Bond Case Briefs

Municipal Finance Law Since 1971

WSJ: South Miami Charged With Defrauding Bond Investors.

For the second time in a month, federal securities regulators have charged a U.S. city with defrauding municipal-bond investors with improper disclosures.

The Securities and Exchange Commission on Wednesday charged South Miami, Fla. with misleading investors about the tax-exempt eligibility of a downtown public-parking garage and retail development.

South Miami, a city of 11,000 residents, agreed to settle the charges and hire an independent third-party consultant to oversee its internal controls for municipal-bond disclosures.

The SEC said that the city borrowed $12 million in two bond offerings through the Florida Municipal Loan Council. Proceeds from the first offering were loaned to a private developer, and the loan agreement was restructured, jeopardizing the project's tax-exempt financing, the SEC said.

In order for investors to get the tax advantages of municipal bonds, the debt must be used largely for a public purpose. The Internal Revenue Service allows projects to be financed by tax-exempt bonds only if their use by a for-profit developer is kept to a minimum.

The SEC said the city's decision in 2005 to lease both the parking garage and retail space to a private developer jeopardized the tax-exempt status of the bonds.

South Miami officials failed to disclose to investors that the bonds' tax-exempt status had been jeopardized, according to the SEC.

Instead, the SEC said, the city continued to make annual certifications to the Florida Municipal Loan Council from 2003 to 2009 stating falsely that it was in compliance with the terms of the loan agreement.

"The tax-exempt status of their bonds is very material to bond holders," Elaine Greenberg, chief of the SEC's Municipal Securities and Public Pensions unit said in an interview. "That is one of the key features that investors look for in deciding whether to invest in municipal bonds."

City Attorney Thomas Pepe declined to comment on the specifics of the settlement because he said the SEC hadn't contacted him directly about it. Mr. Pepe added that he hoped "the city can put the whole matter behind it."

According to the SEC, South Miami neither admits nor denies the agency's findings in the case.

The SEC recently has ramped up its enforcement cases against municipal borrowers.

Earlier this month, the SEC charged Harrisburg, Pa., with securities fraud for allegedly failing to disclose information on its financial troubles. In March, the agency charged the state of Illinois for failing to adequately disclose in bond documents the shaky condition of the state pension system. Harrisburg and Illinois agreed to settle the charges without admitting wrongdoing.

The SEC settlement didn’t require South Miami or any of its officials or former officials to pay a fine.

But the SEC noted that the city paid the IRS about $260,000 as part of a separate settlement.