

Client Alert

Current Issues Relevant to Our Clients

November 13, 2014

SEC Charges Mayor as a “Control Person” in City’s Fraudulent Municipal Offering

On November 6, 2014, the Securities and Exchange Commission announced that fraud charges had been issued against the city of Allen Park, Michigan, and two former city leaders. An SEC investigation into the city’s sale of \$31 million in general obligation bonds, sold to support a movie studio project, found that the offering documents provided to investors contained false and misleading statements about the scope and viability of the proposed project and about the overall financial condition of Allen Park at the time the bonds were offered to investors.

Two former Allen Park municipal officials were included in the SEC charges, including the former city mayor. The SEC alleges that the ex-mayor was an “active champion” of the failed project and additionally that he was in a position to control the actions of the city and the city administrator. Based on this “control” the SEC held the former mayor accountable for the violations committed by the city and the city administrator.

This enforcement action marks the first instance in which the SEC has charged a municipal officer under a federal statute which creates liability for a “control person.”

The SEC alleged that the former mayor participated in the drafting of inaccurate and misleading press releases, and made inaccurate and misleading public statements about the project during the period when the city voted to issue the bonds. Some of these press releases and related documents were maintained on the city’s website during the same period. The former mayor has agreed to settle the SEC’s charges and, among other conditions, will pay a \$10,000 penalty. The former city administrator was also charged as the official responsible for reviewing and approving the fraudulent bond offering documents.

According to the SEC action, the city began planning a movie studio project in late 2008 with the hope of attracting needed economic development. The city issued two series of bonds (in 2009 and 2010) to raise funds for the development of a \$146 million professional facility with eight sound stages. However, the SEC alleges that by the time the first series of bonds were issued, the project had been downsized to the building and operation of a vocational school, and that these updated plans were not reflected in the offering documents or other public statements made by the city. The SEC further alleges that the city used outdated budget information in the offering documents which did not reflect the city’s then-current \$2 million dollar budget deficit.

The SEC’s press release and the complaints against the city, the former mayor and the former city administrator can be found here:

- [SEC’s press release.](#)
- [SEC’s complaint against Allen Park, Michigan.](#)
- [SEC’s complaint against the former mayor.](#)
- [SEC’s complaint against former city administrator.](#)

To avoid similar SEC charges, issuers should consider these guidelines:

- Keep all financial disclosures timely and disclose any conditions indicating a decrease in financial stability.

- Any changes in the project or in the issuer's financial condition must be noted for subsequent related series of bonds as well as in annual disclosure on EMMA. Issuers are "speaking to the market" when posting information on EMMA and should be sure that they are not omitting information that would be material to investors.
- A municipal officer who could be considered as a "control person" for the financial decisions and public statements of the municipal entity should carefully review and understand the bond transactions and the representations made in any offering document.
- Municipal officials should be careful when making public statements relating to bond transactions or posting information on issuer websites that might be considered misleading or that omit important facts. Financial information on issuer websites should have appropriate disclaimers.

For More Information

To discuss any of the topics covered in this client alert, please contact a member of our Public Finance Group or visit us online at chapman.com.

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