

Municipal Securities Enforcement: The SEC Takes Aim at Municipal Advisors

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PRACTICES Investment Banking and Broker Dealer, Public Finance

As a part of its emphasis on transparency and disclosure in the municipal securities markets, the Securities and Exchange Commission ("**SEC**") brought charges this month against an advisor to municipal entities. Following a series of actions against municipal issuers and underwriters in the past year, this action was the first enforcement action under the municipal advisor provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank**").¹ On July 13, 2016, the SEC announced settled proceedings against School Business Consulting, Inc. ("**SBCI**") and its President,² as well as against Keygent LLC, and two of its managing directors.³ The SEC alleged that SBCI failed to register as a municipal advisor and that it improperly shared with Keygent information regarding five California school districts in their selection of municipal financial advisors.

Background

According to the SEC's Order, SBCI, through its President and sole employee, Terrance Bradley, provided consulting services to California school districts and made recommendations to those districts regarding the selection of municipal advisors. Keygent, a municipal advisory firm, and two of its managing directors, Anthony R. Hsieh and Chet Wang, advised California school districts and community colleges that issued bonds.

The SEC alleged that, in 2010, SBCI entered into a contract with Keygent to advise it on strategy, business development, public policy and research. In addition, Bradley began serving on Keygent's advisory board, for which SBCI was paid \$2,500 per month. The SEC alleged that Bradley introduced Keygent representatives to five SBCI school district clients that were seeking to hire a municipal advisor. Bradley, who often participated in drafting requests for qualifications issued by SBCI's client school districts, allegedly provided Keygent, Hsieh and Wang with confidential information about the hiring processes used by each district, including advance notice of draft interview questions and details of some of their competitors' proposals.

In the Order, the SEC found that Bradley verbally disclosed his relationship with Keygent to the school districts and that Keygent's contracts with the school districts disclosed Bradley's position on their advisory board. However, the SEC alleged that SBCI and Bradley did not have authority to share confidential information with Keygent and, further, that the school districts were unaware that such information had been provided. Subsequently, Keygent was hired as the municipal advisor by each of the five school districts.

SEC Charges

The SEC charged SBCI with failing to register with the SEC and Municipal Securities Rulemaking Board ("**MSRB**") as a municipal advisor, as required by Dodd-Frank.⁴ By receiving direct compensation from Keygent and soliciting school districts on Keygent's behalf, the SEC found that

SBCI was engaged in the “solicitation of a municipal entity”⁵ and such solicitation was for the “purpose of obtaining or retaining an engagement . . . in connection with . . . the issuance of municipal securities.” The SEC maintained that SBCI should have been registered as a municipal advisor when it began soliciting on behalf of Keygent. As a result, the SEC found that SBCI violated Section 15B(a)(1)(B) of the Securities Exchange Act of 1934 (“**Exchange Act**”)⁶ by failing to register as a municipal advisor and that Terrance Bradley caused SBCI’s violation.

In addition, the SEC found that SBCI and Bradley breached their fiduciary duties under Section 15B(c)(1) of the Exchange Act,⁷ violated Section 15B(a)(5) of the Exchange Act (which prohibits any fraudulent, deceptive, or manipulative act or practice while undertaking the solicitation of a municipal entity), and failed to deal fairly with the school districts in violation of MSRB Rule G-17 and Section 15B(c)(1). Without admitting or denying the SEC’s findings, SBCI agreed to the entry of a censure and a civil penalty of \$30,000 and Bradley consented to a civil penalty of \$20,000 and to a bar from acting as a municipal advisor in the future.

The SEC found that Keygent and Hsieh violated Section 15B(c)(1) and MSRB Rule G-17⁸ by not dealing fairly with the school districts involved and that Hsieh and Wang caused Keygent’s violations. The SEC further found that Keygent, Hsieh, and Wang caused SBCI’s and Bradley’s violations of Sections 15B(c)(1) and 15B(a)(5) and MSRB Rule G-17. Without admitting or denying the SEC’s allegations, Keygent consented to a censure and \$100,000 civil penalty, while Hsieh and Wang consented to pay penalties of \$30,000 and \$20,000, respectively.

Continuing SEC Focus

The SEC’s specialized enforcement group formed in 2010 to focus on municipal securities and public funds was slow to show activity, even after passage of the Dodd-Frank provision to regulate municipal advisors. However, with this first enforcement action against municipal advisors, the numerous previous settlements with underwriters and issuers under the Municipalities Continuing Disclosure Cooperation Initiative, and additional fraud cases against entities and individuals, there can be no question now that municipal securities professionals will remain subject to SEC scrutiny. Underwriters, issuers, municipal officials, and now municipal advisors must keep fiduciary duties and disclosure at the forefront of their offering activities.

For more information please contact one of the lawyers listed below.

¹ Press Release, *SEC: Muni Advisors Acted Deceptively With California School Districts* (June 13, 2016).

² Order Instituting Administrative and Cease-And-Desist Proceedings Pursuant to Sections 15B(c) and 21C, and Rule 15Bc4-1 of the Securities Exchange Act of 1934, and Section 9(b) of the Investment Company Act of 1940, Making Findings, and Imposing Remedial Sanctions and a Cease-And-Desist Order In the Matter of School Business Consulting, Inc. and Terrance Bradley.

³ Order Instituting Administrative and Cease-And-Desist Proceedings Pursuant to Sections 15B(c) and 21C, and Rule 15Bc4-1 of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-And-Desist Order In the Matter of Keygent LLC, Anthony Hsieh, and Chet Wang (the “Keygent Order”).

⁴ Although it had registered with the SEC as a municipal advisor and soliciting municipal advisor in

February 2014 under the temporary registration rules, the SEC found that SBCI failed to register under the final registration rule, effective July 1, 2014, and had never registered with the MSRB.

⁵ As defined in Section 15B(e)(9) of the Exchange Act.

⁶ Section 15B(a)(1)(B) prohibits a municipal advisor from providing “advice to or on behalf of a municipal entity or obligated person . . . or [undertaking] a solicitation of a municipal entity or obligated person, unless the municipal advisor is registered in accordance with this subsection.”

⁷ Section 15B(c)(1) of the Exchange Act requires that municipal advisors shall not “provide advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products, the issuance of municipal securities, or to undertake a solicitation of a municipal entity or obligated person, in contravention of any [MSRB Rule].”

⁸ MSRB Rule G-17 states that, “in the conduct of its municipal securities or municipal advisory activities, each broker, dealer, municipal securities dealer, and municipal advisor shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice.”