

SESSION ONE

RECENT ENFORCEMENT ACTIONS AGAINST ISSUERS AND PUBLIC OFFICIALS

Presented by

Robert Doty, President and Proprietor, AGFS, Annapolis, MD
Elaine Greenberg, Partner, Greenberg & Taurig

EXPANDING MUNICIPAL SECURITIES ENFORCEMENT

Profound Changes for Issuers & Officials

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Bond Buyer California Pre-Conference

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SEC NON-MCDC ENFORCEMENT SINCE EARLY 2013

- **NON-MCDC ENFORCEMENT ACTIONS (3 ½ Years)
AGAINST—**

- **18 State or Local Governmental Entities**
- **16 Local Officials**
- **Includes 4 Actions Pending Against 6 Local Governmental Entities & 6 Officials**

- **CONTRAST:
IN 14 YEARS FROM 1999 THROUGH 2012—**
 - **11 State or Local Governmental Entities**
 - **10 Local Officials**

SINCE EARLY 2013

- **Two States**—Illinois & Kansas
(Not First—New Jersey in 2010,
Add Hawaii and Minnesota After MCDC)
- **State Agency**—Rhode Island Commerce Corp.
(formerly, Economic Development Commission) (in
progress)
(Not First—Massachusetts Turnpike in 2003,
After MCDC, 10 State Agencies)

**COMMISSION GOING TO
FEDERAL DISTRICT COURT
MORE OFTEN
(As Opposed to Administrative Proceedings)**

**Will Lose Some, But Also Will Produce Court
Decisions as Precedent**

**More Remedies in Federal Court
(e.g., Control Person Liability, Injunctions, Emergency
Relief to Halt Ongoing Conduct)**

To Date, Quite Successful

NOTABLE “FIRSTS” & OTHER DEVELOPMENTS

FIRST TIME:

**Emergency Injunction Against Issuer To Halt
Bond Offering in Progress**

**(City of Harvey, Illinois)
(Pacific Genesis, Underwriter, in 2001)**

FIRST TIME:

**Prohibitions Against Issuers Issuing Bonds in Future
(Without Satisfying Conditions Precedent)**

**UNO Charter School Network—5 Years;
Conditions: Policies, Training, Responsible Official, & More**

**City of Harvey, Illinois—3 Years;
Condition: Independent Disclosure Counsel**

**Allen Park, Michigan—2 Years;
Conditions: Disclosure of Order, Certification After Consultation with
Disclosure Counsel**

FIRST TIME:

Civil Penalties Against Issuers

**(Greater Wenatchee, Washington, Regional Events Center
Public Facilities District—\$20,000;
Also Operator of Center and Its President—\$10,000 Each)

(Westlands Water District—\$125,000)**

FIRST TIME:

**SEC Won in District & Appellate Courts on Issue
of
Qualified Immunity of Public Officials**

**Basis: SEC Seeking
Injunction & Civil Penalty
vs. Damages**

(SEC v. Miami's Budget Director)

FIRST TIME:

Bars Against Officials—No Future Bond Issues

**Includes Two Mayors
(One Still Sitting—Can't Certify Bond Disclosures)**

Includes Bars Against Work in Industry

**FIRST TIME:
Bars Against Officials**

- **City of Harvey, Illinois—
Sitting Mayor & Former Comptroller**
- **City of Allen Park, Michigan—
Former Mayor & City Manager**
- **Rhode Island Economic Development
Commission—Former Executive Director &
Deputy Director**
- **United Neighborhood Organization of
Chicago—Former CEO**

FIRST TIME:

Civil Penalties Against State Agency Officials

**(Executive Director and Deputy Director of Rhode
Island Commerce Commission—\$25,000 Each)**

INCREASED USE OF CIVIL PENALTIES AGAINST OFFICIALS

\$180,000 Against 8 Officials

- **City of Harvey, Illinois—Sitting Mayor—\$10,000**
Former Comptroller—\$30,000 (plus disgorgement & interest)
- **City of Allen Park, Michigan—Former Mayor—\$10,000**
- **Westlands Water District—**
General Manager/General Counsel—\$50,000
Former Assistant General Manager—\$20,000
- **Rhode Island Economic Development Commission—**
Former Executive Director—\$25,000
Former Deputy Director—\$25,000
- **United Neighborhood Organization—Former CEO—\$10,000**

CONTRAST:

Prior 15 Years—

**5 Officials (in two actions) \$85,000
(Primarily San Diego Officials)**

**LARGEST CIVIL PENALTY TO DATE AGAINST
ISSUER OFFICIAL—\$50,000**

Double Prior Highest

(Westlands, California, Water District)

FIRST TIME:
BIG DEAL

“Control Person” Liability for Issuer Officials
(Joint & Several with Primary Violator)

- **Mayors of—**
Harvey, Illinois
Allen Park, Michigan
- **Shift in Burden of Proof**
- **SEC Need Only Prove Control, Not Knowledge**
- **Participation in Fraud Unnecessary**

CONTROL PERSON LIABILITY:

- **To Establish Successful Defense,
“Control Persons” Must Prove—**
 - ❖ **“Good Faith”**
—*and*—
 - ❖ **Did Not “Directly or Indirectly”
Induce Action of Primary Violator**

CONTROL PERSON LIABILITY:

- **Poses Significant New Risks for Community Leaders—Mayors, Board Chairs**
- **Absolute “Control” Not Required**
- **Defense May Require Exercise of Oversight to Evidence “Good Faith”**
- **If Policies/Procedures Adopted & Implemented, May Be Helpful**

FIRST TIME:
ANOTHER BIG DEAL

**Issuer Former CEO Fined and Barred
for NOT Reading Official Statement He Signed**

**OS Contained Material Misstatements/
Omitted Material Information**

Only Charged with Negligence

Not Charged with Knowledge of Misrepresentations

(CEO of United Neighborhood Organization of Chicago)

FIRST TIME:

Action Against Issuer for Information on Website
(NOT Official Statement or Continuing Disclosure Filing)

Information on General Webpage (Not Investor Page)

Including Mayor's Political Speech
(Annual State of City—Posted on General Webpage)

(City of Harrisburg, Pennsylvania)

HARRISBURG:

Implications for Disclosure Regarding Outstanding Obligations

**Once Issuer Speaks About Obligations, Must Speak Without Material
Misstatements or Omissions
(*e.g.*, on Website, in Official Statements,
Annual Financial Information Filed at EMMA)**

HARRISBURG:

Illustrates Point That ALL Material Obligations Should Be Disclosed

**Including
“Bank Loans”
Non-Bank Loans,
ALL Material Obligations
(e.g., Judgments, Contingent Liabilities,
Contractual Liabilities)**

FIRST TIME:

**Action Against Issuer with Respect to Information in Documents
Investors Never Saw**

**Tax Certifications to Bond Counsel
& Pool Bond Issuer Regarding Private Use of Project**

(City of South Miami, Florida)

SOUTH MIAMI:

**Illustrates Importance of Internal Issuer Controls
(Four Finance Directors—Not Trained)**

**Unsophisticated Issuer—
No Excuse**

Many Issuers Need Professionals to Assist

**Compliance with Tax Rules, Continuing Disclosure & Bond
Documents**

FIRST TIME:
Independent Conflicts Monitor
(UNO Charter School Network)

FIRST TIME:

Governmental Issuer Alleged to Have Failed to Disclose—

Information Regarding Private Conduit Borrower

In Credit Enhanced Bond Issue

**(Rhode Island Commerce Commission—Pending)
(Two Officials Settled—Barred & Civil Penalties)**

FIRST TIME:

**Liability in True Private Placement
(Under Section 4(a)(2) of Securities Act of 1933)**

Bonds Offered/Sold Solely to Sophisticated Investors

Investment Letters

Action Against State Agency/Officials

Placement Agent's Motion to Dismiss Denied

**(Rhode Island Commerce Commission—Pending)
(Two Officials Settled—Barred & Civil Penalties)**

FIRST TIME:

Local Issuer Counsel

**(Westlands, California, Water District &
Ramapo, New York)**

FIRST TIME:

**Action Against Issuer Already Subject to
Cease-and-Desist Order**

(City of Miami, Florida)

FIRST TIME:

**Federal Court Trial and Jury Verdicts Against
Issuer and Issuer Official**

(City of Miami, Florida)

“REASONABLE” RELIANCE ON PROFESSIONALS

Four Factors Applied by Courts:

- **Complete Disclosure to Professional Regarding Issue**
- **Seeking Professional Advice as to Appropriateness of Conduct
(Participation in Transaction Inadequate)**
- **Receipt of Advice that Conduct Is Appropriate
(Not Merely Negative Assurance)**
- **Reliance on Advice in Good Faith**

Miami Jury Verdict Found None of the Factors Present

FIRST TIME:

**Announced Intention to Coordinate with
Justice Department**

**(City of Ramapo, New York)
(Criminal Action Includes Local Counsel)**

PENDING COURT CASES:
(SEC Seeking Broad Remedies Against Issuers & Officials)

City of Miami & Former Budget Director

**Southern California Logistics Airport Authority,
City of Victorville, & Assistant City Manager**

Rhode Island Commerce Commission
(Formerly, Rhode Economic Development Commission)
(Former Executive Director & Former Deputy Director
Settled)
(Asserting Governmental Responsibility for Private Borrower
Information in Credit Enhanced Bond Issue)

City of Ramapo, New York, Ramapo Local Development
Corp.,
Town Supervisor/President of Development Corp., Town
Attorney, former Executive Director of Development
Corporation/Assistant Town Attorney, & Town's Deputy
Finance Director

COMMON PROBLEM AREAS:

- **Overly Optimistic Information Regarding Economic Development Projects—**
(*e.g.*, Wenatchee Events Center, Allen Park Movie Studio, Ramapo Baseball Stadium, Rhode Island EDC Private Online Game Company, Harvey Holiday Inn)
- **Assumptions & Other Information Supporting Projections & Expert Reports—**
(Wenatchee Events Center, Public Health Trust)

COMMON PROBLEM AREAS:

- **Stale Information**
(Allen Park, Public Health Trust)
- **Conflicts of Interest**
(UNO Charter School Network, Harvey)
- **Insufficient Internal Controls**
(South Miami, Public Health Trust)
- **Misleading Risk Factors**
(Rhode Island Commerce Commission)

**MAJOR SEC OUTCOMES:
(MCDC & Non-MCDC)**

**Large Numbers of Issuers Adopting
Policies & Procedures
& Staff Training**

**Virtually All Underwriters (96% of Bonds)
Required to Employ Consultants Regarding
Due Diligence Practices**

Condition of MCDC Settlements

**Achieved a Re-Focused Review of Marketwide Practices
by Issuers & Underwriters**

ISSUER POLICIES & PROCEDURES:

Potential to Become Market Practice

**Control Persons Might Point to Adoption
as Evidence of “Good Faith”**

**Greater Risk in Enforcement,
If Not Implemented**

BUT, If Adopt, BETTER FOLLOW

ISSUER POLICIES & PROCEDURES:

Many Issuers Need Professionals to Assist

BUT Issuers Are Responsible for Official Statements

Officials Who Sign MUST Read and Understand

ISSUER POLICIES & PROCEDURES:

**SEC Often Accepts Lighter Sanctions
for Careless, Negligent Issuers
(Section 17(a)(2) & (3) of Securities Act of 1933)**

IF

**Issuers Offer to Implement Policies & Procedures,
Designate Responsible Officials, & Train Staff**

NEXT STEPS (MCDC)

Potential Actions Against Non-Self-Reporting Issuers & Underwriters

**Potential Actions Against Issuer Officials
& Individual Underwriter Officers**

Potential Actions Against Professionals

If So, Sanctions Likely To Be More Severe

THE MARKET'S FUTURE

Regulation by Enforcement
(as Well as Through Rule 15c2-12)

Tower Amendment Irrelevant

Legislative Trade-Off in the 1970s

THE END