

MEMO# 24503

August 20, 2010

SEC Charges State of New Jersey with Fraudulent Bond Offerings

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TO: MUNICIPAL SECURITIES ADVISORY COMMITTEE No. 35-10
FIXED-INCOME ADVISORY COMMITTEE No. 15-10 RE: SEC CHARGES STATE OF NEW JERSEY
WITH FRAUDULENT BOND OFFERINGS

The Securities and Exchange Commission has settled a fraud action against the State of New Jersey for misrepresenting and failing to disclose to investors in 79 municipal bond offerings between August 2001 and April 2007 that it was underfunding the State's two largest pension plans. [\[1\]](#) Specifically, the proceedings alleged that the State of New Jersey offered and sold more than \$26 billion worth of bonds using offering documents that provided inadequate information for investors to evaluate the State's ability to fund the Teachers' Pension and Annuity Fund ("TPAF") and the Public Employees' Retirement System ("PERS") or the impact of the State's pension obligations on the State's financial condition. The Commission therefore charged the State of New Jersey with violations of the antifraud provisions of Sections 17(a)(2) and 17(a)(3) of the Securities Act of 1933. The State has agreed to settle the alleged charges without admitting or denying the allegations, and has consented to a cease and desist order from future violations of these provisions.

The Commission alleged that the State made material misrepresentations and omissions about the underfunding of TPAF and PERS in its preliminary official statements, official statements, and continuing disclosures. These disclosure documents created the false impression that the TPAF and the PERS were being adequately funded, masking the fact that New Jersey was unable to make contributions to TPAF and PERS without raising taxes, cutting other services, or otherwise affecting its budget. For example, the offering documents failed to disclose and misrepresented information about: legislation adopted in 2001 that increased retirement benefits for employees and retirees enrolled in TPAF and PERS; special Benefit Enhancement Funds (BEFs) created by the 2001 legislation initially intended to fund the costs associated with the increased benefits; the state's use of the BEFs as part of a five-year "phase-in plan" to begin making contributions to TPAF and PERS; and the state's alteration and eventual abandonment of the five-year phase-in plan.

In the cease and desist order, the Commission found that the State of New Jersey was aware of the underfunding of TPAF and PERS and the potential effects of the underfunding. In addition, it found that the State had no written policies or procedures about the review or update of the bond offering documents and the State did not provide training to its employees about the state's disclosure obligations under accounting standards or the federal securities laws. As a result of this lack of disclosure training and inadequate procedures for the drafting and review of bond disclosure documents, the State of New Jersey made material misrepresentations to investors and failed to disclose material information regarding TPAF and PERS in bond offering documents.

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endnotes

[1] See SEC Press Release 2010-152, SEC Charges State of New Jersey for Fraudulent Municipal Bond Offerings, August 18, 2010, available at <http://www.sec.gov/news/press/2010/2010-152.htm>.

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