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36 Underwriters to Pay $9.3M to Settle Under SEC MCDC Program.

WASHINGTON – Thirty-six municipal underwriters agreed to pay a total of $9.3 million and take remedial actions to settle Securities and Exchange Commission charges that they sold bonds with offering documents that contained false or misleading statements about the issuers' compliance with continuing disclosure obligations.

The underwriters allegedly failed to conduct adequate due diligence to identify the misstatements and omissions before offering and selling the bonds to their customers as required by the SEC's rule 15c2-12, the commission said in the settlements, which were reached under the Municipalities Continuing Disclosure Cooperation initiative. The violations cited in the settlement orders took place between 2010 and 2014. The MCDC, announced last March, encouraged issuers and underwriters to voluntarily report to the SEC any time in the last five years in which they sold or underwrote bonds with offering documents that might not pass legal muster. The reporting period expired on Sept. 10 last year for underwriters and on Dec. 1 for issuers.

"The MCDC initiative has already resulted in significant improvements to the municipal securities market, including heightened awareness of issuers' disclosure obligations and enhanced disclosure policies and procedures," said SEC chair Mary Jo White. "This ongoing enforcement initiative will continue to bring lasting changes to the municipal securities markets for the benefit of investors."

The 36 firms, which did not admit or deny the SEC's findings, agreed to cease and desist from future violations. They agreed to pay civil penalties based on the number and size of the fraudulent offerings, up to a cap based on the size of the firm. The maximum penalty, imposed on 10 underwriters, was $500,000. The smallest one announced was $40,000. The $500,000 cap was for firms who reported more than $100 million of revenue in fiscal year 2013. All the participating underwriters agreed to retain independent consultants to review their policies and procedures on due diligence and make recommendations for improvements.

"The MCDC initiative highlights the importance of continuing disclosure in the municipal bond market and due diligence in the underwriting process," said Andrew Ceresney, director of the SEC's enforcement division. LeeAnn Gaunt, chief of the enforcement division's municipal securities and public pensions unit, said the actions will help investors.

"The settlements announced today reflect these underwriters' cooperation in self-reporting their own misconduct and agreeing to improve their procedures going forward," Gaunt said. "Because these 36 firms underwrite a substantial portion of the country's municipal bonds each year, we expect a large number of bondholders will benefit from the resulting improvements in due diligence and disclosure."

Ceresney said during a press call that the 36 firms represent about 70% of muni underwriting volume by dollar amount for the past four fiscal years. Some large firms were not among those named. Wells Fargo & Co., which was a top five underwriter that accounted for nearly 7% of the

dollar volume of underwritings in 2014, was not named. Nor was Barclays, a top 10 underwriter accounting for nearly 5%. Ceresney told The Bond Buyer that more settlements with underwriters who participated in the MCDC initiative could be coming.

The conduct cited in the settlements included instances in which official statements failed to disclose that the issuer had done almost no continuing disclosure at all. The settlement against Citigroup, for example, said that in five negotiated sales between 2011 and 2013 the issuer did not disclose that it had failed to file four annual financial reports since 2009. The settlement with The Baker Group cited competitive offerings, including an instance of a 2014 issuance in which the official statement did not disclose that the issuer had been between 145 and 374 days late in filing annual financial information in four prior bond offerings.

The SEC granted waivers to the firms to prevent them from being disqualified from certain exemptions or safe harbors in SEC rules. Without such waivers, firms charged under the MCDC might be unable to do certain types of non-muni transactions. Firms will still need to go through a process to reinstate their memberships with the Financial Industry Regulatory Authority, Ceresney said.

The SEC had previously charged one issuer under the MCDC, but Kings Canyon Joint Unified School District in California was already under investigation when it chose to take advantage of the standardized settlement terms of the initiative.

Jessica Giroux, general counsel and managing director of federal regulatory policy at Bond Dealers of America, said BDA supports improving disclosure but found the MCDC disrupted service to issuer clients.

“This has been a long and burdensome process for our dealers who have spent countless hours and a massive amount of resources working to comply with this enforcement initiative,” she said.

Giroux said BDA was also disappointed that the SEC did not pursue the MCDC initiative under only Section 8A of the Securities Act of 1933 instead of Section 15(b) of the Securities Exchange Act of 1934 because that modification could have avoided triggering statutory disqualifications of all the firms.

Michael Diver, the head of Katten Muchin Rosenman’s litigation and enforcement group in Chicago, questioned whether the SEC could have gotten a judge to agree that the disclosures were material to investors and that selling the bonds violated the antifraud provisions of the law. Diver, who represented four underwriting firms, including BMO Capital Markets GKST Inc., Oppenheimer & Co., and Loop Capital Markets, said the SEC developed an effective initiative with the MCDC.

“The SEC developed a fairly effective ‘carrot and stick’ approach to drive participation in the initiative and I think broker-dealers that are active in the municipal securities marketplace were wise to participate,” he said.

Diver added that assessing issuer compliance can be difficult and that he saw his broker-dealer clients respond “in good faith” to the SEC’s March 2012 risk alert on 15c2-12 compliance, well before the MCDC initiative.

A Securities Industry and Financial Markets Association spokesperson said that SIFMA wants disclosure to improve, but that issuer disclosure failures “could have been handled by the SEC in an alternative manner with far less expense and collateral consequences to market participants, especially considering the absence of harm to investors.”

The SEC is expected to release future “waves” of settlements with issuers and with individuals whom the commission decides to charge separately.

Underwriters Fined Under MCDC Settlements include:

• The Baker Group, LP – $250,000

• B.C. Ziegler and Company – $250,000

• Benchmark Securities, LLC – $100,000

• Bernardi Securities, Inc. – $100,000

• BMO Capital Markets GKST Inc. – $250,000

• BNY Mellon Capital Markets, LLC – $120,000

• BOSC, Inc. – $250,000

• Central States Capital Markets, LLC – $60,000

• Citigroup Global Markets Inc. – $500,000

• City Securities Corporation – $250,000

• Davenport & Company LLC – $80,000

• Dougherty & Co. LLC – $250,000

• First National Capital Markets, Inc. – $100,000

• George K. Baum & Company – $250,000

• Goldman, Sachs & Co. – $500,000

• Hutchinson, Shockey, Erley & Co. – $220,000

• J.P. Morgan Securities LLC – $500,000

• L.J. Hart and Company – $100,000

• Loop Capital Markets, LLC – $60,000

• Martin Nelson & Co., Inc. – $100,000

• Merchant Capital, L.L.C. – $100,000

• Merrill Lynch, Pierce, Fenner & Smith Incorporated – $500,000

• Morgan Stanley & Co. LLC – $500,000

• The Northern Trust Company – $60,000

• Oppenheimer & Co. Inc. – $400,000

• Piper Jaffray & Co. – $500,000

• Raymond James & Associates, Inc. – $500,000

• RBC Capital Markets, LLC – $500,000

• Robert W. Baird & Co. Incorporated – $500,000

• Siebert Brandford Shank & Co., LLC – $240,000

• Smith Hayes Financial Services Corporation – $40,000

• Stephens Inc. – $400,000

• Sterne, Agee & Leach, Inc. – $80,000

• Stifel, Nicolaus & Company, Inc. – $500,000

• Wells Nelson & Associates, LLC – $100,000

• William Blair & Co., L.L.C. – $80,000

THE BOND BUYER

BY KYLE GLAZIER and JACK CASEY

JUN 18, 2015 12:48pm ET

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