material adverse effect on other debt holders. In sum, although the risks identified in the RBP may be legitimate, we caution against the implication that they are unique to bank loans when, in fact, most of them would attend any additional short-term debt issuance.

Under the heading, "Potential Effects of Lack of Disclosure of Bank Loans," the RBP states that "properly structured" bank loans will be less likely to negatively affect credit quality. That statement is true enough, but we urge you to avoid any implication that there are a significant number of improperly structured bank loans, because the data, or at least lack of examples to the contrary, suggest that the vast majority of bank loans have not had an adverse effect on credit quality. ABA is aware of only one instance in which a rating agency stated that it would take an adverse rating action as a direct result of the structure of a bank loan, and in that instance the obligor and the lender promptly entered into an amendment to correct the issue. Comparing that one instance with, for example, the 404 direct loans evaluated by S&P in 2014 alone,[2] it is difficult to conclude that the structure of bank loans is a pervasive concern. Similarly, we were disappointed by the suggestion that "disclosure issues" relating to bank loans could lead to a narrower investor base and higher costs for obligors. Although that may be a theoretical possibility, we have no evidence that it has actually occurred. If the NFMA has any data to support that conclusion, we would welcome their publication.

2. Impact on Bondholders of Lack of Disclosure

The RBP suggests that disclosure for bank loans should be as robust as the disclosures for public bond issues. This idea has surface appeal, but the nature of the disclosure for bank loans should respect the fundamental differences between public offerings and bank loans; namely, that a bank loan is a privately negotiated extension of credit from a commercial lender that does its own (regulated) diligence before making the loan, and, as a result, the bank neither needs nor requires a separate disclosure document for the bank loan. That is not to say that full and prompt disclosure of a bank loan is unreasonable or inappropriate, but rather we would note that there are legitimate reasons why the *form* and *timing* of bank loan disclosure should differ from that of public offerings.

The RBP further states that post-execution disclosure could prejudice existing bondholders by eroding the value of their bonds and depriving them of the ability to liquidate. This argument proves too much, because it indicates that an existing bondholder may be uncomfortable with the ability of the existing covenant protections (*e.g.*, the obligor's ability to issue additional debt subject only to an additional debt test) to protect the value of its investment. If that is the case, then the bondholder accepted inadequate structural protections when it bought the bonds.

[2] See Standard & Poor's Ratings Services Ratings Direct, "Standard & Poor's Maintains Its Focus on Direct Loans After Evaluating $15.8 Billion In 2014," dated January 28, 2015.

3. Timing and Content of Disclosure

Subject of course to the views of the relevant obligor, ABA generally supports the routine and prompt disclosure of bank loans following their consummation. At the same time, the RPB's views on what to disclose and when to disclose deserve more rigorous evaluation.

Under the rubric "what to disclose," the RPB begins by saying that, at a minimum, all applicable documents for a bank loan should be publicly available. ABA generally can support this view so long as (i) there is a standard of reasonableness applied to the determination of which documents are applicable, and (ii) the applicable documents are redacted to avoid disclosing information that is commercially sensitive or susceptible to fraudulent use. In each case, we believe that the RBP should be informed by MSRB Rule G-34(c) and the related MSRB guidance, which the MSRB has said may be considered analogous for the purpose of posting bank loan documents.[3] Regarding which documents are applicable, we believe that the standard should be akin to that set forth in the Regulatory Notices elaborating on MSRB Rule G-34(c),[4] and should not require posting of documents that do not contain information that is critical to the subject bank loan (for example, a fee letter).[5] The same goes for redacting bank loan documents. The MSRB guidance relating to Rule G-34(c) accepts redaction of certain confidential information that is otherwise of limited value to investors, so long as it is kept to a minimum and does not include information that would reasonably be assumed to be used by an investor or other market participant in evaluating the relevant obligation. We believe the RBP should take the same approach to the disclosure of bank loan documentation.

ABA views any requirement that a summary of the bank loan be posted on the EMMA website as highly problematic for both the lender and the obligor. First, as stated above, there is no independent need for a disclosure document, so the preparation of a summary would be an additional expense to the obligor that does not benefit any of the parties to the bank loan transaction. Second, a summary may give rise to concerns for the obligor with respect to SEC Rule 10b-5 and the SEC's Municipalities Continuing Disclosure Cooperation initiative. Finally, posting properly redacted copies of the applicable financing documents as described above will allow third parties access to all relevant information relating to the bank loan, making a summary superfluous. Although in limited circumstances a summary may be desirable to the obligor (i.e., where the lender's rights, remedies, security, and other protections are identical to those of other debt holders and can be described in a very straightforward manner), requiring the preparation and filing of a summary would serve only as a short cut to a thorough analysis by other interested parties and a needless complication and added expense to an otherwise attractive financing option for the obligor.

Under the rubric "when to disclose," the RPB begins by saying that, at a minimum, disclosure of a bank loan should be made as soon as possible following the closing of the bank loan. ABA agrees that disclosure promptly after closing is appropriate and supports the ten business day standard referenced in the RBP; however, we believe that any express or implied recommendation by the NFMA to disclose the bank loan prior to its consummation is unwarranted if disclosure and transparency are the sole objectives. For many of the reasons detailed above (i.e., additional cost, liability, etc.), advance disclosure of a bank loan would prejudice the parties entering into the transaction and is unnecessary since existing debt

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[3] See MSRB Regulatory Notice 2015-03, available at http://www.msrb.org/~/media/Files/Regulatory-Notices/Announcements/2015-03.ashx?n=1.

[4] See MSRB Regulatory Notice 2011-17, available at http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2011/2011-17.aspx?n=1, and MSRB Regulatory Notice 2012-20, available at http://www.msrb.org/Rules-and-Interpretations/Regulatory-Notices/2011/2011-17.aspx?n=1.

[5] See *Supra*.

holders and other interested parties should already be aware of the obligor's ability to enter into a bank loan. As a result, while certain rating agencies have requested that bank loan documentation be provided to them prior to the consummation of the applicable bank loan, we see only drawbacks to the obligor in requiring advance disclosure to other debt holders.

CONCLUSION

To the extent consistent with the wishes of the relevant obligor, ABA supports the prompt disclosure of bank loans following closing. We believe that advance disclosure and summary form disclosure are not required to achieve transparency and will plainly increase the transaction costs associated with bank loans, making them less attractive for municipal borrowers. Accordingly, we urge the NFMA to remove those recommendations from the RBP and instead focus on a shared vision for prompt disclosure upon consummation of bank loans.

Sincerely,

Cristeena G. Naser

Cristeena G. Naser
Vice President
Center for Securities, Trust & Investment