

SEC Files Charges in Municipal Bond "Flipping" and Kickback Schemes

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***Securities and Exchange Commission v. Core Performance Management, LLC, et al.*, No. 9:18-civ-081081-BB (S.D. Fla. filed August 14, 2018)**

***Securities and Exchange Commission v. RMR Asset Management Company, et al.*, No. 3:18-cv-01895-AJB-LL (S.D. Cal. filed August 14, 2018)**

The Securities and Exchange Commission charged two firms and 18 individuals in a scheme to improperly divert new issue municipal bonds to broker-dealers at the expense of retail investors. According to the SEC's complaint, the defendants - known in the industry as "flippers" - purchased new issue municipal bonds, often by posing as retail investors to gain priority in bond allocations. The defendants then "flipped" the bonds to broker-dealers for a fee. The SEC also charged a municipal underwriter for accepting kickbacks from one of the flippers.

The SEC alleges that from at least 2009 to 2016, Core Performance Management LLC ("CPM"), RMR Asset Management Co. ("RMR"), their principals, and certain of their associates, misrepresented their identities to gain priority in new issue municipal bond allocations. Municipal issuers typically require underwriters to give retail investor orders the highest priority when allocating new issue bonds, particularly retail investors within the municipal issuer's jurisdiction. According to the SEC's complaint, these defendants used fictitious business names, falsely linked their orders to ZIP codes within the issuer's jurisdiction, and split orders among dozens of accounts. After acquiring the bonds, the SEC alleges that the defendants quickly resold them to broker-dealers, typically for a fixed, pre-arranged commission, and often sought to hide the flipping activity from issuers and underwriters by manipulating sales tickets.

The SEC alleges that CPM, its principal James P. Scherr, and associates Deborah B. Dora, Sharlene F. Mesite, and Anadel R. Pinzon violated Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5 thereunder; that CPM and Dora also aided and abetted violations of Section 10(b) and Rule 10b-5(b) thereunder; that Scherr and CPM violated Sections 17(a)(1) and (3) of the Securities Act of 1933 ("Securities Act"); that CPM, Scherr, Dora, Mesite, Pinzon, and associate James J. O'Neil violated Section 15(a)(1) of the Exchange Act; that CPM, Dora, Mesite, Pinzon, and Scherr violated Rule G-17 of the Municipal Securities Rulemaking Board ("MSRB"); and that Scherr is liable as a control person under Section 20(a) of the Exchange Act for CPM's violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

In addition, the SEC alleges that RMR, its principal Ralph M. Riccardi, and associates Bruce A. Broekhuizen, Douglas J. Derryberry, David R. Frost, Neil P. Kelly, John M. Kirschenbaum, Timothy J. McAloon, Jocelyn M. Murphy, Dewey T. Tran, and Philip A. Weiner violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder; that RMR, Riccardi, Frost, and Kirschenbaum also aided and abetted violations of Section 10(b) of the Exchange Act and Rule 10b-5(b) thereunder; that RMR, Riccardi, Broekhuizen, Derryberry, Frost, Kelly, Kirschenbaum, McAloon, Murphy, Tran, and Weiner, as well as associates Richard C. Gounaud, David S. Luttbeg, Michael S. Murphy violated Section 15(a)(1) of the Exchange Act; and that RMR, Broekhuizen, Derryberry, Frost, Kelly, Kirschenbaum, McAloon, Jocelyn Murphy, Riccardi, Tran, and Weiner violated MSRB Rule G-17.

CPM, Scherr, Dora, Mesite, O'Neil, and Pinzon settled the SEC's charges without admitting or denying the allegations, agreeing to injunctions, to return allegedly ill-gotten gains with interest, pay civil

penalties, be subject to industry bars or suspensions, and to cooperate with the SEC's ongoing investigation. In addition, RMR, Riccardi, Broekhuizen, Derryberry, Frost, Kelly, Kirschenbaum, Luttbeg, McAloon, Tran, and Weiner settled the SEC's charges without admitting or denying the allegations, agreeing to injunctions, to return allegedly ill-gotten gains with interest, pay civil penalties, be subject to industry bars or suspensions, and to cooperate with the SEC's ongoing investigation.

The settlements are subject to court approval. The SEC's charges against RMR associates Gounaud and the Murphys will be litigated in U.S. District Court for the Southern District of California.

In a related action, the SEC instituted settled proceedings against Charles Kerry Morris, the former head of municipal underwriting at broker-dealer NW Capital Markets Inc. The SEC found that Morris took kickbacks from Scherr and engaged in a parking scheme in which Morris allocated new issue bonds to Scherr with the understanding that Morris would repurchase them. As a result of this trading, the SEC found that Morris and NW Capital caused Scherr and Core Performance's improper unregistered broker activity. Specifically, the SEC found that Morris willfully violated Sections 17(a)(1) and (3) of the Securities Act, Section 10(b) and Rules 10b-5(a) and (c) thereunder, MSRB Rule G-17, and caused violations of Section 15(a)(1) of the Exchange Act. The SEC also found that NW Capital willfully violated MSRB Rule G-17, Section 15B(c)(1) of the Exchange Act, and caused violations of Sections 15(a)(1) of the Exchange Act. The SEC found that Morris's supervisor, James A. Fagan, failed reasonably to supervise Morris's activities within the meaning of Section 15(b)(6) of the Exchange Act, incorporating Section 15(b)(4)(E) of the Exchange Act, and willfully violated MSRB Rule G-27.

Morris, NW Capital, and Fagan agreed to settle the charges without admitting or denying the SEC's findings. Morris agreed to pay a total of \$254,009 and to consent to an industry bar. NW Capital agreed to be censured and pay a total of \$87,065 and Fagan agreed to pay a \$10,000 penalty and to consent to a six-month supervisory suspension.

The investigation, which is continuing, is being conducted by the Division of Enforcement's Public Finance Abuse Unit, including Joseph Chimienti, Laura Cunningham, Warren Greth, Cori Shepherd, and Jonathan Wilcox, with assistance from Deputy Unit Chief Mark Zehner and litigation counsel Nicholas Pilgrim. Kevin Guerrero and Ivonia Slade supervised the investigation. Mr. Pilgrim will lead the litigation against Gounaud, Jocelyn Murphy, and Michael Murphy.