

Recent SEC Enforcement Cases

– What Municipal Advisors Need to Know

Municipal Securities Regulation & Enforcement

- Kim Magrini, New York, NY
- Bill Rhodes, Philadelphia, PA
- Ernesto Lanza, Washington, DC

SEC Enforcement in Context

- What is an SEC enforcement case?
 - Pending complaints
 - Settled actions
 - Final judgments
- Roles in an enforcement action
 - SEC Division of Enforcement
 - Public Finance Abuse Unit
 - Regional Offices
 - SEC Division of Examinations
 - SEC Division of Trading and Markets
 - SEC Office of Municipal Securities
 - MSRB
 - FINRA

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 95726 / September 9, 2022

ADMINISTRATIVE PROCEEDING
File No. 3-21059

In the Matter of

ORDER INSTITUTING ADMINISTRATIVE
AND CEASE-AND-DESIST PROCEEDINGS,
PURSUANT TO SECTIONS 15(b), 15B AND

Case 6:22-cv-06273 Document 1 Filed 06/14/22 Page 1 of 27

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE
COMMISSION,

Plaintiff,

vs.

Case No. 22-cv-6273

COMPLAINT

Jury Trial Demanded



MSRB Rule Book

Click to view all MSRB
Rules

Rule G-42

Duties of Non-Solicitor Municipal Advisors

Rule

Interpretive Guidance

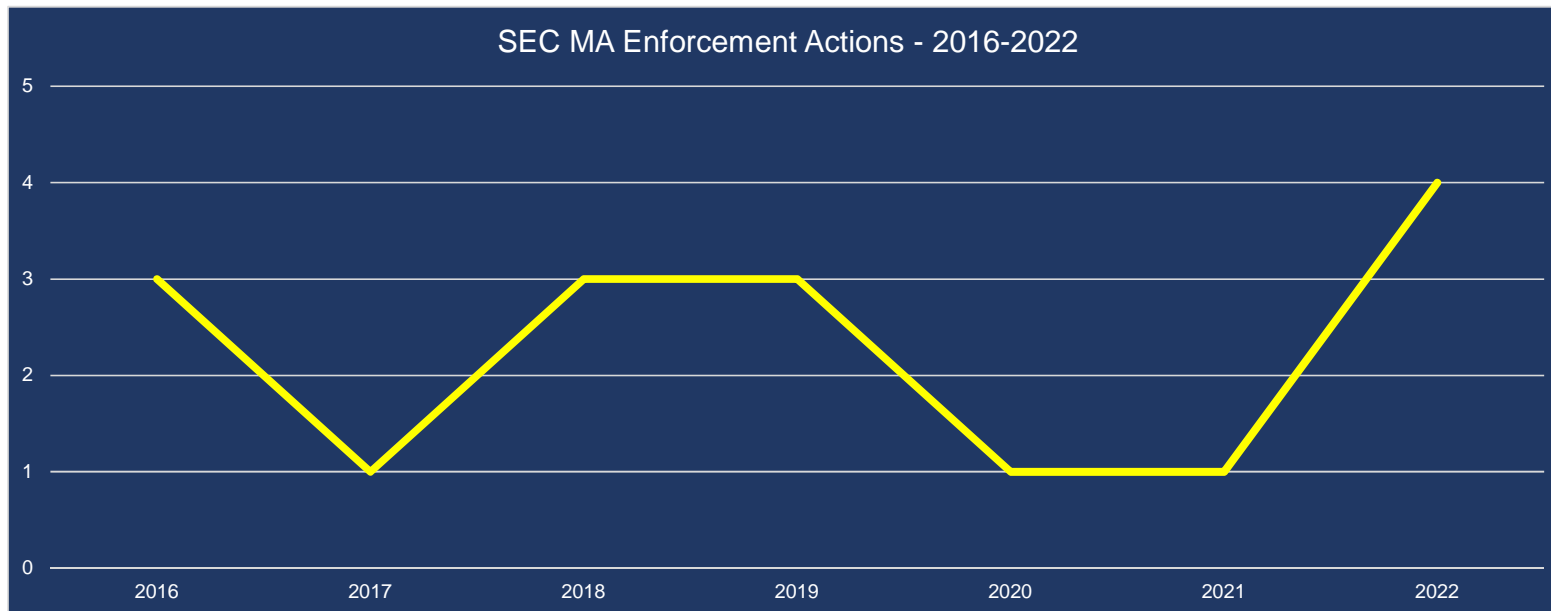
Rule History

Summary

Establishes the core standards of conduct and duties of municipal advisors when engaging in municipal advisory activity under this rule).

SEC Enforcement Trends

- SEC enforcement actions against MAs are picking back up
 - Four MA cases in 2022 so far



SEC Enforcement Trends

- SEC has made the following allegations against MAs and/or MA personnel in enforcement actions since 2016 – most cases cite multiple violations
 - Unregistered MA – 9 violations
 - Unregistered BD – 1 violation
 - MSRB Rule G-3 qualifications – 1 violation
 - MSRB Rule G-44 MA supervision – 1 violation

 - Statutory fiduciary duty – 11 violations
 - MSRB Rule G-42 MA duty – 4 violations
 - MSRB Rule G-17 fair dealing – 9 violations
 - Anti-fraud – 7 violations
 - Aiding & abetting issuer/obligor fraud – 2 violations
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- MSRB Rule G-23 MA/BD role switching – 1 violation
 - MSRB Rule G-27 BD supervision – 1 violation
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- “Process” Violations**
- “Substance” Violations**
- BD/MA Violations**

Registration & Qualification

- Unregistered MA: SEC continues to find unregistered MAs
 - Engaging in traditional MA activities without registering:
 - Advisors to charter and public schools for bond issuances
 - Advisor to town applying for bond approval for private placements
 - Engaging in less traditional MA activities without registering:
 - Broker-dealer providing advice on investment of bond proceeds
 - Unregistered MA also brokered sale of issue as unregistered BD
 - Paid solicitors for MA business (unregistered solicitors & MA using them)
 - Unqualified MA Professional: Even if MA is registered, also must ensure that professionals engaged in MA activities are qualified under MSRB Rule G-3
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MA Duties – Duty of Care – Agreed Upon Services

- Alleged MA violation of fiduciary duty/Rule G-42 for activities in scope of services
 - Rating process & offering disclosure: MA contracted to provide these services
 - MA allegedly allowed materially false information to rating agency & in OS
 - Pricing advice: MA contracted to assist in new issue pricing, negotiate on behalf of issuer for aggressive pricing & undertake specific actions
 - MA allegedly did not take contracted actions & deferred to underwriter
 - Advise on underwriter selection: MA contracted to help issuer identify underwriters most experienced in type of securities
 - MA allegedly took no action to assess underwriter, which had letter of intent that acknowledged issuer not required to use that firm
 - Assist on continuing disclosure compliance: MA contracted to provide service
 - MA failed to advise issuer of flawed CDA amendment
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MA Duties – Duty of Care – Fraudulent/Deceptive Actions

- Alleged MA fraudulent or deceptive activities
 - Materially false disclosures: MA contracted to assist in rating process & offering disclosure allegedly committed fraud & aided & abetted issuer fraud
 - False financial projections: MA prepared false projections in issuer application to state bond commission; application provided to investors
 - MA allegedly committed fraud; aided & abetted issuer in committing fraud; violated statutory fiduciary duty & MSRB Rules G-17 & G-42
 - Sharing issuer confidential information: MA advising issuer on hiring of professionals shared confidential information to firm seeking engagement
 - MA engaged in fraud/deception & violated fiduciary duty & Rule G-17
 - False billing: MA falsely billed issuer client and recommended hiring of underwriter that had made undisclosed payment to MA
 - MA engaged in fraud/deception & violated fiduciary duty & Rule G-17
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MA Duties – Duty of Loyalty – Undisclosed Conflicts

- Alleged MA undisclosed conflicts or prohibited relationships
 - Failure to make conflicts disclosures: MA allegedly failed to disclose conflict from compensation contingent on size or closing & falsely stated MA had no undisclosed conflicts in hundreds of cases – violated fiduciary/G-42 duty
 - Failure under Rule G-44 to have WSPs & then to enforce updated WSPs
 - Undisclosed dual capacity and fee-splitting: MA personnel failed to disclose working for UW, prohibited fee-splitting with UW & higher fee structure – violated fiduciary/G-42 duty & engaged in fraud/deception toward client
 - Undisclosed dual capacity: MA personnel assisting with procuring UW were associated with UW – violated fiduciary duty & Rules G-17 & G-23
 - Undisclosed relationship; misrepresentation: MA also employed by bond counsel firm misrepresented qualifications in brochure & failed to disclose to client its relationship with law firm – engaged in fraud/deception toward client & violated fiduciary duty & Rule G-17
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Reading the Tea Leaves on Potential Future Enforcement Targets

- SEC Enforcement in Other Markets as a Window to the Future
 - BD Failure to Maintain Records of Electronic “Off-Channel” Communications
 - BDs must preserve all communications relating to firm’s business as such
 - BDs’ WSPs generally prohibited use of unapproved electronic communications methods & personnel should not use unapproved personal email, chat or text-messaging applications for business purposes
 - Messages sent through BD-approved communications methods were archived, but messages sent through unapproved methods were not
 - BDs failed to enforce WSP, failing to maintain copies of messages
 - So far, over a dozen BDs settled recordkeeping & supervision charges for large fines & SEC efforts continuing
 - Note that MA recordkeeping rule has comparable language to BD recordkeeping rule
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Reading the Tea Leaves on Potential Future Enforcement Targets

- SEC Division of Examinations – August 22, 2022 MA Risk Alert
 - Registration and Filings: Inaccurate/incomplete/inconsistent filings; failure to amend/untimely amendments; annual filing & MSRB fee payment failure
 - Recordkeeping: All categories of records
 - Supervision: Deficiencies of WSPs/annual reviews & certifications
 - Engagement Documentation/Conflicts Disclosure: No disclosure/no statement of “no conflicts”/late or inadequate relationship documentation
 - Exams to focus more sharply on core MA standards of conduct & duties – possible areas discussed at SEC/MSRB/FINRA compliance events:
 - Documenting/fulfilling MA’s scope of services
 - MA duties during new issue pricing process
 - Role of MAs in bank loans/direct placements
 - Basis for MA’s recommendation or review of third-party recommendations
 - Use of consultants/co-MAs – licensing, documentation, oversight
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Reading the Tea Leaves on Potential Future Enforcement Targets

- Recent MSRB MA-Related Activity
 - CUSIPs in Competitive Offerings: Changes to MA requirement have recently been finalized
 - Use of Social Media: With SEC BD messaging enforcement actions, the recent new social media requirements may generate regulator interest
 - MA Website & Other Marketing Materials: While MSRB may soon allow testimonials, other marketing activities may be of interest to regulators
 - Gift & Pay-to-Play Rules: Gift recordkeeping & practices are periodically of interest to regulators & regulators sometimes look back at political giving after an election cycle
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Tips to Avoid Becoming an Enforcement Target

- Put your self in your client's shoes – given nature of engagement agreement & pattern of interaction, what does the client think you're obligated to do?
 - Pay attention to your scope of services – explicitly limit where needs limiting & don't overpromise, especially services you have no intention of providing
 - Remember, your legal scope is not just what is written in engagement agreement but also what actions you in fact take:
 - Either: (i) don't act in contradiction to what you say in writing or (ii) update the written scope if you take action not consistent with agreement
 - Rather than be defensive about examination findings, use them to build good will with the regulator & to make changes to buttress your compliance efforts
 - Keep up with what the regulators say (by rule, interpretation, compliance resource or at conferences) and what they do (by enforcement)
 - Take actions for your client as if you were acting for yourself – you do what's right & don't help your client do wrong!
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Ballard Spahr MA Legal & Compliance Services Contacts



Ernesto A. Lanza

lanzae@ballardspahr.com

202.777.6053
Washington, DC



Kimberly D. Magrini

magrinik@ballardspahr.com

646.346.8086
New York, NY



William C. Rhodes

rhodes@ballardspahr.com

215.864.8534
Philadelphia, PA



Teri M. Guarnaccia

guarnacciat@ballardspahr.com

410.528.5526
Baltimore, MD



Scott L. Diamond

diamonds@ballardspahr.com

646.346.8065
New York, NY



Lisa Brice

bricel@ballardspahr.com

646.346.8014
New York, NY



Jennifer P. Brooks

brooksjp@ballardspahr.com

303.299.7384
Denver, CO



Tyler M. Cobb

cobbt@ballardspahr.com

602.798.5420
Phoenix, AZ



Brian R. Peltier

peltierb@ballardspahr.com

612.371.3231
Minneapolis, MN



Dara N. Smith

smithdn@ballardspahr.com

215.864.8382
Philadelphia, PA



Tesia N. Stanley

stanleyt@ballardspahr.com

801.531.3036
Salt Lake City, UT



Ben Vernon

vernonb@ballardspahr.com

424.204.4321
Los Angeles, CA

Municipal Advisor Legal & Compliance Services

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