SEC Proposes Major Regulatory Changes for Muni Market

On July 31, the Securities and Exchange Commission released a report on the municipal securities market that recommended significant regulatory and legislative changes. The SEC's report covers a broad range of market areas, from the timeliness and usefulness of financial disclosure to market price transparency. While the SEC's proposals would not create a regulatory scheme similar to that under which corporations must operate, if implemented the changes would have significant impacts on the availability and usefulness to individual investors of issuer financial and operating data and market pricing data.

In its report, the SEC explicitly states that it does not seek to repeal the Tower Amendment, which prohibits the SEC and the Municipal Securities Rulemaking Board (MSRB) from requiring municipalities to file presale disclosure documents (like companies are required to do for debt and equity offerings). However, the report does outline numerous recommendations which would expand the reach of both the SEC and the MSRB in regulating municipal disclosure and price transparency in the market. The report's legislative recommendations include:

- Authorizing the SEC to require dissemination of Official Statements and continuing disclosure while an issuer has securities outstanding; to set the timeframes, frequency and minimum disclosure requirements for such disclosure; and to enforce the new rules.
- Require conduit borrowers who are not municipalities to comply with the regulatory requirements for companies in the securities markets.
- Authorizing the SEC to establish the form and content of financial statements for municipal issuers and the ability to require municipal securities issuers to have financial statements audited.
- Create new mechanisms for enforcing compliance with continuing disclosure requirements.

On the regulatory side, the SEC report outlined a number of ways that the Commission and the MSRB could enhance price transparency, including: new requirements for publicly disseminating bid and offer information; requiring that dealers report yield spread information on trades in real time; enhancing the EMMA website to provide better information availability to individual investors; and a number of steps to provide enhanced "prevailing market price" data to investors.

It is unclear to what extent Congress will have the appetite to take any action on the SEC's legislative recommendations. Clearly, though, the SEC has taken a greater interest in the municipal market and it seems likely to us that there will be additional regulatory action in the marketplace in the coming years. We are generally supportive of measures that improve investors' access to high quality financial and operating data on municipal issuers, and we would expect that the SEC's report may help drive enhancements in the availability of issuer information that could prove beneficial to municipal investors. We will continue to report on developments with the SEC's proposals as they develop.

Delta Shuttering of Comair Highlights Risks in Airport Bonds

On September 29, Delta Airlines (DAL/NYSE, rated B2/B/BB-) will cease operations of its Comair regional carrier. Comair is based in Cincinnati, and its closure will take 44 planes and 1,700 employees out of the local air travel market. Cincinnati/Northern Kentucky International Airport (rated A3/A-/BBB+, outlooks Stable/Negative/Stable) has already been hurt by a substantial reduction in flights and passenger traffic following the merger of Delta and Northwest. While Delta pledged to maintain the airport as one of its network hubs, and has stated that it will not reduce Delta flights at the airport in conjunction with the Comair move, the loss of Comair could have material negative impacts on the airport and its operations.

Delta's move in Cincinnati highlights one of the credit risks inherent in airport revenue bonds. While these bonds finance critical transportation infrastructure and provide an essential transportation service that cannot effectively be substituted by the private sector, the financial performance of all airports depends to varying degrees on the performance of a financially troubled industry that continues to face serious challenges. The situation surrounding American Airlines current bankruptcy and the potential impacts on operations and finances at its Miami International Airport (rated A2/A-/A, outlooks na/Stable/Negative) hub also illustrate the credit uncertainty that can affect these issuers.

There are a number of factors that help determine the credit quality of airport revenue bonds. Among the most important fundamental credit features in evaluating credit quality are the nature of the air travel market in a metro area and the extent to which the airport (or airports) serving that market are dependent on the business operations of a single air carrier. The degree of concentration of traffic in a single carrier is one useful measure of an airport's exposure to business risk in the airline industry. So, too, is the extent to which an airport depends on airline hubbing operations to drive traffic levels. Industry analysts look at the percentage of traffic at an airport that is connecting versus the amount that is originating in that airport or arriving at the airport as a final destination (Origination and Destination, or "O&D"). The percentage of O&D traffic at an airport is an indicator of the inherent demand for air travel in that marketplace, while connecting traffic is driven largely by airlines' use of the airport as a hub. Consequently, the greater an airport's percentage of O&D traffic, the less exposed it is to changes in airline route structures that could take flights out of an airport and reduce passenger traffic and airline operations – key drivers of airport revenues. While major operation centers and key hub operations may be insulated from significant changes in airline strategy (e.g., Delta at Atlanta-Hartsfield, American at DFW, Southwest at Dallas Love Field), secondary and regional hubs are at much greater risk from airline industry changes.

We have seen this dynamic at work in a number of cities that have suffered cuts in service as a result of airline mergers over the past decade. In the 10 years since TWA merged with American Airlines, following American's decision to "de-hub" St. Louis, enplaned passenger levels (the number of passengers getting on a plane) at Lambert-St. Louis Airport declined more than 50%. Significant, though less substantial, drops in enplanement levels have also occurred at regional and secondary hubs like Memphis, Cleveland and Cincinnati.

The table below outlines the airports with rated revenue bonds having the highest percentages of concentration in a single carrier. The table also includes recent data from Fitch on the percentages of enplanements that were O&D traffic and the current ratings and outlooks on the airports' most senior revenue bonds. Generally speaking, mid-size and smaller airports with higher carrier concentrations and lower O&D percentages are at greater credit risk from changes in the airline industry. However, it is important to examine the details of an airport's operations to understand the credit factors at work.

Airport with Highest Carrier Concentrations

Airport	Ratings	Outlooks	Enplanements	Largest Carrier	Carrier Share %	O&D %
Chicago Midway	A2/A/A	Stable	9,459	Southwest	91.1	61
Charlotte/Douglas	Aa3/A+/A+	Stable	19,711	US Airways	89.8	25
Memphis	A2/A-/A	Negative/Stable/ Stable	4,780	Delta	86.0	41
Dallas/Fort Worth	A1/A+/A+	Negative/Stable/ Negative	28,867	American	85.0	42
Cincinnati (Kenton County, KY)	A3/A-/BBB+	Stable/Negative/ Stable	3,525	Delta	82.0	64
Long Beach, CA	A2/BBB/A-	Stable	1,532	Jet Blue	80.7	98
Detroit	A2/A/A-	Stable	16,226	Delta	80.0	44
Minneapolis-St. Paul	Nr/AA-/AA-	Stable	15,972	Delta	78.7	54
Atlanta Hartsfield	A1/A+/A+	Stable	46,192	Delta	77.7	32
Oakland (Port of)	A2/A/A+	Stable/Positive/Stable	4,688	Southwest	74.0	87
Houston Airport System	Aa3/AA-/A+	Stable/Stable/ Negative	24,945	United	71.2	53
Cleveland	Baa1/A-/A-	Stable	4,609	United	68.0	72
Philadelphia	A2/A+/A	Stable	15,612	US Airways	67.2	54

Sources: "Peer Review of U.S. Airports," July 20, 2012, FitchRatings; Moody's; S&P

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