NATIONAL ASSOCIATION OF BOND LAWYERS

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SEC and FINRA Enforcement

Chair:

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Panelists:

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I. Background

a. The SEC Division of Enforcement and the Enforcement of Municipal Securities

i. Congress charged the U.S. Securities and Exchange Commission (the "SEC" or the "Commission") with civil enforcement of the federal securities laws. The purpose of the SEC is to "protect investors—including investors in municipal securities—maintain fair, orderly and efficient markets, and facilitate capital formation." *U.S. Securities and Exchange Commission, Report on the Municipal Securities Market*, at i (July 31, 2012), *available at* www.sec.gov/news/studies/2012/munireport073112.pdf (the "2012 Report").

ii. Historically, the municipal securities market has been largely exempt from regulation by the Commission. "The Securities Act of 1933 ("Securities Act") and the Securities Exchange Act of 1934 ("Exchange Act") were both enacted with broad exemptions for municipal securities from all of their provisions except for the antifraud provisions of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 promulgated thereunder." *See* 2012 Report, at 27. Pursuant to amendments adopted in 1975 (the "1975 Amendments"), Congress enacted a limited regulatory scheme for the municipal securities market by requiring firms transacting business in municipal securities and banks to register with the SEC as broker-dealers and municipal securities dealers, respectively. The 1975 Amendments also created the Municipal Securities Rulemaking Board (the "MSRB"), a self-regulatory organization subject to SEC oversight that is authorized, as expanded by the Dodd-Frank Act, to adopt rules regulating the sale of municipal securities. While the SEC's Office of Municipal Securities had functioned independently previously, it later was incorporated into

the Division of Trading and Markets. The Dodd-Frank Act required that the Office of Municipal Securities be restored to independent status. The Office of Municipal Securities coordinates the SEC's activities relating to the municipal securities, including three primary areas: municipal advisor regulation, municipal securities market structure initiatives and municipal securities disclosure initiatives.

iii. The Tower Amendment: The 1975 Amendments did not give the SEC the authority to directly regulate municipal securities issuers and certain provisions of the 1975 Amendments (the "Tower Amendment") prohibit the SEC and the MSRB from directly or indirectly requiring municipal issuers to file documents with them or register prior to the sale of their securities. As a result, the SEC has largely relied on its express authority to regulate broker-dealers and municipal securities dealers, its oversight of the MSRB, and its enforcement authority under the antifraud provisions of the Securities Act and the Exchange Act as its regulatory tools.

iv. The Public Finance Abuse Unit: In 2010, the Commission created a specialized Enforcement unit to address abuses in public finance. The Public Finance Abuse Unit is staffed "with experienced attorneys and … non-attorney specialists with real world experience in the public finance industry" who partner with the Commission's Office of Municipal Securities. Andrew Ceresney, Director of Enforcement, *The Impact of SEC Enforcement on Public Finance* (Oct. 13, 2016), *available at* https://www.sec.gov/news/speech/speech-ceresney-10132016.html.

The recent change in administrations has not altered the SEC's primary enforcement priorities. "The core organizing principle is that we want to pursue, and we prioritize, cases where there is a clear risk of investor harm," said LeeAnn Gaunt, Chief of the SEC's Public Finance Abuse Unit. "We also consider it a key part of our mission to protect issuers, particularly small, infrequent issuers, from abusive practices by municipal advisors and broker-dealers." See *Outlook 2021: SEC To Focus On Price Transparency, Muni Advisors And Disclosure Enforcement*, The Bond Buyer, January 4, 2021.

v. In February 2020, the staff of the Office of Municipal Securities issued Legal Bulletin No. 21 ("Bulletin 21") regarding the application of the antifraud provisions of Section 10(b) and Rule 10b-5 to public statements made by issuers of municipal securities. Bulletin 21 provides that the "antifraud provisions apply to the purchase and sale of municipal securities in the secondary market, including to statements made by municipal issuers that are reasonably expected to reach investors and trading markets." Rule 10b-5, in part, "prohibits, in connection with the purchase or sale of any security, the making of any untrue statement of fact or omitting to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading."

Bulletin 21 acknowledges that municipal issuers do not have the option of remaining silent and notes that municipal issuers disclose information about themselves in a variety of ways, including "public announcements, press

releases, interviews with media representatives, and discussions with groups whose members have a particular interest in their affairs." Noting that the "access to 'current and reliable information is uneven and inefficient' in the municipal securities market," the SEC staff believes these types of statements are "'a principal source of significant, current information about the issuer of the security, and thus reasonably can be expected to reach investors and the trading markets.'" Considering this information a compliment to the formal disclosures under the Exchange Act, the SEC staff goes on to note in Bulletin 21 that "[t]he fact that they are not published for purposes of informing the securities markets does not alter the mandate that they not violate the antifraud provisions."https://www.sec.gov/municipal/application-antifraud-provisions-staff-legal-bulletin-21

b. SEC Recent Enforcement Activity

i. Since the 2012 Report, there have been a number of significant municipal enforcement actions. Some examples include:

1. Financial Penalties for Municipal Issuers and Individuals: In 2019, the SEC brought an enforcement action against Montebello Unified School District ("MUSD"), its former Chief Business Officer (Ruben Rojas) and its Superintendent of Schools (Anthony Martinez) for defrauding investors by failing to disclose fraud and internal controls concerns raised by MUSD's independent auditor. According to the SEC's complaint and order, MUSD's independent auditor repeatedly raised concerns about allegations of fraud and internal controls issues to MUSD's Board of Education and management. In response, MUSD allegedly refused to authorize the fees needed for the audit firm to complete its audit and instead decided to terminate the audit firm. The offering documents for MUSD's $100 million of general obligation bonds in December 2016 failed to disclose this information to investors and instead included a copy of the District's audit report from the prior fiscal year, which included an unmodified or "clean" audit opinion from the firm.

   The SEC's complaint charged Rojas with violating the antifraud provisions of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder as well as Section 17(a) of the Securities Act, and seeks permanent and conduct-based injunctions as well as a financial penalty. MUSD was ordered to cease and desist from future violations of the antifraud provisions of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder as well as Section 17(a) of the Securities Act. It also agreed to engage an independent consultant to evaluate its policies and procedures related to its municipal securities disclosures. Martinez was ordered to cease and desist from future violations of Section 17(a)(3) of the Securities Act and also ordered to pay a $10,000 penalty. See *SEC Charges Los Angeles County School District and Two Officials with Defrauding Investors in $100 Million Bond Offering*, SEC Litigation Release No. 24602 (September 19, 2019).

See also: In the Matter of The Greater Wenatchee Regional Events Center Public Facilities District, Allison Williams, Global Entertainment Corporation, and Richard Kozuback, Sec. Act. Release No. 9471 (Nov. 5, 2013) (imposing a $20,000 penalty on the district, $10,000 on the developer and $10,000 on the president of the developer); In the Matter of Westlands Water District, Thomas W. Birmingham, and Louie David Ciapponi, Sec. Act. Release No. 10053 (Mar. 9, 2016) (imposing $125,000 penalty on water district, $50,000 on general manager, and $20,000 on assistant general manager); *SEC Obtains Final Judgments Against Gary Burtka and Eric Waidelich*, Litig. Rel. No. 23229 (Apr. 6, 2015) (imposing $10,000 penalty on former city mayor); In the Matter of the Port Authority of New York and New Jersey, Sec. Act. Release No. 10278 (January 10, 2017) (imposing $400,000 penalty on the Port Authority of New York and New Jersey); In the Matter of O'Connor & Company Securities, Inc. and Anthony Wetherbee, Sec. Act Release No. 81462 (August 23, 2017) and *Former Executive Director of Muni Bond Issuer Charged with Disclosure Failures*, Litig. Release No. 23920 (August 24, 2017) (imposing $15,000 penalty on the underwriter and $37,500 on city manager).

In 2022, the SEC charged the City of Rochester, New York, its former finance director Rosiland Brooks-Harris, and former Rochester City School District CFO Everton Sewell with misleading investors in a $119 million bond offering. The SEC alleges that in 2019 the defendants misled investors with bond offering documents that included outdated financial statements for the Rochester City School District and did not indicate that the district was experiencing financial distress due to overspending on teacher salaries. Sewell was allegedly aware that the district was facing at least a $25 million budget shortfall, but he misled a credit rating agency regarding the magnitude of the expected shortfall. The SEC's complaint against Brooks-Harris filed in the U.S. District Court for the Western District of New York, charges him with violating the antifraud provisions of the securities laws. The complaint also charges others with violating the municipal advisor fiduciary duty, deceptive practices, and fair dealing provisions of the federal securities laws. The Commission sought injunctive relief and financial remedies against all parties. Sewell agreed to settle the SEC's charges by consenting, without admitting or denying any findings, to a court order prohibiting him from future violations of the antifraud provisions and from participating in future municipal securities offerings, and to pay a $25,000 penalty. See SEC Press Release 2022-108 (June 14, 2022).

In 2022, the SEC charged Crosby Independent School District (Crosby ISD) and its former Chief Financial Officer, Carla Merka, with misleading investors in the sale of $20 million of municipal bonds in order to pay its outstanding construction liabilities and fund new capital projects. The SEC also charged Crosby ISD's auditor, Shelby Lackey, with improper professional conduct in connection with the audit of the school district's 2017 fiscal year financial statements. Crosby ISD agreed to settle the SEC's

charges by consenting, without admitting or denying any findings, to the entry of an order finding that it violated the antifraud provisions. The SEC's complaint against Merka, filed in U.S. District Court for the Southern District of Texas, charged her with violating the antifraud provisions of the securities laws. Without admitting or denying the allegations in the complaint, Merka agreed to pay a $30,000 penalty and not participate in any future municipal securities offerings.

2. Focus on Charter Schools. *SEC Charges Two California Charter School Officials with Misleading Investors in Bond Offering*, Litig. Release No. 24806 (April 27, 2020). In April 2020, the SEC charged William Alfred Batchelor and John Michael Zukoski with misleading investors in a $25.4 million bond offering for Tri-Valley Learning Corporation. Batchelor, then CEO, and Zukoski, then Director of Finance, were charged with signing offering documents and related certifications despite knowing that the Tri-Valley Learning Corporation was in "serious financial distress," and that the offering contained misleading financial projections. Batchelor and Zukoski agreed to be enjoined from future violations of Section 17(a)(3) of the Securities Act and from participating in future municipal debt offerings. Batchelor agreed to pay a $20,000 penalty and Zukoski agreed to pay a $15,000 penalty.

   Similarly, in September 2020 the SEC charged Park View School, Inc. based in Arizona and its former President, Debra Kay Slagle, with misleading investors in an April 2016 $7.6 million municipal bond offering. According to the SEC's complaint, in the years and months leading up to the bond offering, Park View experienced significant operating losses and repeatedly made unauthorized withdrawals from two reserve accounts to cover routine operating expenses, to pay other debts, and to transfer money to affiliated entities. Park View allegedly provided investors an offering document that included misleading statements about profit and expense projections and showed that Park View would be profitable in the upcoming fiscal year and able to repay the bondholders. Park View defaulted one year later by reducing the interest payments that it made on the bonds. Without admitting or denying the allegations in the complaint, Slagle and Park View agreed to settle with the SEC and to be enjoined from future violations of Section l0(b) of the Exchange Act, Rule 10b-5 thereunder, Sections 17(a)(l) and (3) of the Securities Act (and, in the case of Park View only, Section 17(a)(2) of the Securities Act). Slagle further agreed to pay a $30,000 penalty and to be enjoined from participating in future municipal securities offerings. See SEC Press Release 2020-208 (September 14, 2020).

3. Court Order to Halt Bond Offering: *City of Harvey Agrees to Settle Charges Stemming from Fraudulent Bond Offering Scheme*, Litig. Release No. 23149 (December 5, 2014). On June 25, 2014, the SEC obtained an emergency court order in the U.S. District Court for the Northern District of Illinois against the City of Harvey and its comptroller, Joseph T. Letke, to stop a fraudulent bond

offering that the city had been marketing to potential investors. The SEC had been investigating the City of Harvey and its comptroller for improperly using proceeds from prior bond offerings. While investigating, the SEC learned that the city intended to issue new limited obligation bonds; the SEC alleged that the offering documents made materially misleading statements about the purpose and risks of those bonds, while omitting that past bond proceeds had been misused.

The city agreed to a final judgment that enjoined it from committing future violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. In addition, the city was prohibited from engaging in the offer or sale of any municipal securities for three years unless it retained independent disclosure counsel. The court issued a permanent injunction prohibiting Letke from participating in any municipal securities offerings. Letke was further ordered to disgorge a total of $217,115.23, including interest and penalty.

4. Bars: In 2016, the SEC settled with Juan Rangel, the former President of UNO Charter School Network Inc. and former CEO of United Neighborhood Organization of Chicago ("UNO"), for materially misleading investors by failing to disclose terms of certain outstanding obligations in its offering documents, including certain conflicts of interest. Rangel agreed to pay a $10,000 fine, to be permanently enjoined from future violations of Section 17(a)(2) of the Securities Act and to be barred from participating in any future municipal bond offering (other than for his personal account). See SEC Press Release 2016-125 (June 21, 2016), *available at* www.sec.gov/news/pressrelease/2016-125.html.

5. Criminal Charges: In 2016 the SEC brought fraud charges against the Town of Ramapo, New York, the town's local development corporation, and town officials for failing to adequately disclose the town's failing financial condition. The U.S. Department of Justice (the "DOJ") also brought criminal charges against Christopher St. Lawrence, the town supervisor, and Aaron Troodler, the assistant town attorney and executive director of the local development corporation, consisting of 22 counts of securities fraud, wire fraud, and conspiracy—the first criminal securities fraud case brought against city officials for accounting fraud in connection with the sale of municipal bonds. Troodler pled guilty in March 2017 and was ordered to pay a $20,000 fine and a special assessment of $200, and was sentenced to three years of probation. Troodler was also disbarred as a result of his felony conviction. St. Lawrence was found guilty by jurors in May 2017 of securities fraud, wire fraud, and conspiracy. In November 2017 the U.S. District Court for the Southern District of New York permanently enjoined the Town and the local development corporation from violating the antifraud provisions and ordered them to retain independent consultants to review and recommend improvements to financial reporting procedures and controls and disclosure

practices and to adopt such recommendations, to retain independent auditing firms, and for a period of three years, to retain separate disclosure counsel (unaffiliated with bond counsel) prior to proceeding with the offering or sale of municipal securities. In December 2017, St. Lawrence was sentenced to 2 ½ years in prison. In addition to the prison term, St. Lawrence was sentenced to three years of supervised release and a $2,000 special assessment.

See DOJ Press Release No. 17-394 (December 13, 2017), *available at* https://www.justice.gov/usao-sdny/pr/former-ramapo-town-supervisor-christopher-st-lawrence-sentenced-30-months-prison.

In 2022, the SEC charged former City of Johnson City, Texas chief administrative officer and city secretary, Anthony Michael Holland, with securities fraud for creating and causing to be distributed falsified financial statements and a falsified audit report for the city's 2016 fiscal year. According to the SEC's complaint, Holland created the falsified documents to prevent discovery on his ongoing embezzlement of funds. The complaint alleges that, between 2015 and 2020, Holland stole approximately $1 million from the city, including $107,137 during the 2016 fiscal year. The complaint further alleges that, to hide his theft, Holland initially delayed the annual independent audit of the city's 2016 financial statements, and then, in approximately August 2018, falsified the 2016 documents by changing dates on the 2015 financial statements and audit report. According to the complaint, Holland then provided the falsified documents to the city's mayor and municipal advisor, knowing that the material would be posted to the city's public website and the Municipal Securities Rulemaking Board's Electronic Municipal Market Access (EMMA) system and made available to investors. During the time the falsified documents were available to investors on EMMA, investors engaged in secondary trading in the city's outstanding municipal bonds. Holland was also criminally charged by the United States Attorney's Office for the Western District of Texas and pled guilty to one count of Theft from a State or Local Government and admitted to stealing over $1 million from the city for his personal benefit. See *SEC Charges Former Texas City Official for Falsifying City's Financial Documents*, Litig. Release No. 25426 (June 16, 2022).

6. Unregistered Municipal Advisors: In September 2020, the SEC charged Funding the Gap, LLC, and its principal, Irene P. Carroll, with failing to register as Municipal Advisors. The SEC's order found that from at least July 2014 through September 2019, FTG and Carroll provided municipal advice to twelve charter schools located throughout the country in connection with the issuance of municipal bonds, including advising the schools regarding financing structures, interest rates, and underwriter selection. In total, the charter schools, advised by FTG and Carroll, borrowed, through conduit issuers, $222 million through municipal bond offerings. The order found that while FTG and Carroll provided and FTG was paid for municipal advisory services, neither was registered as a municipal advisor. The SEC's order

found that FTG violated the registration provisions of Section 15B(a)(1)(B) of the Exchange Act and that Carroll caused the violation. Without admitting or denying the findings in the order, FTG and Carroll agreed to cease-and-desist orders and to pay, jointly and severally, a civil penalty of $30,000. See *SEC Charges Charter School Municipal Advisor with Failing to Register with the Commission,* Admin. Proceeding File No. 3-20072 (September 25, 2020).

In 2022, the SEC charged an unregistered municipal advisor, Twin Spires Financial LLC, and its owner, Aaron B. Fletcher, with misleading investors in the sale of $5.8 million in municipal bonds across two offerings in 2017 and 2018. The SEC further alleges that Twin Spires and Fletcher provided municipal advisory services to the town of Sterlington, Louisiana without Twin Spires being registered as a municipal advisor with the Commission. The U.S. District Court for the Western District of Louisiana entered final judgment against Fletcher and Twin Spires and ordered them to pay, on a joint and several basis: (a) disgorgement of $26,303 and prejudgment interest of $6,642.88; and (2) a $200,000 civil penalty. See *SEC Obtains Final Judgment Against Municipal Advisor and Its Owner in Municipal Bond Offering Schemes*, Litig. Release No. 25511 (September 19, 2022).

In 2022, the SEC settled charges against Legacy Funding Services, LLC ("Legacy Funding"), and Raymond Howard Sowell, its sole owner, managing member and president, both of Raleigh, North Carolina, in connection with unregistered municipal advisory activity and unregistered broker services by Legacy Funding. settled charges against Legacy Funding Services, LLC ("Legacy Funding"), and its sole owner, managing member and president, Raymond Howard Sowell, both of Raleigh, North Carolina, in connection with unregistered municipal advisory activity and unregistered broker services by Legacy Funding.

The SEC's order finds that from 2017 through 2019, Legacy Funding, through Sowell, provided municipal advisory and broker services in connection with four municipal bond issuances for the benefit of three public charter schools. These services included providing advice to the charter schools on the structure, timing and terms of the issuances and identifying, soliciting and negotiating with investors to purchase the bonds, and receiving transaction-based compensation. Neither Legacy Funding nor Sowell were registered with the Commission in any capacity when they provided these services. The SEC's order finds that Legacy Funding willfully violated the registration provisions of Sections 15B(a)(1)(B) and 15(a)(1) of the Securities Exchange Act of 1934 and that Sowell caused Legacy Funding's violations. Without admitting or denying the findings in the order, Legacy Funding agreed to be censured and Legacy Funding and Sowell agreed to cease-and-desist orders and to pay, jointly and severally, a civil penalty of $60,000. See *SEC Charges Municipal Advisor and Broker to Charter Schools With Failing to Register With The Commission,* Administrative Proceeding File No. 3-21059.

In 2022, the SEC charged Chicago-based Loop Capital Markets, LLC for providing advice to a municipal entity without registering as a municipal advisor. The action marks the first time the SEC has charged a broker-dealer for violating the municipal advisor registration rule. According to the SEC's order, between September 2017 and February 2019, Loop Capital advised a Midwestern city to purchase particular fixed income securities, which the city purchased using the proceeds of its own municipal bond issuances. In addition, the SEC's order found that Loop Capital did not maintain a system reasonably designed to supervise its municipal securities activities and had inadequate procedures, including insufficient methods to identify potential violations of the municipal advisor registration rules. Loop Capital agreed to settle with the SEC and consented, without admitting or denying any findings, to the entry of an SEC order finding that it violated the rules regarding municipal advisor registration and supervision requirements, censuring it, and ordering it to pay disgorgement and prejudgment interest of $5,456.73 and a civil penalty of $100,000. See SEC Press Release No. 2022-163 (September 14, 2022).

7. Actions Against Municipal Advisors: See In the Matter of Clear Scope Advisors, Inc., Exchange Act Release No. 85618 (April 11, 2019) (advisor did not meet professional qualification standards and was censured and required to pay disgorgement of $20,000 and a penalty of $5,000). See also SEC Charges Municipal Advisor with Breaching Fiduciary Duty, SEC Litigation Release No. 24520 (June 27, 2019). The SEC complaint charged the municipal advisor and its principal with breaching its fiduciary duty and failure to protect the interests of their client in connection with a $6 million municipal bond offering by the Harvey Public Library District in Harvey, Illinois. According to the SEC's complaint, the mispricing of the bonds will cause the Library District to pay more than $500,000 in additional interest over the life of the bonds. The complaint charged the defendants with breaching their fiduciary duties in violation of Section 15B(c)(1) of the Exchange Act. The SEC sought permanent injunctions, disgorgement plus prejudgment interest, and civil penalties.

   In 2022, the SEC also charged the City of Rochester's municipal advisor Capital Markets Advisors, LLC (CMA) and its principal Richard Ganci with misleading investors and breaching their fiduciary duty to the city and the Rochester City School District. CMA, Ganci and CMA co-principal Richard Tortora were also charged with failing to disclose conflicts to municipal clients. The SEC alleges that Ganci was also aware of the Rochester City School District's increased financial distress, including overspending on teacher salaries, yet he made no effort to inquire further about the district's financial condition prior to the bond offering, nor did he inform investors of the risks that the overspending posed to the district's finances. In September 2019, 42 days after the offering, the district's auditors revealed that the district had overspent its budget by nearly $30 million, resulting in a downgrade of the city's debt rating and requiring the intervention of the State of New York.

The SEC's complaint also alleges that CMA and Ganci failed to disclose to nearly 200 municipal clients that CMA had material conflicts of interest arising from its compensation arrangements. In many cases, CMA, Ganci and Tortora falsely stated that CMA had no undisclosed material conflicts of interest. See SEC Press Release 2022-108 (June 14, 2022).

In 2021, the SEC charged a Texas- and Colorado-based municipal advisor, Choice Advisors LLC, and its two principals, Matthias O'Meara and Paula Permenter, with violating their duties, engaging in unregistered municipal advisory activities, and related misconduct with respect to Choice's charter school clients. The actions were the first-ever SEC cases enforcing Municipal Securities Rulemaking Board Rule G-42 on the duties of non-solicitor municipal advisors. Permenter, who agreed to settle with the SEC, consented, without admitting or denying any findings, to the entry of an SEC order finding that she violated rules regarding municipal advisor registration and the duties of non-solicitor municipal advisors, censuring her, ordering her to pay a $26,000 penalty, and requiring that she participate in training on the duties of non-solicitor municipal advisors as well as have her engagement letters reviewed by a third party for a period of one year. See SEC Press Release 2021-188 (September 21, 2021).

8. Municipal Continuing Disclosure Cooperation Initiative ("MCDC Initiative"): Under the MCDC Initiative, announced in 2014, municipal issuers, obligated parties and underwriters had the opportunity to self-report inaccurate statements in final official statements about their prior compliance with the continuing disclosure obligations specified in Rule 15c2-12. In exchange for self-reporting, the Public Finance Abuse Unit agreed to recommend standardized, favorable settlement terms. The settlements were achieved through administrative proceedings in which each respondent (1) neither admitted nor denied the SEC's findings, (2) was censured, (3) was ordered to cease-and-desist from future violations, and (4) was ordered to enhance its continuing disclosure compliance.

   In three waves of settlements from June 2015 to February 2016, the SEC entered into settlements with 72 underwriting firms under the MCDC Initiative. In 2016 the SEC announced that it had entered into settlements with 71 issuers and obligated parties.

   Following the announcement of the MCDC settlements, the SEC began to investigate issuers and underwriters that did not participate in the initiative. For example, in August 2017 the SEC charged the Beaumont California Financing Authority for failing to accurately disclose in its bond disclosure documents its failure to materially comply with its prior continuing disclosure obligations. The financing authority, its former executive director, the underwriting firm (O'Connor & Company Securities Inc.), and the lead individual underwriter each agreed to settle the charges. Among other settlement terms, the financing authority's former executive director agreed

to pay $37,500 and to be barred from participating in future bond offerings, the underwriting firm agreed to pay $150,000, and the lead individual underwriter agreed to pay $15,000 and be subject to a six-month suspension. The SEC noted that the parties "would have been eligible for more lenient remedies had they self-reported during the MCDC Initiative." See SEC Press Release 2017-148 (August 23, 2017), *available at* www.sec.gov/news/press-release/2017-148.

9. Limited Offering Exemption in Rule 15c2-12 and Violations Against Underwriters: In 2022, the SEC filed a litigated action against Oppenheimer & Co. Inc. and separately announced settlements with BNY Mellon Capital Markets LLC, TD Securities (USA) LLC, and Jefferies LLC, charging each of the four firms with failing to comply with municipal bond offering disclosure requirements. These are the first SEC actions addressing underwriters who fail to meet the legal requirements that would exempt them from obtaining disclosures for investors in certain offerings of municipal bonds. According to the SEC's complaint and the settled orders, during different periods since 2017, the four firms sold new issue municipal bonds without obtaining required disclosures for investors. Each of the firms purported to rely on an exemption to the typical disclosure requirements called the limited offering exemption, but they did not take the steps necessary to satisfy the exemption's criteria. The SEC's orders find that BNY, TD, and Jefferies each violated Rule 15c2-12 under the Securities Exchange Act of 1934, which establishes disclosures that must be provided to investors, as well as Municipal Securities Rulemaking Board (MSRB) Rule G-27 relating to supervision and Section 15B(c)(1) of the Exchange Act. Without admitting or denying the SEC's findings, these three firms agreed to settle the charges, cease and desist from future violations of those provisions, be censured, and pay the following monetary relief: (i) BNY: $656,833.56 in disgorgement plus prejudgment interest and a $300,000 penalty; (ii) TD: $52,955.92 in disgorgement plus prejudgment interest and a $100,000 penalty; and (iii) Jefferies: $43,215.22 in disgorgement plus prejudgment interest and a $100,000 penalty. The SEC's complaint against Oppenheimer, filed in federal district court in Manhattan, charges the same violations as above in connection with at least 354 offerings. The complaint also alleges that Oppenheimer made deceptive statements to issuers in violation of MSRB Rule G-17, which prohibits deceptive, dishonest, or unfair practices. The complaint seeks permanent injunctions, disgorgement plus prejudgment interest, and a civil money penalty.

In addition, in late 2022, the SEC announced that PNC Capital Markets LLC has agreed to settle charges that it failed to comply with municipal bond offering disclosure requirements under Rule 15c2-12 of the Securities Exchange Act of 1934. According to the order, between March 2018 and November 2021, PNC sold new issue municipal bonds without obtaining required disclosures for investors in 36 municipal bond offerings. PNC purported to rely on an exemption to the typical disclosure requirements

called the limited offering exemption, but it did not take the steps necessary to satisfy the exemption's criteria. The order also found that PNC failed to enforce its own policies and procedures for disclosures in limited offerings. The order finds that PNC willfully violated Section 15B(c)(1) of the Exchange Act, Rule 15c2-12 under the Exchange Act, as well as Rule G-27 of the Municipal Securities Rulemaking Board. Without admitting or denying the SEC's findings, PNC agreed to settle the charges, cease-and-desist from future violations of those provisions, be censured, and pay $81,362 in disgorgement plus prejudgment interest of $16,961, and a $100,000 civil money penalty. In March 2023, the SEC also agreed to settle similar charges with Keybanc Capital Markets Inc. As a result of its findings in these investigations, the SEC staff has begun investigations of other firms' reliance on the limited offering exemption.

c. FINRA Division of Enforcement and the Enforcement of Municipal Securities

i. FINRA is a self-regulatory organization that oversees more than 4,400 securities firms and nearly 630,000 registered securities representatives in the United States. FINRA's responsibilities include, among others: regulating broker-dealers and their registered persons; providing market information; adopting and enforcing rules to protect investors and the financial markets; examining broker-dealers for compliance with FINRA rules as well as federal securities laws, including the rules and regulations thereunder, and MSRB rules; informing and educating the investing public; providing industry utilities; and administering the largest dispute resolution forum for investors and registered firms.

ii. While its responsibilities extend well beyond the municipal securities market, FINRA plays an instrumental role in overseeing the registration and examination process for municipal dealer professionals and encouraging, examining, and enforcing compliance with MSRB rules by nonbank municipal dealers. However, FINRA's rules explicitly do not apply to transactions in and business activities relating to municipal securities because transactions in municipal securities effected by municipal bond dealers, and municipal advisory activities engaged in by municipal advisors, are subject to the rules of the MSRB.

iii. MSRB-registered broker-dealers are members of and examined by FINRA, with the remaining dealers registered with the SEC as municipal securities dealers and examined primarily by the various federal bank regulators. The SEC approved a change to MSRB Rule G-16 (Periodic Compliance Examination) to provide for risk-based examinations for FINRA member brokers and dealers. In addition to examinations, FINRA surveils the marketplace with respect to the pricing of bond transactions and markups.

iv. FINRA has conducted sweeps and targeted exams in the area of municipal sales practices; issued guidance reminding firms of their sales practice and due diligence obligations when selling municipal securities in the secondary market;

and conducted an informal look at new-issue retail order periods to address concerns about the potential for "flipping" municipal bonds.

II. Control Person Liability

a. Control Person Liability

i. Section 20(a) of the Exchange Act provides that "every person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable . . . unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action."

b. SEC Enforcement Actions Involving Control Person Liability

i. In 2014, the SEC brought an enforcement action against the City of Allen Park, Michigan and two former city officials (Gary Burtka and Eric Waidelich) in connection with municipal securities offered to finance a movie studio project in the city. The action against the former mayor (Burtka) was brought under Section 20(a) of the Exchange Act as a "control person" for the city. According to the complaint, the offering documents contained false and misleading statements about the scope and viability of the project, as well as the city's overall financial condition, and the mayor was an "active champion of the project and in a position to control the actions of the city" with respect to the fraudulent bond issuances. Accordingly, the SEC held the former mayor jointly and severally liable with the city and the city administrator and enjoined all parties from future violations of the charged securities laws. In addition, both Waidelich and Burtka were barred from participating in future bond offerings and Burtka paid a $10,000 penalty. See SEC Press Release 2014-249 (November 6, 2014).

ii. In 2018, the SEC charged Leonard Genova ("Genova"), the former town attorney and deputy supervisor of Oyster Bay, New York, with defrauding investors in the town's municipal securities offering by allegedly hiding the existence and potential financial impact of side deals with a businessman who owned and operated restaurants and concessions stands at several of the town's facilities. The SEC alleged that Oyster Bay agreed to indirectly guarantee four separate private loans to the vendor totaling more than $20 million. The SEC further alleged that Genova concealed the indirect loan guarantees when they should have been disclosed in connection with dozens of securities offerings. The SEC charged Genova with violations of Sections 17(a)(1) and (a)(3) of the Securities Act and Sections 10(b) of the Exchange Act. In addition, Genova was charged with aiding and abetting violations and as a control person under Section 20(a) of the Exchange Act. See *Former Oyster Bay Town Attorney Agrees to Settle SEC Charges*, SEC Litigation Release No. 24059 (March 1, 2018).

c. Risk of Disclosure Violations and Control Personal Liability Outside of Offering Materials

i. As noted above, Legal Bulletin 21 provides that the "antifraud provisions apply to the purchase and sale of municipal securities in the secondary market, including to statements made by municipal issuers that are reasonably expected to reach investors and trading markets." Bulletin 21 clarifies that public officials may have liability for misstatements and fraudulent omission in public speeches and comments. In addition and as discussed above, officials may also have "control person" liability for fraudulent statements or omissions.

ii. State of the City and Public Speeches

1. In May 2013, the SEC determined that misleading statements were made in the City of Harrisburg's budget report, annual and mid-year financial statements, and a State of the City address. This was the first time that the SEC charged a municipality for misleading statements made outside of its securities disclosure documents. See SEC Press Release 2013-82 (May 6, 2013).

iii. City websites are expressly discussed in Legal Bulletin 21. Website content should be reviewed for purposes of consistency and accuracy of disclosures related to municipal securities.

iv. Public meetings can also be a source of disclosure violations if officials make misstatements.

d. Good Faith Defense

i. Section 20(a) of the Exchange Act provides for a defense where the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.

III. ESG, Cybersecurity and Real Time Disclosure Decisions

a. The SEC launched the Climate and ESG Task Force within the Division of Enforcement to develop initiatives to proactively identify ESG-related misconduct consistent with increased investor reliance on climate and ESG-related disclosure and investment.

b. Types of ESG-related enforcement actions filed to-date, include actions against investment advisers, public companies, and a clean water project founder, among others.

c. On July 26, 2023, the SEC adopted a final rule requiring the disclosure of material cybersecurity incidents by public companies pursuant to new item 1.05 of Form 8-K and cybersecurity risk management, strategy, and governance by public companies pursuant to new item 106 of Regulation S-K disclosures.

d. Apart from the mandates of Rule 15c2-12, there may be other issues or events that could be considered material to investors that an issuer may wish to proactively disclose. In this circumstance, an issuer may consider whether to voluntarily file notice of such issue or event. For example, principal and interest payment delinquencies and non-payment defaults, if material, are required to be disclosed; however, if such events are foreseeable but have not come to fruition, disclosure is not technically required but may be considered. On May 4, 2020, Chairman Jay Clayton and the Director of the Office of Municipal Securities, Rebecca Olsen, issued a public statement entitled *The Importance of Disclosure for our Municipal Markets* encouraging issuers to provide voluntary disclosure, particularly related to COVID-19. Examples include information regarding the impact of COVID-19 on operations and financial condition, information regarding sources of liquidity, information regarding availability of federal, state and local aide and reports prepared for other governmental purposes that might include significant sources of current information of interest to investors. Similarly, voluntary disclosures could extend to ESG and cybersecurity matters.

e. Other examples of events where voluntary disclosures may be considered include:

i. The Discovery of Accounting or Audit Issues – New auditors or new financial staff at a public entity may disagree with prior accounting treatment and/or discover new material issues.

ii. Litigation Surprises – Significant new litigation may be threatened or filed and pending litigation may move in an unanticipated direction.

iii. Legal Advice - After the SEC's enforcement action in *In the Matter of the Port Authority of New York and New Jersey*, disagreements between former and current counsel on issues where legal opinions differ could create disclosable events.

iv. Storms that cause significant damage to a municipality and its infrastructure.

v. Cyberattacks that prevent an issuer from collecting certain revenue supporting the payment of outstanding securities.

vi. Public Events – Issuers may consider whether to file notice of major events or news that may become important local or regional news in effort to get ahead of the commentary, such as changes in senior staff, major news regarding operations, economic or environmental factors, or other events that may gain attention.

IV. An Overview of an SEC Investigation

a. General Process. SEC investigations generally involve the following steps and process: legal hold of documents; document requests; witness testimony; Wells Notice and Wells Submission; and settlement negotiations. Defense counsel may also make presentations to the SEC staff.

b. **SEC Investigations Are Not Public**. All SEC investigations are "non-public," meaning that neither the SEC nor its staff should acknowledge or comment on the investigation unless and until charges are brought. However, parties under investigation may, and are sometimes obligated to, disclose the pendency of an investigation. The need to disclose an investigation depends on the facts and circumstances.

c. **Legal Hold and Document Requests**. Most SEC investigations begin with a subpoena to provide documents and to not destroy any documents related to the matter under investigation. In an investigation of any consequence, the SEC may make several sets of document requests.

d. **Witness Testimony**. If the SEC, after reviewing the document productions, continues to have an investigatory interest, it will usually request sworn witness testimony. Sometimes the SEC will have non-sworn conversations or interviews with the parties.

e. **Opportunities for Advocacy**. Throughout an investigation, there are many opportunities for defense counsel to educate the SEC staff and to advocate. Effective advocacy requires defense counsel to have credibility with the SEC staff. In most cases, the staff will agree to in person meetings with counsel to discuss the salient events and circumstances of interest in the investigation. Extraordinary cooperation can also lead to leniency.

f. **Wells Notice and Wells Submission**. After witness testimony has been completed, the SEC's investigative staff will review the evidentiary record to determine whether to recommend the Commission institute charges. If the staff tentatively decides to make an enforcement recommendation to the Commission in non-emergency cases, it issues a Wells Notice to the proposed defendant (typically by telephone and follow-up letter). The recipient is given an opportunity to respond with a Wells Submission—a detailed legal memorandum explaining his or her position. The staff is generally open to meeting with counsel during this process.

g. **Settlement Negotiations**. If defense counsel does not succeed in convincing the staff that no enforcement action is warranted, counsel will routinely engage the staff in settlement discussions to determine whether the matter can be resolved on mutually agreeable terms. If a settlement is not negotiated, the SEC will commence an administrative or judicial proceeding.

h. **Remedies Available to the SEC**. The SEC is authorized to seek several forms of relief, including: an order against future violations in the form of an injunction (a cease-and-desist order); a censure; financial penalties; and/or a temporary or permanent bar from the securities industry. The availability of some of these remedies may depend on whether the matter is brought administratively or in federal court. Additionally, conditions sought by the SEC in many settlements include other forms of relief such as an undertaking to improve relevant policies and procedures, and the appointment and adoption of an independent consultant's recommendations.

i. Self-Reporting and Cooperation Credit

i. In October 2001, the Commission issued a Report of Investigation and Statement, commonly known as *The Seaboard Report*. For an entity, measures of cooperation include:

1. Self-policing prior to the discovery of the misconduct, including establishing effective compliance procedures and an appropriate tone at the top;

2. Self-reporting of misconduct when it is discovered, including conducting a thorough review of the nature, extent, origins and consequences of the misconduct, and promptly, completely and effectively disclosing the misconduct to the public, to regulatory agencies, and to self-regulatory organizations;

3. Remediation, including dismissing or appropriately disciplining wrongdoers, modifying and improving internal controls and procedures to prevent recurrence of the misconduct, and appropriately compensating those adversely affected; and

4. Cooperation with law enforcement authorities, including providing the Commission staff with all information relevant to the underlying violations and the company's remedial efforts. See *Spotlight on Enforcement Cooperation Program, available at* https://www.sec.gov/spotlight/enforcement-cooperation-initiative.shtml.

    a. In March 2019, the SEC charged the former controller of the College of New Rochelle for defrauding municipal securities investors by concealing the college's deteriorating finances. The controller purportedly created false financial records, did not file payroll tax submissions and did not assess the collectability of pledged donations. In 2015, the college's financial statements overstated the net assets by $34 million.

    However, the SEC did not charge the College of New Rochelle due to the institution's extensive cooperation and remediation efforts. The college publicly disclosed the financial issues, engaged outside expertise to conduct a full internal investigation and issued restated financial results. The college "promptly and extensively" cooperated with the SEC in its investigation and "proactively undertook wide-reaching remedial measures to enhance its internal controls and governance." See SEC Press Release 2019-46 (March 28, 2019).

    In a related matter, the SEC charged two KPMG auditors (Christopher Stanley and Jennifer Stewart) for the issuance of an unmodified audit opinion regarding the College of New

Rochelle's 2015 financial statements. Specifically, the SEC said the auditors "violated Generally Accepted Auditing Standards by, among other things, failing to obtain sufficient appropriate audit evidence, properly prepare audit documentation, properly examine journal entries, adequately assess audit risk, and exercise due professional care and professional skepticism." Without admitting or denying the findings, Stanley and Stewart each agreed to be suspended from appearing or practicing before the SEC as an accountant with the right to apply for reinstatement after three years and one year, respectively. Each also agreed to not serve as the engagement manager, engagement partner, or engagement quality control reviewer in connection with any audit expected to be posted in the MSRB's Electronic Municipal Market Access system until they are reinstated by the SEC. See SEC Press Release 2021-32 (February 23, 2021).

V. An Overview of FINRA Investigation

a. **General Process**. FINRA investigates potential securities violations and, when appropriate, brings formal disciplinary actions against firms and their associated persons. FINRA investigations may be opened from various sources, including automated surveillance reports, examination findings, filings made with FINRA, customer complaints, tips, referrals from other regulators or other FINRA departments and press reports. As a policy, FINRA's investigations are confidential. If it appears that rules have been violated, FINRA Enforcement ("Enforcement") will determine whether the conduct merits formal disciplinary action. FINRA can take disciplinary action through two separate procedures: a settlement or a litigated proceeding. With a settlement, the respondent can opt to resolve alleged rule violations early by submitting a Letter of Acceptance, Waiver and Consent (AWC). Otherwise, FINRA may issue a formal complaint to FINRA's Office of Hearing Officers (OHO). If the respondent does not settle the complaint, the matter proceeds to a contested hearing before OHO, which hears the case and issues a decision.

b. **Bringing SEC Cases.** Enforcement also brings disciplinary cases on behalf of the securities exchanges with which it has entered into Regulatory Services Agreements (RSAs). These matters may be brought on behalf of a single exchange or, more commonly, may be brought as global settlements on behalf of multiple self-regulatory organizations, sometimes including FINRA.

c. **Sanctions.** Sanctions for wrongdoing include fines, suspensions, and, in cases of serious misconduct, bars from the brokerage industry. FINRA publishes its Sanction Guidelines so that members, associated persons and their counsel understand the types of disciplinary sanctions that may be applicable to various violations. Whenever possible, Enforcement orders firms and individuals to make restitution to harmed customers.

d. **Other Outcomes.** Not all investigations result in formal disciplinary action. For example, if the violation is of a minor nature and there is an absence of customer harm or detrimental market impact, the matter may be resolved with an informal disciplinary action, such as the issuance of a Cautionary Action. While Cautionary Actions are considered by the staff in any future disciplinary matter, these actions do not constitute formal discipline and are not reportable on FINRA's Central Registration Depository (CRD) system or Form BD. In addition, Enforcement may determine not to recommend formal disciplinary action following an investigation and may close the matter without further action.

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