Bond Case Briefs

Municipal Finance Law Since 1971

SEC Turns Up the Heat on Issuer Officials.

Two recent SEC enforcement actions demonstrate that the Securities and Exchange Commission remains intently focused on the municipal market and, in particular, on officials participating in financings that fail to accurately and completely disclose material information. In an action arising from defaulted bonds sold by a Michigan city to develop a soundstage, the SEC successfully brought fraud charges against the former mayor of the City of Allen Park, Gary Burtka, and, for the first time, charged a municipal official with "control person" liability, thereby barring him from participating in any future municipal bond offerings. In another case involving a proposed bond issue, the SEC obtained a court order halting the City of Harvey, Illinois from issuing bonds for an economic development project and brought charges against the City's comptroller, Joseph Letke.

The SEC's enforcement actions over the past several years, read together, comprise a line of cases clarifying the SEC's views of the scope of securities fraud in the municipal markets and, increasingly, the personal liability of officers of the issuers or borrowers. Although the facts in each of these cases are relatively clear and often damning, the lessons that the SEC's enforcement actions teach are important for officers of health care institutions that are borrowers in the municipal market to take to heart.

The SEC is clearly sending a message to the municipal market that inadequate, incomplete or misleading disclosure relating to municipal bonds is not only unacceptable, it is a violation of the federal securities fraud statutes and will not be tolerated. Thus, officers of borrowers of tax exempt bonds must ensure that the disclosure contained in the Official Statement regarding the borrower, as well as in the on-going annual and event disclosure, is accurate and complete. Failure to meet this obligation can lead to significant penalties, including fines and a bar from involvement with the issuance of municipal bonds, potentially threatening the ability of such officers to continue to serve in their existing positions.

What can officers of health care borrowers do to protect themselves from such liability?

1. Understand the scope of the borrower's disclosure responsibilities.
2. Assemble a strong team of internal staff and external experts to assist in preparing disclosure, both for the primary offering and for continuing disclosure.
3. Ensure that you obtain input from those persons in your organization that are knowledgeable about the various areas that are addressed in the disclosure document – it is unlikely that any single person will have all of the necessary information to prepare accurate and complete disclosure.
4. Do not completely rely on others. Read the draft disclosure and test the statements, ask questions of those preparing the materials and be certain that any inaccuracies that come to light are corrected. Do not assume that someone else will catch an inaccurate statement; ultimately, the document is the issuer or borrower's responsibility.

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Foley & Lardner LLP

David Y. Bannard

Partner

David Y. Bannard is a partner and business lawyer with Foley & Lardner LLP. He focuses his practice on representing airports in a wide variety of matters, including regulatory compliance, leasing, rate-setting and concessions agreements, and public finance matters. Mr. Bannard is an experienced bond lawyer, having served as bond counsel to airports and other issuers, and counsel to borrowers and underwriters, as well as in-house issuer's counsel, in many transactions. He is a member of the firm's Finance & Financial Institutions, Public Finance,…

dbannard@foley.com
617.342.4033
www.foley.com