Bond Case Briefs

Issue 486

Municipal Finance Law Since 1971

- **Ed. Note: We'll be off next week. You're welcome.**
- Hawkins: The Regulatory Impact of Jarkesy, Loper Bright, and Corner Post
- Profiting From Financings for Charter Schools: SEC Sues Unregistered, Fee-Splitting Municipal Advisor – Norris McLaughlin
- Proposed Rule Change Consisting of Amendments to MSRB Rule G-14 and to Amend FINRA Rule 6730: SIFMA Comment Letter
- Institutional Investors Pay Half Price of Retail Buyers in Muni Trades.
- Texas Drought Forces Small Town to Default on Water System Debt.
- Buffalo's Home County to Issue 'Bills Bonds' for NFL Stadium.
- *River Creek Development Corporation and City of Hutto, Texas v. Preston Hollow Capital, LLC* – Court of Appeals upholds validity of conduit bonds issued by city and local government corporation formed to assist with the financing of a newly-created public improvement district, finding that the parties had lawfully entered into an interlocal agreement, including its provisions requiring the city to make payments from its levied assessments to the local government corporation to secure its issuance of indebtedness to finance the improvements.
- And Finally, When We Remember We Are All Mad, The Mysteries Disappear And Life Stands Explained – Mark Twain is brought to us this week by *Ryan v. State*, in which Ray Ryan was remanded to solitary confinement (only those of us who've had the pleasure are allowed to refer to is as "The Hole"). Upon his return to the general population (of the prison, not the State of Nebraska) he discovered that the property left behind in his cell had been stolen. He then sued the Nebraska Department of Corrections to recover the value of said property. In the amount of $496.05. Four Hundred. Ninety Six. And Five Cents. Your Editor's life (such as it is) has come to a screeching halt. The (imaginary) girlfriend has left. The cat has died. All because he can think of nothing else but the galactically gob-smacking mystery of how Mr. Ryan arrived at the five cents. Fortunately, we still have 5 to 10 to get to the bottom of this. Or less, with good behavior.

LABOR & EMPLOYMENT - CALIFORNIA

Stone v. Alameda Health System

Supreme Court of California - August 15, 2024 - P.3d - 2024 WL 3819163

Employees, who formerly worked at hospital, brought putative class action against employer, which was county health system established by county board of supervisors, for alleged violations of wage orders and statutes governing meal and rest breaks and full and timely payment of wages, for penalties under Labor Code Private Attorneys General Act of 2004 (PAGA), and for other claims. Employer demurred.

The Superior Court sustained demurrer without leave to amend, finding provisions of Labor Code and wage orders at issue did not apply to employer as public agency. The First District Court of Appeal reversed in part. Petition for review was granted.

The Supreme Court held that:

- Public employers were not “employers” within meaning of meal-and-rest-break provisions of Labor Code and wage order covering hospital workers;
- As a matter of first impression, Labor Code’s definition of “person” excluded non-enumerated entities, including public entities;
- County health system was public entity excluded from Labor Code’s definition of “person”;
- County health system was “municipal corporation” excluded from certain wage-payment provisions of Labor Code; and
- PAGA exempts public employers from penalties for violations of Labor Code provisions carrying their own penalties; disapproving *Sargent v. Bd. of Trustees of Cal. State Univ.*, 61 Cal.App.5th 658, 276 Cal.Rptr.3d 1.

Government employers were not “employers” within meaning of Labor Code provisions imposing meal-and-rest-break obligations on employers and wage order provisions entitling hospital workers to meal and rest breaks; wage order required “employer” to be “person” as defined by Labor Code, Labor Code in turn limited definition of “person” to “any person, association, organization, partnership, business trust, limited liability company, or corporation,” thereby excluding entities not expressly mentioned, legislature specified that other provisions of Labor Code applied to public employers, wage order, which covered hospital workers, expressly excluded public employees from its scope absent contrary language in a provision, and legislature chose not to displace wage order’s exclusion.

Text of statute enabling specific county’s board of supervisors to create county health system to provide medical care to indigent residents demonstrated that legislature considered health system to be quasi-governmental “public entity,” for purpose of determining whether health system was exempt from meal-and-rest-break obligations imposed on employers under Labor Code and under wage order covering hospital workers; enabling statute described health system as “public agency” and made its affairs intertwined with and dependent upon county, health system as public hospital authority was “public entity” as defined in Health and Safety Code, and enabling statute set forth health system’s rights, liabilities, and exemptions under laws applying specifically to public entities.

In statute enabling specific county’s board of supervisors to create county health system, subdivision stating that health system “shall be a government entity separate and apart from the county, and shall not be considered to be an agency, division, or department of the county” did not indicate legislature meant to subject health system to meal-and-rest-break requirements of Labor Code and of wage order covering hospital workers notwithstanding such requirements’ general exemption of public entities; subdivision expressly classified health system as “government entity,” public-entity exemption did not extend only to divisions of a state or local government body, and enabling statute gave health system some of the same powers, obligations, and protections as a division of government.

Definitions of “political subdivision” in False Claims Act, which included any “legally authorized local governmental entity with jurisdictional boundaries,” and California Voter Participation Rights Act, which referred to “geographic area of representation created for the provision of government services,” did not impose requirement of “geographic jurisdiction” for county health system or any other public employer to qualify as “political subdivision” under Labor Code’s definition; Labor Code did not refer to need for “geographic jurisdiction,” and similarly broad definitions of term “political subdivision” appeared in other codes without any requirement of geographic jurisdiction.

Whether a public entity is exempted from meal and rest break obligations imposed on employers by the Labor Code and the wage order covering hospital employees does not depend on whether

applying those obligations to the public entity in question would cause infringement of sovereign powers; besides the absence of a statutory basis, such an outcome would frustrate the legislature's clear intent to exclude public entities from the Labor Code requirements at issue.

The term "municipal corporation" in the Labor Code section stating that certain wage-related provisions "do not apply to the payment of wages of employees directly employed by any county, incorporated city, or town or other municipal corporation" refers to something other than a county, incorporated city, or town; the only reasonable interpretation of this section is that the legislature knew from the decided cases that "incorporated city or town" referred to a municipal corporation in the strict sense, and intended that "or other municipal corporation" should refer to municipal corporations in the commonly accepted sense, that is, public corporations or quasi-municipal corporations, and this construction is consistent with legislative history and administrative interpretations.

County health system, which legislature authorized county board of supervisors to create to provide medical care to indigent residents, was "municipal corporation" within meaning of Labor Code section stating that certain wage-payment provisions, including those governing semimonthly payments and creating penalty and cause of action for failure to make payments, "do not apply to the payment of wages of employees directly employed by any county, incorporated city, or town or other municipal corporation."

The Labor Code Private Attorneys General Act (PAGA) exempts public employers from penalties for violations of Labor Code provisions which establish their own penalties recoverable by the Labor and Workforce Development Agency; PAGA specifies that the Labor Code's definition of person, which excludes public entities, applies throughout PAGA, including to the provisions referring to employers subject to suit as "persons," legislative history demonstrates that PAGA's use of this definition of "person" was intentional, and requiring public entities to pay PAGA penalties would contravene the public policy behind the statute shielding public entities from punitive sanctions; disapproving *Sargent v. Bd. of Trustees of Cal. State Univ.*, 61 Cal.App.5th 658, 276 Cal.Rptr.3d 1.

LIABILITY - NEBRASKA

Ryan v. State

Supreme Court of Nebraska - August 9, 2024 - N.W.3d - 317 Neb. 337 - 2024 WL 3732939

Inmate brought negligence action against State pursuant to the State Tort Claims Act (STCA), alleging that Department of Correctional Services (DCS) failed to fulfill its duty under state regulations to investigate his allegation that other inmates stole his property.

The District Court dismissed for lack of subject matter jurisdiction. Inmate appealed.

The Supreme Court held that inmate disciplinary procedure statutes and regulations did not give rise to a tort duty of State to investigate alleged theft of inmate's property.

Inmate disciplinary procedure statutes and regulations did not give rise to a tort duty of State to investigate alleged theft of inmate's property by other inmates, and therefore inmate did not have an actionable negligence claim against State under the State Tort Claims Act (STCA); statutes and regulations were enacted to prescribe disciplinary procedures for inmates who allegedly engaged in such misconduct.

PUBLIC EMPLOYMENT - OHIO

Harmon v. City of Cincinnati

Supreme Court of Ohio - August 6, 2024 - N.E.3d - 2024 WL 3657975 - 2024-Ohio-2889

City employees, who were members of city employees union, appealed determination of city's civil service commission that employees were not entitled to hearing on their appeal to commission of city's decision to place them on leave under emergency leave program due to COVID-19 pandemic.

The Court of Common Pleas reversed. City and commission appealed. The First District Court of Appeals held that Court of Common Pleas had jurisdiction to consider employees' appeal. The Supreme Court accepted city and commission's appeal.

The Supreme Court held that:

- Specific layoff provisions of collective bargaining agreement (CBA) between city and city employees union prevailed over management rights clause of CBA to determine whether employees could appeal decision of civil service commission to court of common pleas;
- CBA allowed employees to enforce their individual employee rights concerning conditions of employment not specified in CBA through normal civil service, regulatory, or judicial processes, for purposes of whether employees could appeal decision of civil service commission to court of common pleas;
- Policy reasons did not preclude employees from appealing decision of civil service commission to court of common pleas; and
- Commission's decision that leave was not a layoff was from a "quasi-judicial proceeding," such that employees were permitted to appeal decision to court of common pleas.

CONDUIT BONDS - TEXAS

River Creek Development Corporation and City of Hutto, Texas v. Preston Hollow Capital, LLC

Court of Appeals of Texas, Austin - August 22, 2024 - Not Reported in S.W. Rptr. - 2024 WL 3892448

River Creek Development Corporation (River Creek) and the City of Hutto, Texas (the City), appealed from the trial court's final judgment rendered in favor of Preston Hollow Capital, LLC; 79 HCD Development, LLC; Public Finance Authority; and U.S. Bank National Association. The judgment granted the parties' respective summary-judgment motions and awarded each of them attorney's fees and costs.

In June 2018, the City passed a resolution authorizing creation of a Public Improvement District (the PID) to undertake and finance public improvements for the benefit of property within the PID. The PID's 2018 Service and Assessment Plan identified the initial improvements at a cost of $17.4 million.

In September 2018, the City passed a resolution authorizing the creation of River Creek, a local government corporation, to "assist with the financing" of the PID development pursuant to Tex. Transp. Code § 431.101.

In December 2018, the City, River Creek, and other parties executed a series of agreements to

secure the development and financing of the PID. Among the parties in some of those agreements is appellee Public Finance Authority (PFA), a Wisconsin-based governmental entity. Rather than issue the bonds themselves, the City and River Creek chose to structure the transaction using PFA as a conduit issuer of the bonds to avoid potential liability and reduce financial risk.

Following a series of internal governmental disruptions, River Creek and the City brought this action for declaratory relief.

They sought the following declarations:

1. An "installment sales contract" described by the interlocal agreement provides "insufficient legal authority for all stated installment payments due under such a contract to be authorized costs of improvements under the PID Act";
2. The bonds were not issued in strict compliance with the PID Act and applicable state law;
3. Transportation Code Section 431.006 limits the applicability of the general authority of Chapter 22, Business Organizations Code, because of the express statutory requirement in Section 431.071 that "notes" be submitted to the attorney general or the express statutory statement in Section 431.108 that the operations of a local government corporation are governmental; and
4. Government Code Section requires all promissory notes issued by a Chapter 431 corporation or a local government corporation be submitted to the attorney general for examination.

Preston Hollow answered and filed a counterclaim seeking a declaratory judgment that:

1. The loan agreement and promissory note are valid and enforceable,
2. The bonds did not need to be submitted to the AG for review and approval, and
3. The City and River Creek lawfully entered the interlocal agreement.

The Court of Appeals held that:

1. The loan agreement was valid and enforceable;
2. The promissory note is valid and enforceable;
3. The bonds issued by PFA did not need to be submitted to the AG for approval; and
4. The City and River Creek lawfully entered into the interlocal agreement, including its provisions requiring the City to make payments from its levied assessments to River Creek to secure River Creek's issuance of indebtedness to finance the improvements.

"We conclude that the legislature's silence on the consequences of failure to obtain AG approval, its failure to expressly condition the validity and enforceability of a Section 431.070 bond or note on AG approval, and its express requirement that a corporation merely "submit" the subject instrument "for examination" (as opposed to, e.g., "obtain AG approval") are dispositive and support the trial court's challenged first and second declarations."

"The 'indebtedness' that River Creek issued to PFA via the promissory note and loan agreement—including any 'costs of issuance,' such as transaction-financing costs or bond-issuance fees, that River Creek undertook as part of that indebtedness—falls under Section 372.026(f), and River Creek is entitled to recoupment of such costs through the interlocal agreement."

"We hold that Section 372.026 expressly authorizes the interlocal agreement to require the City to make payments from its assessments to River Creek to secure its costs of issuing debt to PFA and thus that the interlocal agreement is not void as appellants contend."

State of California: Fitch New Issue Report

The state of California's 'AA' Issuer Default Rating (IDR) incorporates the state's large and diverse economy, which supports strong, albeit cyclical, revenue growth prospects, a solid ability to manage expenses through the economic cycle and a moderately low level of long-term liabilities. Strong fiscal management, institutionalized across administrations and demonstrated through the buildup of the budgetary stabilization account (BSA) and elimination of past budgetary borrowing, allows the state to better withstand economic and revenue cyclicality.

Access Report

Tue 20 Aug, 2024 – 12:11 PM ET

California Munis for Police, Teacher Housing Show Cracks.

- **Local agencies sold as much as $10 billion of the bonds**
- **Deals were highly levered and rely on high occupancy**

High-yield municipal bonds issued to finance housing for police officers, teachers and nurses in California are showing signs of strain.

Mira Vista Hills Apartments, a 280-unit rental complex in the Bay Area city of Antioch, disclosed in a Friday filing that it didn't meet a debt-service coverage ratio required by investors. At least four other complexes, known as "workforce housing," have drawn on reserves since the start of 2023 to help pay their debt, according to securities filings.

About $8 billion to $10 billion of munis — all in a speculative category without a credit rating — have been issued in California to convert market-rate apartments into affordable housing for middle-income households, according to research firm Municipal Market Analytics. Seven of the nation's 10 priciest housing markets are in the state, according to the National Association of Realtors.

Continue reading.

Bloomberg Markets

By Martin Z Braun

August 20, 2024

Texas Drought Forces Small Town to Default on Water System Debt.

- **Clyde, Texas, missed its Aug. 1 municipal bond payment**
- **The action caused S&P to drop debt rating from A- to D**

A persistent drought in Texas is hurting the finances of a small town, making it unable to pay bondholders in a rare instance of climate-related default.

The city of Clyde, located roughly halfway between Dallas and Midland, informed investors it couldn't make a debt payment due in August, according to a securities filing. Instead, its bond insurers — Assured Guaranty and Build America Mutual — were asked to cover the payment, illustrating the financial strain facing the city.

"Such draw is unscheduled and reflects financial difficulties of the issuer, including without limitation financial difficulties resulting from increased costs related to operations and maintenance of the issuer's waterworks and sewer system," the filing dated Aug. 15 read. The bonds were sold to support the city's water and wastewater system.

That caused S&P Global Ratings to drop the grade on the bonds to D from A-, a whopping 15-notch downgrade, according to a report from the company late Friday. It also cost the city its A- credit rating, as S&P downgraded Clyde's general-obligation debt to B, which is below investment-grade.

Analysts led by Misty Newland wrote that "a lack of willingness to pay an unconditional debt obligation results in a rating cap."

Clyde is a commuter community near Abilene, and is home to about 4,000 residents. Roughly one-third of Callahan County, where it's located, is facing a moderate drought. The city has been implementing a drought-contingency plan for several years, which includes double-digit water reductions. Following the restrictions, the town's water sales decreased — which hit revenues.

On Aug. 1, the day the bond payment was due — Clyde issued a "water emergency" notice, outlining "severe water shortage" conditions with the intention of reducing usage by 30%.

Local government bond defaults are incredibly rare, with those caused by climate-related events all but unprecedented. While bondholders will be made whole because the debt is insured, Clyde's financial challenges are a stark reminder that the $4 trillion municipal bond market isn't without risk and extreme weather can pose a threat.

Texas is the epicenter of such weather events in the US, and has faced multiple disasters this year. Hurricane Beryl knocked out power in Houston for days in July. A May derecho punched windows out of skyscrapers in the city and a storm that month dropped hailstones the size of DVDs near Lubbock. The largest wildfire in state history burned more than 1 million acres in the panhandle in February and March.

Currently, more than 30% of Texas is experiencing drought conditions, according to the US Drought Monitor. The most extreme issues are in western part of the state, but almost all of North Texas is facing dryness. Governor Greg Abbott has issued a drought disaster proclamation for the state.

To help reduce water usage, officials in Clyde have prohibited the use of water for cleaning sidewalks and driveways. Only new lawns at residents' homes can be watered, not existing ones.

The drought has affected life in other ways. Some residents were unhappy that a splash pad — which is a playground of sprinklers used by children — wasn't working, according to local news station KTXS.com.

"Would you rather have your splash pad running so your kid can spend two hours a day in the water there, or do you wanna be able to bathe your kid with water at your house?," the mayor told KTXS.com.

Michael Stanton, head of strategy and communications at Build America Mutual, said in an emailed statement that the company's insurance protected investors. "Although this is a small exposure, our team is in contact with city officials and their professional advisors and will continue to represent bondholders' interests in those discussions," the statement read.

Robert Tucker, senior managing director of investor relations and communications at Assured Guaranty, said in a statement that bondholders would be protected. "The type of situation Clyde, Texas, encountered – unexpected conditions leading to the non-payment of debt service – is exactly what our bond insurance is designed for," he said.

Bloomberg Green

By Amanda Albright

August 19, 2024

— With assistance from Jeremy Diamond, Will Wade, and Songyan Yu

---

Houston Schools Propose Largest Debt and Property Tax Increase in Texas History.

Voters would have to approve a $4.4 billion bond package in November, to be financed by property tax increases over 33 years. Including interest, the package would cost $11 billion.

The Houston Independent School District board voted last week to pass a $4.4 billion bond proposal. This total excludes the interest on the principal. When included, it brings the total debt obligation to nearly $11 billion.

To pay for it, the board will authorize levying new, additional property taxes over 33 years, if voters approve the proposal in November. Taxpayers would be saddled with additional debt and taxes through 2058, according to the bond certificate filed by the district.

This is the largest debt and property tax increase proposal in state history.

Continue reading.

governing.com

Aug. 14, 2024 • Bethany Blankley, The Center Square

Peace River Manasota Regional Water Supply Authority (FL): Fitch New Issue Report

The 'AA' rating on the revenue bonds and 'AA' Issuer Default Rating (IDR) reflect Peace River Manasota Regional Water Supply Authority's 'Very Strong' financial profile in the context of its 'Very Strong' revenue defensibility and operating risk profile, as well as the very strong credit quality of the authority's two largest wholesale customers — Sarasota County, FL (utility system rated 'AA+')

and Charlotte County, FL. The authority's revenue defensibility is supported by strong contract provisions with the ability to reallocate costs, limiting bondholder exposure to individual members. The purchasers' obligation to make payments to the authority is unconditional and payable as an operating and maintenance expense of their respective utilities based on proportional water use. The authority's operating risk assessment reflects a very low operating cost burden and moderate life cycle investment needs. The revision of the outlook to Negative from Stable reflects the authority's projected increases in leverage, measured as net adjusted debt to adjusted funds available for debt service (FADS), as it works through a capital-intensive period driven by surface water expansion projects to meet growing demand. Leverage registered 6.1x in fiscal 2023 and is expected to grow substantially to 17.8x in fiscal 2025 in Fitch's rating case scenario.

Access Report

Thu 22 Aug, 2024 – 2:30 PM ET

McKinsey: Will Mortgages and Markets Stay Afloat in Florida?

Flood risk is rising in Florida due to climate change. How exposed is residential real estate—both directly and indirectly—and what can be done to manage the risks?

Located in a tropical cyclone zone with low elevation and an expansive coastline, Florida faces numerous climate hazards, including exposure to storm surge and tidal flooding that are worsened by sea level rise, and heat stress due to rising temperatures and changes in humidity. Other unique features include the state's porous limestone foundation which can exacerbate flooding as water seeps into properties from the ground below and also causes saltwater intrusion into water aquifers, and makes adaptation challenging.

Much of Florida's physical and human capital is located along its vulnerable coast. Two-thirds of the state's population lives near the coastline, exposing many of them to tidal flooding, and almost 10 percent is less than 1.5 meters within sea level. At the same time, Florida's economy depends heavily on real estate. In 2018, real estate accounted for 22 percent of state GDP. Real estate also represents an important part of household wealth for the 65 percent of Floridians who are home owners: primary residences represent 42 percent of median home owner wealth in the United States.

In this case study, we focus on residential property in Florida exposed to flooding from storm surges and to tidal flooding and assess the likely impact both in terms of direct and knock-on effects, for example through housing price adjustments (See sidebar: An overview of the case study analysis).

Continue reading.

McKinsey Global Institute

April 27, 2020

Sixth Circuit Considering Whether Placing a Water Lien on a Property Could

Violate the Fair Housing Act.

In 1968, the Federal Fair Housing Act (FHA) was enacted to protect individuals from discrimination based on certain protected characteristics when they are renting or buying a home, getting a mortgage, seeking housing assistance, or engaging in other housing-related activities. However, a recent class action lawsuit—which is currently on appeal before the federal Sixth Circuit—seeks to stretch one provision of the FHA further than any other case before it, with significant consequences to municipalities.

Under 42 U.S.C. § 3604(a), which codified Section 804 of the FHA, it is unlawful to "make [housing] unavailable" to individuals based on those protected characteristics. Actions such as redlining, discriminatory pricing, racial steering, and discriminatory appraisals have all been held to violate § 3604(a).

But in 2019, a group of individuals filed a class action against the City of Cleveland, Ohio, under § 3604(a). See *Picket et al. v. City of Cleveland*, Case No. 19-cv-2911 (N.D. Ohio). Their claim? That Cleveland makes housing unavailable when it certifies a tax lien against a property when the owner or tenant has let their water bill become seriously delinquent. (State law allows cities to certify liens in that circumstance, and the plaintiffs do not challenge that authorization.)

Continue reading.

Frost Brown Todd LLP – Philip K. Hartmann, Jesse J. Shamp and Anthony R. Severyn

August 22 2024

NJ Lines Up $2.4 Billion Muni Bond Sale for Transportation Fixes.

- **A state trust fund will invest billions to modernize transit**
- **The bonds were assigned an 'A' rating by Fitch Ratings**

New Jersey is poised to sell $2.4 billion of bonds for its transportation infrastructure, according to a report from Fitch Ratings.

The New Jersey Transportation Trust Fund Authority is expected to issue $1.3 billion of transportation system bonds and roughly $1.1 billion of transportation program bonds through a negotiated sale in October, the Fitch report said.

The fund is charged with modernizing statewide transportation infrastructure like highways and bridges as well as providing additional capital funding for NJ Transit — New Jersey's public transit agency. The state is expected to extend as much as $8.8 billion in bonding authorization to the authority over the next five years, or approximately $1.76 billion annually, according to a March press release.

Continue reading.

Bloomberg Markets

By Sri Taylor

August 20, 2024

[Casino Reinvestment Development Authority, New Jersey: Fitch New Issue Report]

Future growth is likely to resemble pre-pandemic trends, with longer-term growth prospects limited, supporting a 'bbb' assessment. Factors potentially affecting long-term growth include the effects of competing regional gaming options, online gambling and sports betting. The sharp rebound in pledged revenue following pandemic-related shutdowns in 2020 has rebuilt the structure's cushion against volatility relative to recent years. Additional leverage in the current sale modestly reduces the structure's cushion against future revenue volatility, but resilience remains consistent with an 'a' assessment. The Casino Reinvestment Development Authority is an instrumentality of the State of New Jersey, which is the collection agent for luxury taxes. The brief deposit of these revenues in the state's general fund caps the rating at New Jersey's Issuer Default Rating (IDR) of 'A+'/Stable; this is not currently a rating factor for the bonds given that the bond rating is four notches below the state's IDR. Pledged revenues are separate from the financial operations of the city of Atlantic City.

Access Report

Tue 20 Aug, 2024 – 12:41 PM ET

Penn State Will Likely Take On Up to $700M in Debt for Beaver Stadium Upgrades. How Will It Pay It Back?

STATE COLLEGE — Penn State is prepared to take on up to $700 million in debt to renovate Beaver Stadium, a price tag drawing scrutiny at a time when the university is implementing steep budget cuts and offering buyouts to some employees.

The school has emphasized that the athletics department, which has a self-sustaining budget, will pay back the debt and interest incurred through the renovation process. Students' tuition and taxpayer dollars will not fund the project, the university has said.

However, Penn State University is likely to take on the necessary debt rather than the athletics department. One expert told Spotlight PA this setup is typical for universities and allows an organization like Penn State to secure better financing costs.

Penn State generally uses its standing as a public university with tens of thousands of tuition-paying students to secure bonds and provide financial backing for debt, according to a review of bond documents. For example, last year Penn State sold $204 million in bonds under the university's authority. That sale was used in part to finance "replacements to and renovations of Beaver Stadium," though the university said at the time the bonds would be repaid by athletics.

Penn State declined to make an official available for an interview for this story. A university spokesperson wrote in an email that the university's support for the project "is a signal of the commitment to bettering our student-athletes' experience and as a land-grant university, elevating Beaver Stadium's significance in driving local and state economies."

Christopher Collins, vice president and senior municipal credit analyst at Moody's Ratings, told Spotlight PA that although universities could have specific departments take out debt — perhaps as a way to increase accountability — issuing bonds through the entire university lowers financing

costs. A university generally has a better credit rating, and a wider source of possible repayment, than a specific department, said Collins, who has analyzed Penn State's credit rating.

Some university trustees questioned what would happen if Penn State defaults on the debt. Penn State's athletic department reported $126,000 in profit off of a $202 million total budget in fiscal year 2023.

By Wyatt Massey Spotlight PA State College Aug 22, 2024

Buffalo's Home County to Issue 'Bills Bonds' for NFL Stadium.

When it comes to the construction of the Buffalo Bills' $1.7 billion new stadium, local officials are taking the concept of "public financing" to a new level.

On Sept. 24, Erie County in western New York will offer fans the opportunity to buy "Bills bonds" toward the development of the new facility being built next door to Highmark Stadium. The county is issuing $125 million in bonds to pay half of its portion toward construction.

The county is offering the bonds to individuals for a single day before it offers them to outside investors.

"This is a once-in-a-generation opportunity," county comptroller Kevin Hardwick said in a radio interview on Monday, "and there might be some average Bills fans out there who normally do not invest in municipal bonds, who might be interested in saying to themselves or telling their grandchildren that I had a hand in helping construct that stadium."

The minimum investment for the bond is $5,000. The website for the bond offering indicated that "the Series 2024B Bonds are general obligations of the County and are not an obligation of the Buffalo Bills."

Sportico has reached out to the Erie County's comptroller office as well as the Bills, but has not heard back.

Construction of the new Highmark Stadium is being funded largely by taxpayers in one of the most controversial stadium financing deals in recent memory. In March 2022, New York Gov. Kathy Hochul, herself a Buffalo native, announced a deal between the Bills, the state and county to develop the 62,000-seat, open-air stadium in Orchard Park next door to the team's current home.

Of the $1.4 billion in financing, the state will contribute $600 million while Erie County will put in $250 million. The NFL will loan $200 million to the Bills, and the team itself will add $350 million. The $850 million in state and county contributions are the largest public subsidy ever committed to the development of an NFL stadium. The team will have a 30-year lease for the new field, which will officially be owned by the state.

Healthcare insurer Highmark Blue Cross Blue Shield of Western New York is carrying on its naming rights deal from the current building, which originally opened as Rich Stadium in 1973, to the new stadium. The current Highmark Stadium was also known as Ralph Wilson Stadium after the late founding owner, and New Era Field until the insurer took the rights in 2021.

In April, the Pegula family retained Allen & Company to facilitate the sale of a non-controlling

minority stake in the Bills, with a reported "working figure" of 25% to be offered. The Bills are worth $5.03 billion, according to Sportico's latest NFL franchise valuations, published last week. Buffalo ranks 23rd among all 32 teams, jumping three spots compared to one year ago, as the price tag rose by 23%.

sportico.com

By Jason Clinkscales

August 26, 2024 3:54pm

[New York City, New York: Fitch New Issue Report]

New York City's 'AA' Long-Term IDR and GO bond ratings reflect New York City's exceptionally strong budget monitoring and controls, supporting Fitch Ratings' 'aa' financial resilience assessment given the city's 'high' revenue control, 'mid-range' expenditure control and Fitch's expectation that the city will maintain reserves at or above 7.5% of spending. For the purposes of this calculation, Fitch includes unrestricted general fund reserves (the sum of committed, assigned and unassigned), the available balance in the retirees' health benefits trust (RHBT) and the fiscal year-end budget stabilization and discretionary transfers of surplus for prepayment of certain of the following year's operating expenditures. The available balance as of fiscal year-end 2023 was $12.8 billion, equal to 11.8% of expenditures and transfers out.

[Access Report]

Mon 19 Aug, 2024

[The City of New York Announces Successful Sale of $1.8 Billion of General Obligation Bonds.]

The City of New York (the "City") announced the successful sale of $1.8 billion of General Obligation bonds, comprised of $1.5 billion of tax-exempt fixed rate bonds and $300 million of taxable fixed rate bonds. Proceeds from the sale will be used to fund capital projects.

The City received over $327 million of orders during the retail order period and $4.9 billion of priority orders during the institutional order period, which in total represents approximately 3.5x the tax-exempt bonds offered for sale.

Due to investor demand for the tax-exempt bonds, yields were reduced relative to the start of the institutional order period by 2 basis points in 2028, 2029, and 2042; by 3 basis points in 2027 and 2052; by 4 basis points in 2041, 2047, and 2048; by 5 basis points in 2030, 2043, and 2044; by 6 basis points in 2050; and by 8 basis points in 2031.

Final yields ranged from 2.62% in 2026 to 4.19% in 2052.

The tax-exempt bonds were underwritten through a syndicate led by book-running lead manager Loop Capital Markets, with BofA Securities, J.P. Morgan, Jefferies, Ramirez & Co., Inc., RBC Capital

Markets, Siebert Williams Shank, and Wells Fargo Securities serving as co-senior managers.

The City also sold $300 million of taxable fixed rate bonds via competitive bid. The bid attracted 8 bidders, with J.P. Morgan winning at a true interest cost of 4.617%.

August 22, 2024

NYC Drama School Faces 14.5% Interest Rate on Muni-Bond Breach.

- **American Musical and Dramatic Academy borrowed money in 2023**
- **School faces penalty for covenant default related to cash pile**

A drama and arts school with campuses in New York City and Los Angeles is facing an interest rate as high as 14.5% as a penalty for breaching an agreement with its municipal bondholders.

The American Musical and Dramatic Academy didn't maintain a cash pile that would last three months, breaking an agreement with holders led by Preston Hollow Community Capital. The school had 67 days of cash on hand as of June 30, while it was supposed to maintain 90 days, a regulatory filing shows. Such a breach is known as a covenant default.

Now, the academy will have to pay jacked-up interest rates between 12.25% and 14.5% on two series of debt, according to letters sent to the school this month by Preston Hollow. The correspondence was included in a securities filing posted Thursday. The two series of bonds priced with already-high coupons of 7.25% and 9.5%, according to data compiled by Bloomberg.

Such a move by bondholders is rare in the municipal market. It's more common for investors to enter into forbearance agreements with struggling borrowers — meaning holders pledge not to take actions such as demanding immediate repayment on debt even if they have that right. For colleges, these agreements provide a runway to fix their finances while often requiring them to disclose more regular information or hire a consultant to offer suggestions.

The right to charge higher interest rates if a borrower defaults is a common protection that corporate and real estate lenders write into their credit documents. In practice, the ability to charge default interest often becomes a key element of negotiations between the parties on how to resolve the borrower's financial challenges.

Such penalties risk worsening distressed borrowers' financial situation, said Eric Kazatsky, senior US municipals strategist for Bloomberg Intelligence.

A spokesperson for Preston Hollow declined to comment. John Galgano, AMDA's chief operating officer, didn't reply to phone calls or email messages seeking comment. David Silverman, the school's chief financial officer, didn't respond to an emailed request for comment.

Campus Real Estate

The American Musical and Dramatic Academy opened in 1964 and is a prominent performing arts institute with about 3,000 students stretched across two campuses, on Manhattan's Upper West Side and in Hollywood. Its alumni includes Modern Family star Jesse Tyler Ferguson and pop star Jason Derulo.

This isn't the college's first brush with distress. The financings last year were meant to provide relief

to the academy after it went into covenant default on prior obligations.

In 2023, the school sold $91.6 million of bonds in two separate deals. The borrowing, which refinanced old debt and also included funds for campus projects, was originated by Preston Hollow and the firm purchased $51.65 million of the securities, according to a November statement from the company. The deal "gives AMDA the flexibility to build out exciting new initiatives as they continue to pursue their important mission," Ron Van Den Handel, a former managing director at Preston Hollow, said in the statement at the time.

Like other small US colleges, the school has struggled in recent years. Its performing-arts focus has also brought unique challenges, especially after Broadway performances closed during the pandemic. Total enrollment has been falling, dropping from 4,098 in 2018-19 to a projected 3,219 in 2023-24, according to the 2023 bond documents.

The letters from Preston Hollow say the school also needs to begin "real estate monetization procedures" as a result of the covenant breach. The 2023 bond documents noted that if the borrower couldn't satisfy certain financial covenants, it could be required to sell real estate.

The academy has several buildings in New York City and its main facility is located at 211 West 61st Street, close to Lincoln Center. It has an Art-Deco tower in Los Angeles blocks from the Hollywood Walk of Fame, along with other campus buildings.

Bloomberg Markets

By Amanda Albright

August 23, 2024

— With assistance from Erin Hudson

Fitch Places 18 U.S. Life Plan Communities Under Criteria Observation.

Fitch Ratings – New York – 22 Aug 2024: Fitch Ratings has placed 18 U.S. Life Plan Communities (LPCs) Under Criteria Observation (UCO), following the publication of Fitch's revised 'U.S. Public Finance Not-For-Profit Life Plan Community Rating Criteria' on Aug. 19, 2024.

The ratings placed on UCO will require additional information and analysis to fully assess the effect of the criteria on the ratings. While these ratings may be affected by the criteria changes, not all of the ratings designated as UCO will necessarily change. Placement on the UCO list does not indicate a change in the issuer's underlying credit profile, nor does it affect existing Rating Outlooks or Rating Watch statuses. Fitch will review all the ratings designated as UCO as soon as practicable, but no later than six months following the date of the criteria release.

Continue reading.

Fitch Feedback Report: U.S. Public Finance Not-for-Profit Life Plan

Community Rating Criteria

View the Report.

Mon 19 Aug, 2024

S&P Sustainability Insights Research: No Quick Fix For The U.S. Affordable Housing Shortage

Due to high mortgage interest rates and persistently high real estate prices, a median priced home is now unaffordable for a median income American household. Conditions are most acute for households in highly populated areas and earning less than the U.S. median income, over 63% of which now spend greater than 30% of household income on housing. Demand for assistance from U.S. affordable housing issuers has risen, leading to a 32% year-to-date increase in debt issuance over 2023 highs. At some point, not-for-profit housing issuers, particularly multifamily lenders, may struggle to preserve credit quality by deploying reserves to meet affordable housing needs.

Download

How Two States Have Spent Their Share of the $1B in Cybersecurity Grants.

With little precedent for such a big federal investment in cybersecurity, states have largely had to write their own playbooks on how to distribute the funds to local governments.

More than two years ago, the federal government began handing out millions of dollars to states to shore up their cybersecurity amid a growing threat of ransomware attacks and data breaches.

The much-needed investment will ultimately pay out an unprecedented $1 billion over four years. The State and Local Cybersecurity Grant Program under the 2021 infrastructure law is a first-of-i-s-kind investment, which has meant states have largely had to create their own playbooks.

At an event hosted this week by Route Fifty, those different approaches were highlighted as two states on opposite coasts detailed how they've gone about shoring up their cyber defenses under the historic grant program.

Continue reading.

Route Fifty

by Chris Teale

August 20, 2024

Climate Change is messing with City Sewers — And the Solutions are Even

Messier

As heavy rains overwhelm aging pipes, Boston and New York City are choosing very different paths forward.

At the end of July 2023, 3.07 inches of rain fell on Boston in a single day. The city's sewer systems were overwhelmed, resulting in a discharge of sewage into Boston Harbor that prompted a public health warning. The summer of 2023 would turn out to be Boston's second-rainiest on record.

About two months later, 8.65 inches of rain fell on New York City — higher than any September day since Hurricane Donna in 1960. The city's low-lying areas were deluged, and half of its subway lines were suspended as water inundated underground stations.

East Coast cities are increasingly susceptible to flooding due to climate change. But changing weather patterns are only half of the problem — the other is inadequate infrastructure. In particular, these recent flood events were made worse by Boston and New York's combined sewer systems, which carry both stormwater and sewage in the same pipes. When such a system reaches capacity during heavy rainfall or storm surge events, it backs up, sending a mixture of stormwater and raw sewage into waterways (and sometimes also into streets and homes).

Continue reading.

Route Fifty

By Angelica Ang,
Grist

August 22, 2024

Institutional Investors Pay Half Price of Retail Buyers in Muni Trades.

- **Smaller trades, a proxy for retail, paid average spread of $10**
- **Retail buyers rely heavily on the secondary market: report**

Retail investors, who hold the largest share of municipal bonds, pay roughly twice the spread that major institutional investors pay when trading recently issued debt.

The Municipal Securities Rulemaking Board measured the spread between prices on deals in the primary market and recent trades in the secondary market. Results showed trades of $100,000 or less, a proxy for retail buyers, paid an average spread of about $10, while trades of $1 million or more paid a spread of $4.42, according to a report published Monday. Institutional investors include major Wall Street firms, insurance companies, regional banks and foreign buyers, among others.

Retail buyers adding bonds to their portfolios rely heavily on the secondary market, where a flurry of trading occurs in the weeks following a new issue before trades tend to drop off. The price an investor secures can dictate the yield they receive for decades.

The report found only 8% of par purchased through large trades occurred in the secondary market, while the share for smaller transactions was closer to half. Researchers used data over a five-year period spanning 2019 to 2023, and measured spreads on purchases that took place in the first seven

days of secondary trading.

Spreads varied year to year and were considerably different between competitive and negotiated deals. For competitive deals, the average spread was $4.16, and the spread on negotiated deals was $11.30.

"We don't think this means issuers should flock to the competitive market," said John Bagley, chief market structure officer at the MSRB and one of the authors of the report. In general, competitive deals tend to come from larger, more well-known issuers.

Investors placing larger orders are able to command more attractive prices, narrowing the profit underwriters make bringing bonds to market. In competitive deals, the average spread on large deals was only 27 cents, and in 2022 and 2023 when rates were rising, the spread was negative.

"If you bought a competitive deal and you didn't sell it right away, and rates went against you, you likely had to cheapen up the deal to get it sold," Bagley said.

Bloomberg Markets

By Nic Querolo

August 26, 2024

— With assistance from Amanda Albright

Credit Work Takes Front Seat: Bloomberg Masters of the Muniverse

As we inch closer to a Fed rate decision and a Presidential election, focusing on municipal credit will take on a heavier emphasis. Hosts Eric Kazatsky and Karen Altamirano are joined by Jennifer Johnston, Director of Research for Franklin Templeton Fixed Income. Bringing over three decades of experience, Jennifer is responsible for leading the group's credit research efforts across all municipal bond sectors. She gives us her perspective on how technology enhances the credit research role and some areas of concern during the back portion of this year and beyond.

Listen to the Podcast.

Aug 20, 2024

Hawkins: The Regulatory Impact of Jarkesy, Loper Bright, and Corner Post

Introduction

This Hawkins Update reviews three recent Supreme Court decisions – *Jarkesy, Loper Bright, and Corner Post*.[1] Although these decisions are likely to substantially affect the rulemaking and enforcement activities of federal administrative agencies generally (including the Department of the Treasury and the Internal Revenue Service), we discuss the cases more specifically with respect to certain potential impacts on the Securities and Exchange Commission (the "SEC").

No Civil Penalties in Administrative Proceedings

In Jarkesy, the Supreme Court considered the manner in which the SEC brings enforcement actions and, more specifically, whether the Seventh Amendment entitles a defendant to a jury trial when the SEC seeks civil penalties for securities fraud.

In 2011, the SEC commenced an enforcement action against Jarkesy and his investment advisory firm, Patriot28, LLC ("Patriot28"). The SEC alleged that Jarkesy and Patriot28 misled investors in connection with the launch and management of two investment funds by: (i) misrepresenting the funds' investment strategies; (ii) hiding the identity of the funds' auditor and prime broker; and (iii) inflating the funds' claimed value to generate larger management fees. In initiating the enforcement action, the SEC alleged that these actions violated the antifraud provisions of the Securities Act, the Securities Exchange Act, and the Investment Advisers Act. The SEC sought remedies that included civil penalties. The SEC adjudicated the matter in-house, found that Jarkesy and his firm had committed securities violations, and levied a civil penalty of $300,000. Jarkesy and Patriot28 appealed.

Continue reading.

by Brian Garzione & Kenneth Roberts

08.22.2024

Hawkins Delafield & Wood LLP

Investing in Aging: Senior Living Bonds as a High-Risk, High-Reward Strategy

When investors think about municipal bonds, safety and stability often come to mind. Afterall, a city or state government has the ability to tax their citizens to help pay for the bonds. As a result, munis often form the cornerstone of many conservative fixed-income investor's portfolios. But not all munis are safe and steady, some are a tad on the risky side. But for investors looking to pick up extra yields, these bonds could be a real opportunity.

Today, that opportunity lies within munis tied to senior living and nursing homes.

The senior living sector has long been one of the riskiest in the high-yield muni space — skewing default rates higher for all muni bonds. Those issues have only gotten worse since the pandemic. But with an aging population and increased elderly care needed, the sector could provide an interesting blend of risk and reward for some income seekers.

Continue reading.

dividend.com

by Aaron Levitt

Aug 26, 2024

Active Muni ETFs Are Rapidly Gaining Traction.

In terms of population, the universe of actively managed municipal bond exchange traded funds is growing at a prodigious pace. That makes sense because there are multiple reasons why the combination of municipal bonds and active management can reward investors.

The ALPS Intermediate Municipal Bond ETF (MNBD) is one of the established names in the active muni ETF patch. MNBD, which turned two years old in May, attempts to beat the Bloomberg Municipal Bond 1-15 Year Blend Index. Admittedly, year-to-date isn't the best measuring stick of muni bond ETF performance. That's because this is a long-term asset class. Still, that doesn't diminish the point that MNBD is beating the widely followed ICE AMT-Free US National Municipal Index by a 2-to-1 margin this year.

Advisors know some perks can be accrued when munis meet active management. These include superior flexibility when it comes to managing credit and interest rate risk as well as the ability of active managers to more readily identify valuation opportunities than can muni indexes. Some other points in favor of MNBD should be considered.

MNBD Hidden Advantages

While municipal bonds are a massive corner of the broader fixed income market, some issues with this form of debt make indexing challenging.

"Municipal bonds are a highly illiquid and fragmented market. This makes indexing difficult and creates more opportunities for active managers than more liquid markets. This favorable arena is reflected in assets; 87% of all muni fund assets are in funds where managers choose the bonds rather than mimic and index," notes Morningstar's Gabe Alpert.

That's not to say passive muni ETFs are "bad" products. Instead, municipal bonds' liquidity, or lack thereof, highlights potential advantages with actively managed funds such as MNBD.

Another reason active management makes sense with municipal debt is because these bonds take various forms. This includes general obligation, revenue, and enhancement program bonds, among others. Each subsection of the muni space brings with it opportunities and risks. That can be viewed as further confirmation of the potency of active management. It could also bode well for the long-term adoption of ETFs such as MNBD.

"As demand for ETFs grew, firms launched muni-bond ETFs. Due to the difficulty of launching active ETFs until a regulatory change in 2019, before then, there were only 19 of these funds. Between 2019 and 2024, an average of 7.5 active muni ETFs were listed each year. This is compared with an average of 3.5 index muni ETFs. Flows have followed, with 60% of 2024 flows to muni ETFs going to active funds despite making up only 15% of assets," concludes Alpert.

etftrends.com

by Todd Shriber

August 26, 2024

Profiting From Financings for Charter Schools: SEC Sues Unregistered, Fee-Splitting Municipal Advisor - Norris McLaughlin

The public education system in the United States has experienced a series of fits and starts since the time of the American Revolution. Although many of the Founders (think Adams, Jefferson, and Madison, for example) were staunch advocates for education, believing that a democratic government requires citizens who are not only literate, but who can understand and assess matters confronting a government "by the People," and support intelligent efforts to resolve problems. That said, there was no national consistency in the availability of schooling, with some communities and/or churches (particularly in New England) offering education to America's young people, funded mainly by the families of those attending classes. The U.S. Constitution lacks any provision mandating education, so the question of government sponsorship for schools remains to this day primarily a state law issue. By the 1830s, American states began to address public education, including requiring some minimum years of school attendance paid for by taxes imposed on residents.

Public education was seen as particularly important in aiding the assimilation of successive waves of immigrants from the 1850s and again at the turn of the century, education being especially important for improving the language skills of newcomers. Building on those experiences and the legal acceptance of public unionism for teachers, America's public schools were seen by many as hampered by conventional thinking, especially in a world confronting the risks of thermo-nuclear war and competition with the Soviet Union. The creation of Advanced Placement courses was a response to those perceived threats. Another was the beginning of a movement, once again in New England and led this time by Ray Budde, to create local schools by contract, or charter, among a group of teachers and a municipality. The expectation was that the resulting schools would be more experimental and progressive. This notion of an "innovative institution" harkened back to educational developments in Ireland in the 1700s, sponsored by the Catholic Church, but not just religious schools.

In America the so-called "Charter School Movement" grew slowly until the late 1980s, when the idea was embraced by Albert Shanker, President of the American Federation of Teachers, who saw an opportunity both to expand the scope and style of schools and to create more jobs for teachers. The first charter school law was passed in the typically progressive State of Minnesota in 1991, followed by New Jersey and Delaware in 1995 and Pennsylvania in 1997. According to one national report, as of 2015 there were over 6700 charter schools in America, enrolling almost 3 million students. Charter schools are publicly funded, but operate independently from local school districts. Funding for their operations depends upon the particulars of state law where the school is located; frequently such schools must first obtain some form of licensure from the state (or a state or local education body), and then function pursuant to a contract with that entity. This arrangement allows charter schools to raise funds by issuing municipal securities, much like a public school, although some of the risks of repayment and the scope of disclosure required vary materially from those in regular public school financings.

As depicted in the 2024 case of the *Securities and Exchange Commission v. Choice Advisors, LLC and Matthias O'Meara*, U.S. District Court for the Southern District of California, Case No.3:21 CV-1669-JO-MSB ("*Choice Advisors*"):

> [Two charter schools] retained Defendants to assist them in the process of issuing municipal bonds so that they could raise money to build new school facilities. … As first-

> time issuers of municipal bonds, these schools sought Defendants' help in structuring a deal with a bank underwriter to raise the funds at the lowest cost possible… To facilitate the municipal bond offering the borrower selects a bank underwriter to market and sell the bonds to investors. … The borrower negotiates the terms of the municipal bond offering with the underwriter, which typically involves the school paying a "fee," "spread", or "discount" – usually a percentage of the total value of the bond issued – to its bank underwriter in exchange for the bank purchasing the school's bond and "lending" the school money. … After purchasing the bonds from the school, bank underwriters resell these bonds to third-party investors for a profit. … This financing structure essentially enables the school to "borrow" the money needed for building projects or operations by issuing bonds that the schools ultimately repay with interest.

As explained at length in my Sept. 22, 2020 Blog "SEC Focus on Municipal Securities," the regulation of disclosure in the area of municipal securities is (to use my word) "peculiar." Congress, in an attempt to better deal with some of those "peculiarities," in 1975 amended the Securities Exchange Act of 1934 to create a new body, the Municipal Securities Rulemaking Board ("MSRB"), to strengthen the regulation of the structure of the municipal securities market and of the participants in that market. The MSRB is subject to SEC oversight. Then in 2010, in the Dodd-Frank Wall Street Reform and Consumer Protection Act, Congress expanded the scope of the MSRB to require registration of municipal securities advisors. As the Court said in *Choice Advisors*:

> The municipal advisor's role in …complex financial transactions [like the ones described in *Choice Advisors*] is to act as the school's "skilled representative in the bond offering transaction" and help it negotiate favorable financial terms in the school's best interest.

I wrote about the role of municipal securities advisors in my Sept. 29, 2020 Blog "What if the Advice is Suspect?" In *Choice Advisors*, the Court was presented with a classic case of abuses of that role. In that case, the investigation of these abuses was conducted by a special part of the SEC's Division of Enforcement, the Public Finance Abuse Unit. As I explained in my June 27, 2022 Blog "Serving the Public," the Public Finance Abuse Unit was created in 2010 to provide a more systematic and unified approach to dealing with the increasing incidence of significant neglect of professional obligations and downright fraud in the municipal securities market.

The "bank underwriter" involved in *Choice Advisors* was BB&T, originally named Branch Bank & Trust, founded in 1872 by Alpheus Branch. Over the years, it grew from its North Carolina roots to become, by 2018, a major regional bank with operations all across the country. Two key employees in BB&T's investment banking subsidiary were Matthias O'Meara of Denver, Colorado, and Paula Permenter of Houston, Texas. In 2019, BB&T merged with SunTrust Bank of Florida to form Truist, the 9th largest American bank, with assets of $514 billion. According to the *Choice Advisors* Court, "O'Meara worked as an underwriter at investment bank BB&T" … "[b]efore becoming a municipal advisor for schools and school districts." Because O'Meara was fundamentally a salesman for the underwriting services of BB&T, he "became acquainted with various schools" including future Choice Advisors clients Bella Mente of Vista, California, and Liberty Tree of Colorado Springs, Colorado. Sometime in January or February 2018, "O'Meara and another BB&T employee, Paula Permenter, decided to leave their jobs at BB&T to start" Choice Advisors. On May 1, 2018, O'Meara resigned from BB&T, giving two weeks' notice. Permenter followed suit.

During the two-week notice period, O'Meara negotiated a deal with BB&T concerning Bella Mente and Liberty Tree, as well as three other California schools identified by O'Meara (so long as the

schools selected BB&T as their respective underwriter). The deal was to split the 2% underwriter fee with BB&T: BB&T to get ¾ of the fee, and O'Meara's firm to be formed, Choice Advisors, LLC, to get ¼ of the fee. For example, the $20 fee on a $1 million bond would be divided $15 to BB&T, and $5 to Choice. Choice Advisors, LLC, registered with the SEC as an investment advisor on Aug. 27, 2018,and registered with the MSRB as a municipal securities advisor on Oct. 16, 2018. On May 8, 2018, O'Meara sent Bella Mente an engagement letter to serve as its municipal securities advisor. However, the letter failed to disclose to the school that i) he was still employed by BB&T; and ii) the fee splitting agreement, including the fact that it might pose a conflict of interest for Choice. Similarly, on May 14, 2018, O'Meara's second to last day with BB&T, he sent a parallel engagement letter to Liberty Tree. Both letters stated that:

> [There existed] no known actual or potential material conflicts that might impair [Choice's] ability to render unbiased or competent advice or fulfill its fiduciary duty… And there are "no Other Engagements or Relationships Impairing [Choice's] Ability to Provide Advice.

In addition, the Defendants **completed** the two bond offerings "on the schools' behalf" and received payment for their services **before** they were registered. Choice was paid $157,000 by Bella Mente (on July 11, 2018) and $53, 437.50 by Liberty Tree (on Sept. 21, 2018). Given these facts, the SEC sued Choice on the following grounds:

1. Performing municipal advisory service without being registered;
2. Agreeing to split fees with BB&T;
3. "Deceptively operating in a dual capacity" as both a BB&T underwriter and a municipal securities advisor; and
4. Failing to disclose material conflicts of interest.

It should be emphasized that the two principals of Choice were experienced participants in financial transactions, including the municipal securities market. O'Meara earned a B.A. in finance from the University of Notre Dame and holds a Series 50 municipal advisor license. Permenter, with her B.A.A. from the University of Houston and M.B.A. from the University of St. Thomas, worked for over 20 years in finance, holding a Series 7,66, 79 and 53 before starting Choice, where she, like O'Meara, holds a Series 50 license. Yet they acted as though either asleep or engaged in fraudulent concealment. It is no wonder that the SEC charged them and Choice with breaching their fiduciary duties to the schools and entering illegal arrangements without even being appropriately registered. Most particularly, the SEC charged the Defendants with violating MSRB Rule G-42, and to the extent they dealt unfairly with their clients and engaged in deceptive practices, violating Rule G-17.

The Court, in an April 22, 2024 decision in *Choice Advisors*, granted Summary Judgment to the SEC for failing to timely register with the SEC and with the MSRB, which in turn was the basis for granting Summary Judgment for committing acts in violation of MSRB Rules. Defendants argued that fee splitting was not prohibited because the terms were agreed to before payment, so the 25% payable to Choice was paid directly and not "split" after receipt by BB&T. The Court, however, granted Summary Judgment against the Defendants on this count, as well as for breach of fiduciary duty, including failure to disclose potential conflicts of interest and the lack of required registration. The Court did not grant Summary Judgment concerning the alleged concealment of the dual employment and fee splitting only because Defendants claimed the schools knew of the Choice arrangements, but reserved for further proceedings on this issue. Finally, Summary Judgment was granted against the Defendants for engaging in "Deceptive, Dishonest, or Unfair Practices" in violation of MSRB Rule G-17.

The Court set Aug. 7, 2024, for the SEC to submit its proposal for the Court order imposing sanctions on Defendants, whose objections were due Aug. 16. Were the two Charter Schools injured by Choice? One cannot be certain, but the appearances suggest that Choice and its principals were in this only for personal profit, and not with any concern about the educational exigencies that make Charter Schools an attractive alternative for parents concerned about the quality of education for their children.

by: Peter D. Hutcheon of Norris McLaughlin P.A. – Business Law Blog

Monday, August 26, 2024

Proposed Rule Change Consisting of Amendments to MSRB Rule G-14 and to Amend FINRA Rule 6730: SIFMA Comment Letter

Summary

SIFMA and SIFMA AMG provided comments to the U.S. Securities and Exchange Commission (SEC) and reiterated comments made in their previous letters, the Commission, FINRA, and the MSRB should reconsider if a one-minute trade reporting requirement is appropriate for fixed-income markets in the first place. If a decision is made to proceed with this proposal, then FINRA and the MSRB should allow for an appropriate implementation period (e.g., two years) and:

- Include a broad exception for manual trades;
- Examine impacts to liquidity, depth, concentration, and transparency prior to decreasing reporting times to shorter intervals to ensure markets are not harmed;
- Provide relief for certain electronic trades where system processing limitations prevent ne-minute reporting, including post-trade allocations; and
- Implement the proposed de minimis exception.

Read the SIFMA Comment Letter.

Copyright © 2025 Bond Case Briefs | bondcasebriefs.com