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SEC Stepping Up Enforcement of Public Finance Market.

Over the last three years, the Securities and Exchange Commission's Enforcement Division has used sweeps to dramatically increase the number of enforcement measures brought against bad actors in the public finance market, Director Andrew Ceresney said.

Ceresney's division has brought enforcement actions against 76 state or local governments, 13 obligated individuals and 16 public officials since 2013. From 2002-2012, the division brought enforcement actions against six government entities, six obligated individuals and 12 public officials.

MCDC and other sweeps.

Enforcement sweeps have been critical to enhancing enforcement of the municipal securities market and the public pension market, which currently hold securities valued at $3.7 trillion and $3.8 trillion, respectively.

"A sweep is a group of enforcement actions brought simultaneously against different parties who have engaged in similar violations," Ceresney said in a speech at the Securities Enforcement Forum on Oct. 13.
The commission's most prominent sweep has been the Municipalities Continuing Disclosure Cooperation Initiative (MCDC) in 2014. The enforcement division implemented the self-reporting initiative to target municipal advisers failing to provide investors with important financial information.

After failing to disclose, bond issuers were falsely telling investors they were complying with disclosure obligations. Additionally, underwriters were suspected of selling bonds to customers using materials containing false statements, the director said.

"While not every self-report resulted in an enforcement action, the commission charged 72 broker-dealers, representing about 96 percent of the market for municipal underwriting," Ceresney said.

Beyond sweeps, the commission has implemented four other new measures in bringing enforcement actions in the public finance space — enjoining bond offerings, dispensing penalties against municipal issuers, issuing injunctions against public officials and raising standards for municipal advisers.

Restrain the bonds.

While the SEC has issued temporary restraining orders in other sectors, the commission never prohibited a municipal issuer from selling bonds until 2013. The SEC alleged the city of Harvey, Ill., had diverted bond proceeds for improper, undisclosed uses. Additionally, the commission alleged Harvey officials had been issuing bonds for the purported development of a hotel, but in reality had diverted $1.7 million of the proceeds toward the city's payroll and other operational costs.

Harvey was going to issue similarly structured bonds in the near future before the enforcement division stepped in to enjoin offerings until necessary safeguards were imposed.

Municipal issuers.

Historically, the commission hasn't brought penalties against municipal issuers, but that changed in recent years, Ceresney said.

The enforcement director presented three recent cases in which the commission charged issuers. In November 2013, the SEC charged a public facilities district in Washington with lying about the financial projections associated with an events center it was hoping to fund.

The SEC charged California's largest agricultural water district last March for lying to investors about its financial condition in connection with a 2012 bond offering worth $77 million. Currently, the commission is pursuing a civil penalty against the city of Miami for officials engaging in a "shell game" — using restricted funds to inflate its general fund.

"These cases demonstrate that municipal issuers should not expect a pass on civil penalties," Ceresney said.

Public official culpability.

The commission has started holding public officials responsible under Section 20(a) of the Exchange Act, "based on their control of the municipal entity that engaged in the fraud," Ceresney said.

Section 20(a) was used in the municipal securities context for the first time in a case against the former mayor and former administrator of Allen Park, Mich., in 2014. The commission alleged the administrator prepared and approved offering documents in association with the construction of a movie studio, despite knowing of negative, undisclosed information. The SEC alleged the mayor, based on his authority and control over the municipality, was also liable.

Municipal advisers.

This year, the commission brought enforcement actions against municipal advisers for the first time. The Dodd-Frank Act mandated municipal advisers register and comply with regulations issued by the Municipal Securities Rulemaking Board. The SEC charged Central States, LLC, and three of its employees, with violating their fiduciary duties and breaching MSRB rules.

"The new registration requirements and regulatory standards were intended to mitigate some of the problems observed with the conduct of some municipal advisers, including failure to place the duty of loyalty to their municipal entity client ahead of their own interest," Ceresney said.

By Timothy Weatherhead, The Hill Extra – 10/14/16 05:04 PM EDT