

Ceresney Warning: Expect Continued SEC Enforcement Activity Regarding Municipal Securities

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In the [keynote address](#) at the 2016 Securities Enforcement Forum last week, Andrew J. Ceresney, Director of the SEC's Division of Enforcement, made clear that the SEC will continue and even expand its focus on the public finance market, particularly in the municipal securities area. Ceresney noted that enforcement activity in the municipal securities arena has increased substantially. In the 10 years from 2002 to 2012, the SEC filed enforcement action against 6 government entities, 6 obligated persons and 12 public officials. In contrast, the Commission has filed enforcement actions against 76 government entities, 13 obligated persons and 16 public officials in the last 3 1/2 years. The SEC has been conducting well-publicized enforcement sweeps in the area. Perhaps the most well-known of those is the Municipal Continuing Disclosure Initiative ([reported](#) about here), which caught up 72 broker-dealers and 71 municipal underwriters. Also of note was the [Puerto Rico Junk Bond sweep](#), which illustrates the increased use of surveillance in the area. The junk bond offering was considered appropriate for only institutional investors and therefore had a minimum denomination of \$100,000. Recognizing that some dealers might nevertheless try to break up the bonds into smaller denominations for retail customers, the SEC staff surveilled the trading, identifying a number of sales below \$100,000. Settled enforcement actions were brought against 13 firms as a result. In addition to the sweeps, the Commission has been using remedies and theories that, up until recently, have been seen only in the non-municipal context. Among those are the following:

- **Temporary Restraining Orders.** In 2014, the first request for a [temporary restraining order](#) was filed to stop an offering of bonds by the City of Harvey, Illinois, until certain safeguards regarding the use of the proceeds could be put into place. The SEC alleged that in connection with prior offerings city officials had diverted \$1.7 million in proceeds to pay the city's operational expenses, as opposed to the projects that were supposed to be funded by those earlier bonds.
- **Civil Penalties Against Municipal Issuers.** The [first imposition of a civil penalty against a municipal issuer](#) occurred in 2013. In that case, a public facilities district in the state of Washington, which had issued about \$42 million in bond anticipation notes, was alleged to have misled investors by failing to disclose that an independent consultant had questioned the projections contained in the official statement for the notes. Ceresney cautioned that the Commission will continue to pursue penalties against municipal issuers when appropriate, "even when the source of those funds is the taxpayer base."

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- **Controlling Person Liability for Government Officials.** In 2014, the SEC used section 20 of the 1934 Act for the first time against a former government official. That case concerned a bond offering by the City of Allen Park, Michigan, to finance a movie studio project. The SEC alleged that the offering documents contained misleading statements about both the viability of the project and the financial condition of the city, including its ability to service the bond debt. The SEC alleged the [former mayor of Allen Park](#) was liable as a controlling person because of his authority and control over the city.
- **Injunctions Against Participation in Future Offerings.** The SEC is also seeking to enjoin issuer officials from participating in future municipal bond offerings. Thus, for example in the City of Harvey case discussed above, the [mayor agreed](#) to an order enjoining him from participating in future offerings.
- **Coordination with Criminal Authorities.** In 2014, the SEC's increased coordination with criminal authorities in the municipal finance area resulted in what may be the first filing of municipal bond-related criminal securities fraud charges. On April 14, 2016, the SEC brought civil [fraud charges](#) against Ramapo, New York, its local development corporation and four town officials, alleging they hid deteriorating financial conditions from bond investors. That same day, the U.S. Attorney for the Southern District of New York [unsealed an indictment](#) against a former town supervisor and executive director of the development corporation, charging them with securities fraud, wire fraud and conspiracy. Ceresney promised that coordination between the SEC and the public corruption and public integrity units of the U.S. Attorneys' offices and the FBI will continue to increase, particularly in the investigation of whether there is corruption in the awarding of underwriting business.

Ceresney closed with a warning to the municipal securities industry: "[O]ne municipal securities industry commentator recently observed of the last 3½ years that '[t]here is a definite change in tone.' I am here to say that this change in the tone of Enforcement is here to stay. You can expect continued activity in this area to protect investors."