Bond Case Briefs

Municipal Finance Law Since 1971

SEC's Miami Win Likely to Embolden Muni Crackdown: Lawyers

NEW YORK — The U.S. Securities and Exchange Commission's courtroom victory in a fraud case against the City of Miami will likely further embolden the agency in its years-long effort to more tightly regulate the $3.7 trillion municipal bond market, securities lawyers said.

A jury took only a few hours on Wednesday to find Miami and its former budget director Michael Boudreaux liable for securities fraud in the sale of over $150 million in municipal debt in 2009. The SEC had accused the city of "playing a shell game" by shuffling money among accounts to conceal its deteriorating financial condition from investors.

The SEC told the court on Wednesday it would present a request for injunctive relief and monetary penalties within two weeks. The city and Boudreaux, who argued the fund transfers had been approved by auditors and publicly disclosed, said they planned to appeal.

The verdict is a "big boost" for the SEC, making the agency likely to sue more municipalities, Bradley Bondi, a former SEC lawyer now with Cahill Gordon & Reindel, said in an interview. The SEC has been criticized for favoring administrative proceedings over trials to resolve cases, he noted.

The SEC had subjected the municipal bond market to light enforcement, for reasons that include a reluctance to impose penalties that might be passed on to taxpayers. But its stance changed following a wave of defaults during the financial crisis.

In 2010, the agency set up a special enforcement unit for municipal securities and public pensions. Since 2012, it has brought cases against 19 municipal issuers over faulty disclosures, most of which have settled or ended in default judgments. An additional 71 issuers settled charges last month through a special self-reporting program.

Other cases have targeted municipal officials with fines. Since the start of 2013, eight officials have been hit with SEC civil penalties, compared to just five in the 15 preceding years, Robert Doty, a litigation consultant who tracks securities cases, said.

"It is truly a sea change and we have seen the SEC ramp up its municipal enforcement very aggressively," Stephen Crimmins, a lawyer with Murphy & McGonigle who had previously led the SEC's trial unit, said in an interview.

The Miami case also shows the SEC is losing some of its aversion to seeking financial penalties, said Kit Addleman, a former SEC lawyer now with Haynes and Boone in Dallas.

Now the SEC feels very strongly that "in some cases conduct is egregious enough that a penalty is the only way to drive the message home that the entity needs to clean up its act," she said in an interview on Tuesday.

The SEC had won a 2003 cease-and-desist order against the city in a previous case over similar conduct. Miami's repeat offense was a "rare situation" among muni cases, Bondi said.

In April, the SEC, which is only empowered to bring civil charges, announced a cooperative case with the U.S. Justice Department involving the criminal indictment of a town supervisor of Ramapo, New York, and one other individual over fraudulent disclosures in the sale of $150 million municipal bonds.

The SEC also has civil lawsuits pending against Rhode Island's economic development agency and the municipality of Victorville, California.

"We will continue to hold municipalities and their officers accountable, including through trials, if they engage in financial fraud or other conduct that violates the federal securities laws," Andrew Ceresney, director of the SEC's division of enforcement, said in a statement following the Miami verdict.

Crimmins said municipal issuers would be challenged by the SEC's more aggressive stance. Despite raising large sums of money, they largely fall short compared to corporations in terms of gathering financial data and evaluating and reporting it.

"Obviously this is a wake up call for people in the municipal securities area," he said.

By REUTERS

SEPT. 15, 2016, 3:57 P.M. E.D.T.

(Reporting by Dena Aubin and Sarah N. Lynch; Editing by Anthony Lin and Richard Chang)