Bond Case Briefs

Municipal Finance Law Since 1971

SEC Obtains Court Judgment Against Unregistered Municipal Advisors.

Fraudulent La. Bond Offering to Improve a City Sewer System

One of the consequences of the collapse of various portions of the financial markets in the Great Recession of 2007-2009 was the passage of the Wall Street Reform and Consumer Protection Act of 2010, better known as the Dodd-Frank Act. Among the Act's other innumerable provisions was a requirement that persons (with certain exceptions for professionals such as attorneys and accountants) register with the Municipal Securities Rulemaking Board ("MSRB") as "municipal advisors." The MSRB itself is both created and supervised by the U.S. Securities and Exchange Commission ("SEC") under Section 15 B of the Securities Exchange Act of 1934, as amended (the "34 Act"). Section 975(a)(5) of the Dodd-Frank Act forbids a "municipal advisor" from engaging in any fraudulent, deceptive, and/or manipulative practice, because Congress found that they had. I have previously discussed these developments at length in my Sept. 29, 2020 blog "What if the Adviser is Suspect? Municipal Securities Advisor Registration and Dereliction." That blog also reports on a series of SEC and MSRB enforcement actions where "municipal advisors" failed to register as required and/or engaged in fraudulent, deceptive, and/or manipulative practices.

In 2017 and 2018, the small city of Sterlington, Louisiana, a town of some 2,600 residents, sold two issues of revenue bonds "to finance the development of a water system and improvements to its existing sewer system," according to a Sept. 19, 2022 SEC Press Release. As spelled out at length in my June 27, 2022 blog "Serving the Public? SEC Charges Two Municipalities and Their Leaders with Bond Fraud," bond issuances in Louisiana require prior presentation to, and approval by, the Louisiana State Bond Commission. That process is an effort to prevent fiscally unwise and even unsustainable borrowings. In the end, though, the process is dependent upon the quality of financial information, including projections submitted to the Bond Commission. In the case of Sterlington, the historical and projected number of sewer customers was "substantially overstated" in order to support the bond issues when, in fact, the actual sewer system revenues would not be sufficient to cover the debt service on the bonds. The Public Finance Abuse Unit of the SEC, created in 2010 to deal with the ever-growing instances of inadequate disclosure and fraud involving municipal securities, took the lead in investigating the Sterlington sewer financings.

As reported in my "Serving the Public?" blog, after the SEC sued Sterlington, its former mayor, and its unregistered municipal advisor, the town consented to the entry of a judgment against it while the former mayor continued to litigate the matter. Now comes news that the unregistered municipal advisor, Twin Spires Financial, LLC, and its principal, Aaron B. Fletcher, consented to the entry of a judgement against them, which was entered by the Court on Aug. 2, 2022. Although Twin Spires Financial, LLC, is headquartered in Frisco, Texas, Fletcher is a graduate of the University of Kentucky, hence the reference in his company's name to the "Twin Spires" of Churchill Downs, the Louisville home of the Kentucky Derby. The Sept. 19, 2022 SEC Press Release in this matter reports that after the defendants consented to the entry of a judgment enjoining them from future violations of the anti-fraud and municipal advisor registration, ordering disgorgement of their ill-gotten gains plus prejudgment interest, and imposing a civil money penalty, the Court ordered that they (jointly and severally) pay disgorgement of $26,303 plus interest of $6,642.88, and pay a penalty of $200,000. A poor return (even in pure economic, let alone reputational, damage) from activity that generated only $26,303 of gain.

By Peter D. Hutcheon

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