INITIAL DECISION RELEASE NO. 274
ADMINISTRATIVE PROCEEDING
FILE NO. 3-11465

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of	:	
	:	
PUBLIC FINANCE	:	
CONSULTANTS, INC.,	:	INITIAL DECISION
ROBERT D. FOWLER,	:	February 25, 2005
DOLPHIN AND BRADBURY,	:	
INCORPORATED,	:	
and ROBERT J. BRADBURY	:	
	:	

APPEARANCES: Denise D. Colliers, Patricia A. Paw, and Mark R. Zehner for the Division of Enforcement, Securities and Exchange Commission.

Joseph U. Metz for Respondents Public Finance Consultants, Inc., and Robert D. Fowler.

Philip G. Kircher, Scott Magargee, and William J. Winning for Respondents Dolphin and Bradbury, Inc., and Robert J. Bradbury.

BEFORE: James T. Kelly, Administrative Law Judge.

The Securities and Exchange Commission (SEC or Commission) issued its Order Instituting Proceedings (OIP) on April 26, 2004, pursuant to Section 8A of the Securities Act of 1933 (Securities Act) and Sections 15(b), 15B, and 21C of the Securities Exchange Act of 1934 (Exchange Act).

The proceeding arises out of the issuance of $75.35 million in long-term, non-taxable municipal bonds by the Dauphin County General Authority (DCGA or Authority), a non-party, to finance the purchase of Forum Place, an office building and parking lot complex in Harrisburg, Pennsylvania, in July 1998. According to the OIP, the Official Statement (OS) and the financial projections used to market the bonds to prospective investors were misleading and omitted to state material facts about Forum Place, specifically, the departure of a major tenant.

Public Finance Consultants, Inc. (PFC), of Harrisburg, Robert D. Fowler (Fowler), PFC's President, Dolphin and Bradbury, Inc. (D&B), a broker and dealer located in Philadelphia,

Pennsylvania, and Robert J. Bradbury (Bradbury), D&B's chief executive officer, are named as Respondents. PFC and Fowler served as financial advisors to DCGA, and D&B and Bradbury served as the underwriter for the Forum Place bond transaction.

The OIP alleges that the Authority violated, and PFC and Fowler caused the Authority's violations of, Sections 17(a)(2) and 17(a)(3) of the Securities Act.[1] The OIP also asserts that D&B and Bradbury willfully violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, Exchange Act Rule 10b-5, and Municipal Securities Rulemaking Board Rule G-17 (MSRB Rule G-17). Finally, the OIP claims that D&B willfully violated, and Bradbury willfully aided and abetted and caused D&B's violations of, Section 15B(c)(1) of the Exchange Act.

The Commission's Division of Enforcement (Division) seeks the imposition of cease-and-desist orders, disgorgement of ill-gotten gains, and prejudgment interest against all Respondents. In addition, the Division requests civil monetary penalties against D&B and Bradbury. Respondents maintain that all charges should be dismissed.

I held a seven-day hearing in Philadelphia during August 2004.[2] The parties have filed posthearing pleadings and the matter is ready for decision.[3] I base my findings and conclusions on the entire record and on the demeanor of the witnesses who testified at the hearing. I have applied "preponderance of the evidence" as the standard of proof. See Steadman v. SEC, 450 U.S. 91, 97-104 (1981). I have considered and rejected all arguments, proposed findings, and proposed conclusions that are inconsistent with this decision.

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[1] In a separate proceeding, the Authority, without admitting or denying the Commission's allegations, consented to the entry of findings that it violated Sections 17(a)(2) and 17(a)(3) of the Securities Act and to the imposition of a cease-and-desist order. See Dauphin Co. Gen. Auth., 82 SEC Docket 2884 (Apr. 26, 2004) (settled case).

[2] The hearing transcript, as corrected by my Orders of September 23 and October 7, 2004, will be cited as "Tr. ___." The Division's exhibits will be cited as "DX ___." PFC and Fowler's only exhibit will be cited as "RX 16." D&B and Bradbury's exhibits will be cited as "RX ___."

[3] The Division's Proposed Findings of Fact and Conclusions of Law and the Division's Post-Hearing Brief, both dated Oct. 8, 2004, will be cited as "Div. Prop. Find. ___" and "Div. Br. ___," respectively. PFC and Fowler's Post-Hearing Brief, dated Oct. 7, 2004, will be cited as "PFC Br. ___." The Bradbury Respondents' Proposed Findings of Fact and Conclusions of Law and Post-Hearing Legal Memorandum, both dated Oct. 8, 2004, will be cited as "D&B Prop. Find. ___" and "D&B Br. ___," respectively. The parties also submitted reply pleadings, dated Nov. 1, 2004, which will be cited as "Div. Reply to PFC ___," "Div. Reply to D&B ___," "PFC Reply Br. ___," and "D&B Reply Br. ___," respectively.

FINDINGS OF FACT

A. Background.

Respondents

PFC is a financial advisory business incorporated in Pennsylvania in 1986 (PFC Answer). The firm is not registered with the Commission in any capacity (PFC Answer). PFC was a financial advisor on approximately two-thirds of DCGA's bond transactions between 1986 and June 1, 2000 (PFC Answer; Tr. 879; DX 1). DCGA did not use a financial advisor on some of the remaining one-third of its bond transactions (Tr. 879). PFC served as a financial advisor to DCGA in connection with the Forum Place bond transaction in 1998 (PFC Answer). The relationship between PFC and DCGA was based on a handshake (Tr. 973).

Fowler, age fifty-one, is a founder and President of PFC (PFC Answer; DX 2). He earned a B.A. degree in Economics from the University of Virginia in 1974 and has worked in the financial services industry for twenty-eight years (PFC Answer; Tr. 864). In addition to owning PFC, Fowler operates a second firm, Program Administration Services, Inc. (PASI), which performs program administration services for municipal bond issuers (Tr. 864-65). Before starting his own firms, Fowler worked as an investment banker for approximately ten years (Tr. 866). Fowler resides in Hummelstown, Pennsylvania (Tr. 864).

D&B is an investment banking firm located in Philadelphia (D&B Answer; Tr. 801-02). It specializes in the origination and distribution of non-taxable bonds issued by municipalities and municipal authorities within the Commonwealth of Pennsylvania (Commonwealth) (D&B Answer; RX 28). D&B has fourteen employees (Tr. 802). It has been registered with the Commission as a broker and dealer since 1986 (D&B Answer). Before 1986, D&B operated as a partnership (RX 28). D&B had worked closely with DCGA since 1989 as underwriter on several successful bond issuances (D&B Answer; Tr. 745). DCGA retained D&B in 1998 to underwrite the bond issue for the purchase of Forum Place (D&B Answer).

Bradbury, age fifty-six, owns 38% of D&B and serves as the firm's chief executive officer (D&B Answer; Tr. 665, 667). He has been licensed by the National Association of Securities Dealers since 1969 (D&B Answer). Bradbury has approximately thirty-five years of experience in underwriting municipal bonds and performing related broker-dealer activities (D&B Answer). He earned a B.S. degree from La Salle University in 1969 and resides in Chadds Ford, Pennsylvania (Tr. 661).

Dauphin County, Pennsylvania

Dauphin County is located in south-central Pennsylvania. It has a population of 251,798 (2000 census). Dauphin County is governed by a three-member Board of Commissioners (Tr. 1303). The largest employer in Dauphin County is the Commonwealth (DX 4 at PW 248, 252-54). Harrisburg is the county seat of Dauphin County and the capital of Pennsylvania (DX 4 at PW 248). Harrisburg has a population of 48,950 (2000 census). See Pennsylvania State Data Center, http://pasdc.hbg.psu.edu.

DCGA

DCGA is a municipal authority organized under the Municipality Authorities Act of 1945.[4] It was incorporated in 1984 and its office is in Harrisburg (DX 16 at 14). The governing body of DCGA is a Board consisting of five members appointed by the Commissioners of Dauphin County to five-year staggered terms (Tr. 826-27; DX 16 at 14). During 1998, DCGA employed a full-time executive director, an administrative assistant/secretary, and a bookkeeper (Tr. 13). Gregory J. Ricci (Ricci) was chairman of DCGA's Board and Sidney A. Reese (Reese) was DCGA's executive director while the Forum Place offering was under consideration (DX 16 at 15).

DCGA was an active issuer of municipal bonds (Tr. 933, 1516-17; DX 1). It was especially aggressive during 1997 and 1998, when interest rates were low (Tr. 937-38; DX 1). The Authority met on a monthly basis from 1986 to 1996, and on a weekly basis during 1997 and 1998 (Tr. 11-12, 49-50; DX 16 at 14, DX 18 at 12). DCGA was the second largest bond issuer in Pennsylvania during 1997, ranking only behind the Commonwealth itself (RX 44, Minutes of Mar. 17, 1998, Meeting at 3) (discussing Daniel Kruger, "1997 Was A Very Good Year for the Region's Large Issuers," 323 Bond Buyer 26 (Feb. 9, 1998)). DCGA continued to be an active issuer until 2000 (RX 41 ¶¶ 181, 536).

Fowler and the Authority shared an expansive understanding of the Municipality Authorities Act: project financing for public purposes was permissible if it benefited any residents of the Commonwealth; the project did not necessarily have to be located in Dauphin County or even benefit the residents of Dauphin County (Tr. 10, 881-84, 928, 1306, 1401). As a result, several of DCGA's bond issues involved financing for projects outside of Dauphin County (DX 1).[5] These included a $64 million offering for a Hyatt Regency Hotel at Pittsburgh International Airport, issuances for golf courses in other counties, and financing for colleges, hospitals, and nursing homes throughout Pennsylvania (Tr. 884-86, 927-28, 936-37, 1401; DX 1). These project financings were so wide-ranging that the Authority even proposed to change its name to reflect the perceived breadth of its mission (RX 44, Minutes of Aug. 18, 1998, Meeting at 8 (adopting Resolution 19-98 and proposing to change DCGA's name to "General Authority of Pennsylvania"), Minutes of Oct. 20, 1998, Meeting at 6).

DCGA also encouraged Hummelstown, a borough in Dauphin County, to create its own authority to handle bond offerings that DCGA could not (DX 26 at 3; RX 44, Minutes of June

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[4] Act of May 2, 1945, 1945 P.L. 382, as amended, 53 P.S. §§ 301-322 (1998). The Municipality Authorities Act was repealed by an Act of June 19, 2001, 2001 P. L. 287, and has been reenacted in codified form as 53 Pa. Cons. Stat. §§ 5601-22 (2001). In this decision, all references to the Municipality Authorities Act will be as it existed during 1998.

[5] In project financing, payment is dependent on the ability of a single project to produce sufficient revenue to provide for maintenance and operation of the project itself while ensuring timely payment of debt service (DX 94 ¶ 8).

23, 1998, Executive Session at 1, Minutes of July 21, 1998, Meeting at 7-8, Minutes of Aug. 18, 1998, Meeting at 9). Under this proposal, DCGA would provide administrative staff and services to the Hummelstown General Authority, and it also agreed to pay for any start-up expenses the Hummelstown General Authority incurred (RX 44, Minutes of June 23, 1998, Executive Session at 1, Minutes of July 8, 1998, Meeting at 7 (short version)). Hummelstown's population is 4,360 (2000 census).

DCGA issued revenue bonds to finance two major projects in Dauphin County during 1998: Forum Place, the $75.35 million transaction that is the subject of the OIP, and Riverfront Office Center, the $45.4 million transaction that served as a model for the Forum Place disclosure document.

In mid-1998, the Dauphin County Commissioners began to rein in the Authority. In July 1998, the Commissioners instructed the Authority to "get out of the golf business" (DX 26 at 3). In the autumn of 1998, shortly after the closings on Riverfront Office Center and Forum Place, the Commissioners summoned DCGA's Board to a public meeting, at which the Commissioners expressed the views that certain projects undertaken by DCGA did not comply with the purpose the Commissioners believed DCGA should serve (RX 44, Minutes of Sept. 22, 1998, Meeting at 1-2, Minutes of Sept. 22, 1998, Executive Session, Minutes of Oct. 5, 1998, Special Meeting at 1-3). The Commissioners subsequently adopted Ordinances that significantly curtailed DCGA's powers (RX 44, Minutes of Oct. 20, 1998, Meeting at 6).[6]

The Capitol Associates Project, Riverfront
Office Center, and Forum Place

There were three bond offerings during 1998 in which public authorities acquired privately owned office buildings in Harrisburg for use by Commonwealth agencies and other governmental bodies. These transactions did not utilize general obligation bonds, backed by the full faith and credit of the issuer. Rather, they involved revenue bonds and repayment was limited to the stream of revenue generated by the buildings themselves. The transactions were based on negotiated sales, not competitive bids. Bradbury and Fowler were involved in all three transactions (DX 16, DX 18, DX 19).

[6] See Ordinance No. 5-1998 (Oct. 7, 1998) and Ordinance No. 6-1998 (Nov. 4, 1998), Confirming the Establishment of the Dauphin County General Authority and Identifying the Types of Projects to be Entertained (official notice). These Ordinances limited the projects that DCGA could entertain to those that would provide a direct benefit to the residents of Dauphin County. They also prohibited transactions involving any individual or any non-public or private sector organization, as well as those projects that would place the Authority in competition with the private sector without substantial spillover benefits to the residents of Dauphin County. The Ordinances permitted the Commissioners to prohibit transactions that would otherwise be authorized. Finally, the Ordinances directed DCGA to inform the Commissioners of all proposed projects on a regular basis, but at least quarterly.

An important issue in these transactions was the negotiation of a voluntary payment-in-lieu-of-taxation (PILOT), by which the acquiring authority would enter into a municipal services agreement with the host jurisdiction(s) (Tr. 749, 1305-06; RX 16 at 55, 58, 98, 120, 130). The PILOT agreements with respect to the Riverfront Office Center and Forum Place capped the Authority's annual payments to the host jurisdictions and subordinated the payments to operating expenses and debt service to bondholders (DX 16 at 14, DX 18 at 12). The absence of a PILOT agreement involving the Capitol Associates Project proved to be quite contentious.

Capitol Associates Project. Bradbury, like Fowler, shared an expansive understanding of the Municipality Authorities Act. The Capitol Associates Project illustrates how Bradbury generated demand for his underwriting services by promoting competition among local authorities.

Capitol Associates, a group of private developers, owned a 3.7 acre tract of land in Harrisburg (DX 19). The tract contains two three-story office buildings and a seven-story parking garage (DX 19). The office buildings house a variety of Commonwealth agencies (DX 19).

New Garden Township is located in Chester County, Pennsylvania (Tr. 673). It is near the Pennsylvania-Delaware border, approximately seventy-three miles from Harrisburg, and has a population of 9,083 (Mapquest; 2000 census). In 1997, Bradbury encouraged New Garden Township to form its own municipal authority, the New Garden General Authority, to purchase the Capitol Associates property in Harrisburg (Tr. 674).

However, the transaction did not occur. Once the Mayor of Harrisburg learned of New Garden General Authority's plan to acquire a commercial property in his city and remove it from the tax rolls, he denounced the scheme as a raid on his city's tax base by a sister jurisdiction (Tr. 675-77). Under the spotlight of adverse publicity, New Garden General Authority chose not to proceed (Tr. 675-76). In a defensive maneuver, the Mayor of Harrisburg then arranged for his own local authority, the Harrisburg Authority, to purchase the Capitol Associates Project from its private-sector owners (Tr. 677; DX 19; RX 16 at 24-25).

The Harrisburg Authority purchased the Capitol Associates Project in June 1998 for \$19.1 million and financed the purchase by issuing unrated, non-taxable revenue bonds (DX 19). As part of the purchase, the Harrisburg Authority agreed to pay a PILOT, to be split among three taxing jurisdictions: the City of Harrisburg, the Harrisburg School District, and Dauphin County (DX 19 at 13).

If New Garden General Authority had completed the purchase of the Capitol Associates Project, Bradbury expected that he would be the underwriter and Fowler would be the financial advisor (Tr. 674, 676-77). When the Harrisburg Authority purchased the Capitol Associates Project, Bradbury was co-underwriter and Fowler was co-financial advisor (Tr. 877-78; DX 19 at 3). The political tempest surrounding New Garden's unsuccessful effort to acquire the Capitol Associates Project created a stampede mentality at DCGA. Members of DCGA began to think: if we do not finance a project, some other authority will finance it and deny Dauphin County a PILOT (Tr. 51, 672-73, 1303-06).

Riverfront Office Center. In June 1998, DCGA purchased Riverfront Office Center from a private owner (DX 18). Riverfront Office Center consists of 19.11 acres of land in Harrisburg, a five-story office building with 365,000 square feet of space, and parking for 1,230 vehicles (DX 18). Before the purchase, the private owner had negotiated leases for office space with the Commonwealth. At closing, the seller assigned the leases to the Authority. DCGA intended to operate the Riverfront Office Center for the public purpose of leasing space to departments and agencies of the Commonwealth or other governmental units (DX 18). DCGA financed the purchase through the public offer and sale of $45.3 million in unrated, non-taxable revenue bonds.

Forum Place. In July 1998, DCGA purchased Forum Place from another private owner, John O. Vartan (Vartan), trustee of the Musalair Trust (Tr. 84; DX 16 at 6; RX 31). Forum Place consists of approximately 2.2 acres of land with a nine-story office building and two below-grade parking levels at Fifth and Walnut Streets in Harrisburg (DX 4 at PW 179, 189, DX 16 at 6). The building contains approximately 376,000 square feet of net leasable office space and a parking garage for approximately 1,090 vehicles (DX 4 at PW 189, DX 16 at 6). Forum Place is located in downtown Harrisburg and is adjacent to the Capitol Complex (DX 4 at PW 187). The location is very convenient and desirable for Commonwealth agencies.

Vartan is a well-known builder, owner, and property manager in the Harrisburg area. He completed construction of Forum Place in 1996 (Tr. 1460). He also negotiated several leases for office space at Forum Place with the Commonwealth and the United States Social Security Administration (DX 16 at 13). By mid-1998, approximately 375,500 square feet of the total net leasable space in the office building was occupied (DX 16 at 13). Terms of the current office leases ran from two to ten years, with various renewal options (DX 16 at 13). Terms of the current parking leases ran from three to eight years (DX 16 at 13). The anchor tenant at Forum Place was the Commonwealth's Department of Transportation (PennDOT) (DX 16, Appendix C).

As with the Riverfront Office Center, DCGA intended to operate Forum Place for the public purpose of leasing space to departments and agencies of the Commonwealth or other governmental units (DX 16). DCGA financed the purchase through the public offer and sale of unrated, non-taxable revenue bonds. The Forum Place offering consisted of $72.25 million Office and Parking Revenue Bonds, Series A of 1998, and $3.1 million Subordinated Office and Parking Revenue Bonds, Series B of 1998. The offering also included $10.9 million of Subordinated Office and Parking Revenue Bonds, Series C of 1998. However, the Series C bonds were not sold publicly and are not the subject of this proceeding.

DCGA's purposes were not entirely altruistic. The Authority stood to earn a fee of $125,000 upon closing the Forum Place transaction (DX 13 at 2, DX 24 at 4-5). In addition, Fowler expected the cash flow at Forum Place to generate an annual surplus of up to $250,000, which would accrue to the Authority (DX 13 at 8, DX 24 at 5). Under the Municipality Authorities Act, an authority has the express power to acquire, hold, and lease "buildings to be devoted wholly or partially for public uses . . . and for revenue-producing purposes." 53 P.S. § 306A(a)(2).

B. The Demand for Leased Office Space in Harrisburg by Qualified Tenants.

Because Interest on the Forum Place Bonds Is
Not Taxable, Only the Demand From
Qualified Tenants Is Relevant Here

Section 103(a) of the Internal Revenue Code (Code) excludes from a taxpayer's gross income interest received on state or local bonds. The general rule in Section 103(a) of the Code is subject to several exceptions listed in Section 103(b), including an exception for private activity bonds, as defined in Section 141 of the Code.

The Forum Place bonds initially qualified as non-taxable under Section 103 of the Code (DX 16 at 16-17, DX 28). DCGA pledged to preserve the non-taxable status of interest on the bonds throughout the life of the bonds (DX 16 at 17). This, in turn, required that at least 90% of Forum Place be leased exclusively by state or local governmental entities. Under the common terms of public finance, at least 90% of Forum Place's value had to be "good use," i.e., use by state and local government entities, and not more than 10% could be "bad use," i.e., use by any other entities or individuals. Use by the federal government, individuals, private for-profit entities, and private not-for-profit entities would all be "bad use" that could cause the retroactive loss of the bonds' non-taxable status if it collectively exceeded the 10% cap (DX 94 ¶ 9; RX 44, Minutes of June 19, 1998, Meeting at 4-5).

Thus, if the Forum Place bondholders were to receive tax-free interest payments over the life of the bonds, the tenants of 90% of the space would have to be state or local government entities. In attracting such tenants, Forum Place would face competition from other commercial office buildings in Harrisburg. However, the Authority could not lease more than a small amount of space at Forum Place to entities other than state and local governments without threatening the non-taxable status of the bonds (DX 94 ¶¶ 10, 51.c, 58).

Dauphin County Had Already Satisfied Its
Own Demand for Leased Office Space

Fowler suggested that Dauphin County needed additional office space in 1998, and that Forum Place might satisfy that need (Tr. 930, 1009-1011). This suggestion lacks record support. There is no evidence that Dauphin County had a large number of employees (DX 4 at PW 252, 254). Moreover, by February 1998, Dauphin County had announced that it would acquire another office building in Harrisburg, known as 100 Chestnut Street (RX 22). In September 1998, DCGA finalized the purchase of 100 Chestnut Street (DX 1; RX 44, Minutes of May 19, 1998, Meeting at 15, Minutes of June 19, 1998, Meeting at 4-5). Dauphin County expected to use 70% to 75% of the space at 100 Chestnut Street for its own employees by 2000 or 2001 (RX 44, Minutes of June 19, 1998, Meeting at 4-5, Minutes of Sept. 10, 1998, Meeting at 2). I find as a fact that Dauphin County had no need to lease a significant amount of additional office space in 1998 or later. Realistically, the only qualified tenant that might lease a large block of office space at Forum Place was the Commonwealth.

How the Commonwealth
Leases Office Space

At all relevant times, the Commonwealth leased a greater proportion of its office space than many other state governments (DX 91 at 23). As of August 1998, the Commonwealth satisfied 54% of its demand for office space in the Harrisburg area with leased space (DX 91 at 16).

The Commonwealth's Department of General Services (DGS) serves as the leasing agent, real estate agent, or tenant representative for most of the Commonwealth's agencies (Tr. 171, 915, 1606). When an agency determines that it needs additional office space in a building not owned by the Commonwealth, it advises DGS of its needs and the agency and DGS jointly prepare a requirements statement (Tr. 157, 1606). DGS then issues a Request for Proposals (RFP) and advertises it to the public (Tr. 157, 170, 1606; RX 16 at 40). Thereafter, DGS reviews the responses to the RFP (Tr. 1606). DGS's Bureau of Real Estate analyzes the economic aspects of the proposals received from bidders and creates a short list of the proposals that offer acceptable rental rates (Tr. 1606-07). DGS then forwards the short list of bidders to the requesting agency, and that agency determines which submission to accept (Tr. 1607-08).

After the requesting agency makes its selection, DGS prepares a lease and the Secretary of DGS executes it on behalf of the Commonwealth (Tr. 1607, 1610-11, 1629; DX 92 at 19). The lease is then submitted for approval to the Board of Commissioners of Public Grounds and Buildings, comprised of the Governor and the Treasurer (Tr. 157; DX 92 at 19; RX 16 at 40-41).[7]

If an agency vacates a leased space with time remaining on the lease, DGS tries to find another Commonwealth entity to replace it (Tr. 1611). As a general matter, the Commonwealth does not enter into leases lasting more than ten years (Tr. 912; DX 94 ¶ 8).

Gary Crowell (Crowell) served as Secretary of DGS from January 1995 to July 2001 (Tr. 155, 169). In that position, he was responsible for renovating Commonwealth-owned buildings and leasing real estate not owned by the Commonwealth (DX 65 ¶ 3). Crowell reported directly to then-Governor Thomas Ridge (Tr. 124, 169, 202).

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[7] OIP ¶ III.E.1 alleges that "PennDOT entered into a lease" for office space at Forum Place. This is inaccurate. The Commonwealth, not the individual agency, signed the lease (DX 92). Paragraph 1 of the lease clearly set forth that the space at Forum Place was "for use by the Department of Transportation <u>or</u> <u>other</u> <u>agency</u> of the Commonwealth" (DX 92 at 1) (emphasis added). Other Commonwealth leases did not contain language identifying alternate occupants (DX 16, Appendix C, Model Lease) ("for use by the Department of Labor & Industry").

PennDOT's Demand for Office
Space in Harrisburg: 1995 to 1998

Until the mid-1990s, most of PennDOT's employees in Harrisburg maintained offices in the Commonwealth-owned Transportation & Safety (T&S) Building (Tr. 156). In 1994, a fire destroyed several floors at the T&S Building (Tr. 156-57). The fire, coupled with ongoing environmental problems (asbestos, PCBs, dioxins), resulted in a decision by Crowell, the then-Secretary of DGS, and Brad Mallory, the then-Secretary of Transportation, to remove PennDOT's employees from the T&S Building and find them suitable facilities elsewhere (Tr. 156-57).

In 1995, DGS issued an RFP for temporary facilities for the occupants of the T&S Building (Tr. 157). At the time of the RFP, the Commonwealth had not yet decided whether to reconstruct the damaged T&S Building, or to tear it down and replace it with a new building (RX 16 at 47-48). By January 1996, however, DGS made a public announcement that the damaged T&S Building would be gutted, demolished, and replaced with a new structure, to be named the Keystone Building (Tr. 179, 187-89).[8]

In October 1995, the Commonwealth and Vartan signed a lease for 284,142 net usable square feet of office space at Forum Place for some of PennDOT's administrative employees (Tr. 171; DX 92). At the time, Forum Place was still under construction. The term of the lease was sixty-one and one-half months and the Commonwealth had an option to renew for one additional year (Tr. 158, 192; DX 92). The Commonwealth always intended to move PennDOT's employees out of Forum Place once renovations to or replacement of the T&S Building could be completed (Tr. 158, 192, 908; RX 16 at 47-49). Vartan needed one year to complete the construction of Forum Place, and PennDOT's administrative employees moved in during October 1996 (Tr. 157-58; DX 16, Appendix C; RX 16 at 47). The Commonwealth's five-year lease on space for PennDOT thus expired in November 2001 (DX 16, Appendix C).

In June 1996, the Commonwealth also leased 226,104 net usable square feet of office space at Riverfront Office Center for PennDOT's Department of Motor Vehicles and Licenses (Tr. 184; DX 18, Appendix C). In contrast to the Forum Place lease, the term of the lease at Riverfront was ten years with two five-year options for renewal (Tr. 159, 908; DX 18, Appendix C). The Commonwealth had no plans to move any PennDOT employees from Riverfront to the Keystone Building (Tr. 105, 159-60, 924).

By July 1998, PennDOT occupied 299,000 square feet of office space at Forum Place (DX 16, Appendix C). This lease accounted for approximately 79% of the office space in Forum Place and generated approximately 60% of Forum Place's total lease revenues (DX 16, Appendix C, DX 57).

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[8] The proposed Keystone Building would offer 845,000 square feet of office space, some 105,000 square feet more than its predecessor (Tr. 163-64; RX 22). The Keystone Building was intended to house not only some of PennDOT's employees, but also the employees of several other Commonwealth agencies (DX 91 at 15; RX 22).

Crowell's Early Representations
About the Commonwealth's Demand for
"Swing Space" at Forum Place

Before Vartan leased office space to the Commonwealth in October 1995, he wanted to determine if Forum Place would remain on a sound financial footing after PennDOT moved out (RX 16 at 44-45). Crowell and George Manakos (Manakos), then-Director of DGS's Bureau of Real Estate, informed Vartan that the Commonwealth had embarked on a renovation program of all the buildings in the Capitol Complex (RX 16 at 39-40, 42-43, 48). Crowell and Manakos told Vartan that the Commonwealth would utilize all of the PennDOT space at Forum Place as "swing space" for other agencies during the renovation program (RX 16 at 48, 50-52).[9] As evidence of the Commonwealth's intentions, Crowell and Manakos advised Vartan that DGS would leave office furniture in Forum Place once PennDOT left, so that the vacant space would be ready for immediate occupancy by the next agency (RX 16 at 51). Vartan never received anything in writing from Crowell or Manakos, but he believed them (RX 16 at 51-52).

Approximately two and one-half years later, Crowell was reported to have made similar statements to the media. See Jack Sherzer, "State Lease Study Spurs City Fears," Harrisburg Patriot News at B1 (Feb. 15, 1998) (RX 22). According to the newspaper article, the Commonwealth had commissioned a Master Space Plan that would, among other things, study whether the Commonwealth should change the way it leased office space around Harrisburg. Some local officials were concerned that the Commonwealth might "abandon or not renew leases for office space in privately owned buildings in the city" (RX 22). As an illustration, the article noted that the planned Keystone Building would be owned by the Commonwealth. However, comments that the article attributed to Crowell dampened some of these concerns. In relevant part, the article stated:

> After the PennDOT offices leave Forum Place, Crowell said, the state will still likely use that building as "swing space" to house a variety of agencies that will be temporarily dislocated as the state continues to renovate Capitol Complex buildings.
>
> In fact, [Crowell] said, the study also will examine whether the state should ask developer John O. Vartan, owner of Forum Place, to add space to that building.

The article went on to observe that the Mayor of Harrisburg would also encourage the Commonwealth to "increase its use of Forum Place" (RX 22).

At the hearing, Crowell intimated that he might have been misquoted in the newspaper article (Tr. 182). I reject this suggestion. First, neither Crowell nor his press secretary complained to the newspaper at the time of publication (Tr. 215-16). Second, the comments

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[9] As used in this decision, "swing space" refers to flexible, vacant office space available for assignment to Commonwealth agencies or departments in need of temporary relocation.

attributed to Crowell in the February 1998 article are quite similar to those that Vartan attributed to Crowell in 1995. However, I find that Crowell never committed to using "swing space" at Forum Place for a fixed period of time, either in 1995 or in February 1998.

PennDOT's Intent to Move to
The Keystone Building

A critical issue in this proceeding is what was known in June and July 1998 about PennDOT's eventual move to the Keystone Building. The OIP repeatedly refers to PennDOT's "scheduled move" (OIP ¶¶ III.E.4, E.6, E.11, E.12). The date of the move was not, in fact, "scheduled" as of July 1998. The Commonwealth's intent to move PennDOT involved a planned action on an uncertain date to an unconstructed building. It is more appropriate to refer to PennDOT's "anticipated move" or "intended move."

As noted, the fire-damaged T&S Building had environmental problems (Tr. 156-57, 190). Therefore, the original demolition/construction schedule was unexpectedly and substantially delayed while the building was depleted of asbestos and PCBs. An environmental lawsuit then further delayed the Keystone Building project. By July 1998, the T&S Building was still standing and site preparation had not even begun for the new Keystone Building (Tr. 156, 190-92). Bradbury knew that there was a construction schedule for the Keystone Building, but he did not inquire into the status of that schedule while he was marketing the Forum Place bonds (Tr. 689-90).[10]

On August 1, 1998, the T&S Building was imploded (Tr. 107, 192, 1497-98, 1571). Plans for the implosion were well publicized in the Harrisburg area for months in advance (Tr. 188-89, 925).

The Keystone Building was constructed on a fast track (Tr. 161-62, 192).[11] PennDOT moved most of its administrative personnel from Forum Place to the Keystone Building in late 2000 (Tr. 158-59, 213). PennDOT vacated 257,140 net usable square feet of space at Forum

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[10] The Settlement Order in Dauphin Co. Gen. Auth., 82 SEC Docket at 2886, finds that the Commonwealth awarded contracts for demolition, construction management, and building design for the Keystone Building in September 1996, and that site preparation and demolition activities began at the T&S Building in January 1997. There is no such evidence in this record, and the findings in the Settlement Order are not binding on the parties to this proceeding. Id. at 2885 n.1.

[11] The OIP alleges that the target date for completion of the Keystone Building was "late 2001" (OIP ¶ III.E.2). A newspaper reporter thought this to be the case (RX 22). However, the free-floating phrase in the newspaper article does not inform the reader as to who, other than the reporter, might have shared the view that "fall 2001" was the "expected completion date." Cf. Young v. Community Nutrition Inst., 476 U.S. 974, 980-81 (1986) ("As enemies of the dangling participle well know, the English language does not always force a writer to specify which of two possible objects is the one to which a modifying phrase relates.").

Place, but left behind some of its computer operations (DX 91 at 5; RX 25 at 15, RX 37 at 11). PennDOT also left behind its furniture, fixtures, and equipment for the next agency expected to move into Forum Place (Tr. 201, 215, 786).[12] The Commonwealth continued to make lease payments to Forum Place for the vacated PennDOT space through November 15, 2001, the end of the five-year lease (Tr. 213).

The Commonwealth's plan to move PennDOT's employees from Forum Place to the new Keystone Building, once that building was ready to be occupied, was publicly available information in the Harrisburg area in mid-1998 (Tr. 32-33, 44-45, 93, 111-12, 146, 179, 189, 218-19, 786, 789, 1410-11; DX 24 at 4-5, DX 101). The information was not widely known outside the Harrisburg area at the time (Tr. 225, 309, 1204-05, 1233, 1468; DX 68, DX 69, DX 101).

C. The Sell Side of the Forum Place Bond Offering.

1. Chronology of the Transaction.

Origins of DCGA's Purchase
of Forum Place From Vartan

In March 1998, the Authority and Vartan began to discuss the purchase of Forum Place. There is conflicting evidence about which side initiated the transaction. However, it is undisputed that discussions began approximately two weeks after publication of the February 15, 1998, article in the Harrisburg Patriot News (RX 22).

According to Fowler, Vartan initiated the transaction (Tr. 890). By early March 1998, "word had gotten out" that the Harrisburg Authority was going to purchase the Capitol Associates Project (Tr. 887; DX 3). Once Vartan learned that the private owners of Capitol Associates were selling their buildings, he asked Fowler if DCGA would be interested in buying Forum Place (Tr. 887-90). Fowler maintained that Vartan was unwilling to approach the Harrisburg Authority for political reasons (Tr. 888). Fowler relayed Vartan's overture to Ricci and Reese, who were willing to explore the matter with Vartan (Tr. 888-89, 1304; DX 3).

According to Vartan, DCGA initiated the transaction (RX 16 at 53-56). Reese, the Authority's executive director, contacted Vartan to inform him that the Harrisburg Authority was going to purchase the Capitol Associates Project. Reese also told Vartan that DCGA did not want Vartan to sell Forum Place to the Harrisburg Authority. Reese encouraged Vartan to sell Forum Place to DCGA, so that Dauphin County, not the City of Harrisburg, could control the

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[12] The parties draw competing inferences from the fact that PennDOT left behind its furniture, fixtures, and equipment. To D&B and Bradbury, this was a significant indicator of the Commonwealth's intent to continue to use space at Forum Place in the future (RX 41 ¶ 269). To the Division, it was a clever tactic on the part of the Commonwealth to avoid paying furniture storage charges (Div. Prop. Find. # 202). Respondents' interpretation finds significant support in Crowell's 1995 representations to Vartan. The Division's interpretation lacks record support.

PILOT (RX 16 at 56, 58, 120, 130). Reese asked Vartan to contact Fowler, who was "putting the numbers together" for DCGA (RX 16 at 56).

To the extent that these two accounts cannot be harmonized, I accept Vartan's explanation as the more complete. Before March 1998, Vartan had not spoken with Fowler in years and had never conducted business with DCGA (RX 16 at 31-32, 56). Vartan did not need to sell Forum Place (RX 16 at 74). Moreover, if Vartan were to sell Forum Place, he did not care who the buyer was, as long as the buyer met his asking price (RX 16 at 59, 120, 128-29). Kristin Milke (Milke) and Ricci, both members of DCGA in 1998, agreed with Bradbury that keeping control of the PILOT was a factor in the Authority's decision to proceed (Tr. 51, 673, 1305-06).

Fowler, Ricci, Reese, and others met with Vartan to discuss Forum Place throughout March and April 1998 (Tr. 889; DX 3; RX 16 at 57-59). Fowler presented his preliminary findings to the Authority on April 3 and April 21, 1998, and received permission to continue with his evaluation (Tr. 889, 892-96; DX 3, DX 5).

As early as April 1998, the Authority and Fowler were concerned about what would happen to Forum Place once PennDOT moved out (Tr. 908-09). At that time, Fowler recognized the issue as a hurdle for the prospective bondholders, as well as the Authority (Tr. 910-11).

The Finance Team

Fowler recommended the underwriter and bond counsel to the Authority (Tr. 14-15, 1408). Bradbury was not involved in negotiating the purchase price of Forum Place with Vartan or in presenting the purchase proposal to the Authority (Tr. 677-78, 720, 729, 976-78). He first learned of the Forum Place project from Fowler, after the Authority had decided to proceed (Tr. 753, 977-78). In their first discussion, Fowler asked Bradbury preliminary questions about likely interest rates, debt service, reserve requirements, and the probable cost of issuing the bonds (Tr. 901-02).

DCGA retained Pepper Hamilton LLP (Pepper Hamilton) as its bond counsel on the Forum Place transaction (Tr. 15; DX 16 at 3, DX 24 at 8). David W. Sweet (Sweet), a former Pennsylvania state legislator and a partner in Pepper Hamilton's Harrisburg office, served as the lead attorney (Tr. 53-54, 62-63, 66-67; RX 16 at 37). Pepper Hamilton, through Sweet and others, had also been involved in the late stages of negotiations between DCGA and Vartan over the purchase price of Forum Place and related real estate issues (Tr. 15, 898, 902-04, 906; RX 16 at 57, 59-60, 64-65, 72-74, RX 30). Sweet, whose practice also involved lobbying activities, offered to act as a liaison with the Commonwealth (Tr. 54, 345, 368, 687, 943, 956-57). Sweet also drafted some of the language in the offering document and signed Pepper Hamilton's supplemental opinion letter at closing (Tr. 69-70, 113; DX 28).

D&B retained Lamb, Windle & McErlane, P.C. (LWM), a law firm in West Chester, Pennsylvania, to serve as underwriter's counsel (Tr. 338, 373-74, 1275; DX 16 at 3, DX 20). LWM concentrates its practice in municipal finance (Tr. 1271, 1274). Thomas J. O'Neill (O'Neill) served as the principal lawyer at LWM with respect to the Forum Place transaction (Tr. 1275-76). O'Neill wrote the bond purchase agreement and prepared drafts of the Preliminary

Offering Statement (POS) and OS (Tr. 355, 375-76). James McErlane (McErlane), O'Neill's law partner, served as a reviewer and took over the assignment while O'Neill was on his summer vacation (Tr. 358, 385, 1276; DX 30, DX 40).

These members of the finance team were well acquainted with each other. D&B had extensive experience in underwriting bond offerings for DCGA (Tr. 744-45). Bradbury had known Fowler since the early 1980s and he first did business with PFC in 1989 (Tr. 710-11, 753). Bradbury had known O'Neill for a long time, as well (Tr. 756). Sweet had known Fowler since approximately 1990 and had worked on several transactions with PFC (Tr. 63-65). Sweet had known Bradbury for several years and Pepper Hamilton had done business with Bradbury for even longer (Tr. 109-10). Sweet and O'Neill had been law partners at one time and were also social friends (Tr. 79-80, 342, 1281). O'Neill had known Fowler for thirty years (Tr. 342). He had worked on more than one hundred transactions with D&B, one dozen transactions with PFC, and three or four transactions with DCGA (Tr. 343). McErlane has known Bradbury as a client and a friend for more than twenty-five years (Tr. 756, 1272-73).

The final member of the finance team was Neil Hendershot (Hendershot), an attorney with the Harrisburg law firm of Goldberg, Katzman & Shipman, P.C. (GKS) (Tr. 26-27, 83, 780, 1645). GKS, through Hendershot, served as the Authority's solicitor from 1984 to February 2000 (Tr. 1645). Hendershot or another representative of GKS regularly attended the Authority's meetings (Tr. 1646; DX 24-DX 26). Hendershot signed an opinion letter from GKS to the underwriter and bond counsel at closing, as required by the bond purchase agreement (Tr. 798-99; RX 31 at 5-6).

O'Neill's First Draft of the POS

Pepper Hamilton was serving as underwriter's counsel to D&B on the Riverfront Office Center project in June 1998 (DX 18 at 3). LWM was not involved in that transaction. On June 16, 1998, Sweet sent O'Neill a computer disc containing the Riverfront POS and related documents to use as a guide for the Forum Place POS (Tr. 73-75, 113-14, 374-75, 1275-76; DX 30).

On June 22, 1998, Bradbury, Sweet, and O'Neill discussed the Forum Place offering by telephone (Tr. 344, 756-58; DX 20). At the hearing, Sweet and O'Neill claimed that they could not recall the specifics of this conversation (Tr. 79, 346-47, 349). During his investigative testimony, O'Neill's recollection was considerably more precise. O'Neill's investigative testimony explained that he learned that Forum Place was the third transaction of its type (after Riverfront and Capitol Associates) and that Bradbury had already lined up interested buyers for the Forum Place bonds (Tr. 344-47) ("it was described to me as sort of a done deal"). During his investigative testimony, O'Neill also recalled that the computer disc came with an explanation that the Forum Place project had "a tight time frame," that "they needed a [draft POS] quickly," and that using the Riverfront POS "would save a lot of time" (Tr. 347, 349). Bradbury did not remember saying that Forum Place was a "done deal," but otherwise he did not contradict O'Neill's investigative testimony (Tr. 727-28). I credit O'Neill's investigative testimony and I give little weight to the hearing testimony of Sweet and Bradbury on these points.

At O'Neill's request, Fowler provided O'Neill with copies of the Forum Place tenant leases (Tr. 367, 954, 1011). O'Neill may have had other conversations with Fowler, but he could not remember the subjects discussed (Tr. 366, 390).

O'Neill used the Riverfront POS as a model for drafting the Forum Place POS. He did not know if there were any distinctions between the two transactions and he assumed that there were none (Tr. 395-96).[13] As a result, the disclosure portions of the Forum Place POS are almost identical to the comparable portions of the Riverfront offering document (Tr. 381, 384; DX 18, DX 33, DX 40, DX 87).

On or about June 26, O'Neill circulated a first draft of the POS for comments (Tr. 357).[14] Bradbury and Sweet reviewed the draft and offered suggestions (Tr. 114, 704-05, 759, 784; DX 31). Fowler knew that the Authority was relying on him to review the OS (Tr. 920). He was aggravated that he had to read a facsimile copy (Tr. 917). He considered the Forum Place POS to be a "knockoff" of the Riverfront POS and "didn't read it line-by-line" (Tr. 918). I find little record support for the allegation that "Fowler substantially participated in drafting the [OS]" (OIP ¶ III.D.4).

Fowler, Sweet, and Reese Meet
with Crowell on June 30, 1998

On June 30, 1998, Fowler, Sweet, and Reese met with Crowell (Tr. 123, 126-27, 929-30, 958; DX 3).[15] Fowler, Sweet, and Crowell agreed that the primary purpose of the meeting was to discuss the Commonwealth's long-range plans for leasing office space in Harrisburg, and specifically, to ascertain the Commonwealth's plans for leasing space at Forum Place after PennDOT moved to the Keystone Building (Tr. 95-96, 99, 126, 161, 194, 931; DX 65 ¶ 5). Fowler and Sweet testified that another purpose of the meeting was to determine if the Commonwealth was satisfied with Vartan's management of Forum Place (Tr. 95-96, 125-26, 931; DX 3). Fowler testified that the meeting also presented an opportunity to confirm the expense figures that Vartan had provided for Forum Place, and to make sure that the

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[13] This assumption was completely unwarranted. PennDOT's motor vehicle and licensing arm intended to stay in the Riverfront Office Center for the long term (Tr. 159-60, 924). For that reason, the Commonwealth signed a ten-year lease with two five-year renewal options at Riverfront. In contrast, PennDOT's administrative personnel intended to stay at Forum Place only until the Keystone Building was completed (Tr. 158). For that reason, the Commonwealth signed a five-year lease with a one-year renewal option at Forum Place (Tr. 158, 192, 908; DX 92).

[14] Robert D. Pope (Pope), the Division's expert witness, explained that lengthy meetings, in which a POS is reviewed page-by-page, are common (DX 94 ¶ 24). Pope characterized the review process here as a highly abbreviated version of the common approach (DX 94 ¶ 23).

[15] Neither Bradbury, the underwriter, nor O'Neill, the underwriter's counsel, attended the June 30, 1998, meeting (Tr. 354, 680).

Commonwealth's demand for leased space had not changed in the four months after publication of the February 15, 1998, newspaper article (Tr. 931, 958). As of June 30, the Authority had not yet purchased Forum Place, and it still had time to withdraw from the transaction if circumstances warranted (Tr. 933).

The participants in the meeting agreed that Crowell gave his best judgment about what the future would bring and shared his knowledge about pending projects (Tr. 96-97; DX 65 ¶ 5). It is undisputed that Crowell never offered any commitments, assurances, or guarantees that the Commonwealth would continue to lease space at Forum Place after PennDOT's departure (Tr. 97, 128-29, 915; DX 65 ¶ 5). Nor is there a dispute that Crowell was reasonably happy with Vartan's management of Forum Place (Tr. 96-97, 125-26). Beyond these basic points, the participants' accounts of the meeting diverge widely on the specifics.

According to Fowler, Crowell outlined "a whole litany" of "all the buildings in the Capitol Complex" that needed renovation, explained that such renovations would be phased in over time, and estimated that it would take the Commonwealth three to four years per building (Tr. 932-33). Fowler quoted Crowell as saying that the Commonwealth would continue to use Forum Place as swing space for the next fifteen to twenty years (Tr. 932). Fowler took "a tremendous amount of comfort" from Crowell's words and concluded that there was a "reasonable likelihood" that the Commonwealth would continue to use Forum Place (Tr. 930, 959).

Before the meeting, Fowler had made a note to obtain a letter from Crowell about the Commonwealth's plans, if any, to use Forum Place after PennDOT's departure (DX 6). Crowell never provided such a letter (Tr. 939-42, 944). I do not agree with the Division that there is significance to this point. Vartan never received anything in writing from Crowell in 1995.

Sweet testified that Crowell described a series of "fairly extensive" renovation projects in Commonwealth-owned office buildings that would last five to ten years (Tr. 129). Sweet said that Crowell described the Commonwealth's need for swing space during this period of renovation, repair, and upgrading (Tr. 96). According to Sweet, Crowell stated that Forum Place would be ideal for such swing space, because of its very convenient location (Tr. 128). Finally, Sweet quoted Crowell as stating that the Commonwealth was still in a "growth mode," in terms of its demand for office space (Tr. 96). When Sweet left the meeting, he took "some comfort" from the fact that Crowell had not identified any "huge negative" to proceeding with the bond offering (Tr. 128).

Crowell's testimony left the impression that he was much vaguer at the meeting about the Commonwealth's intent to use Forum Place as swing space. According to Crowell, the Commonwealth had already completed a significant number of capital improvements in the Capitol Complex and was actually retracting from the marketplace for leased office space in the summer of 1998 (Tr. 162, 165). The only remaining renovations under consideration at the time involved two buildings, the Finance Building and the Forum Building. Neither of those was a high priority (Tr. 162, 186; DX 65). Crowell also testified that, if the Commonwealth did need swing space during a period of renovation and repair, it would look first to buildings it already owned and second to privately owned buildings (Tr. 163-64).

Crowell scoffed at the notion that it would take the Commonwealth fifteen to twenty years to renovate the Finance Building and the Forum Building (Tr. 200). He could see the possibility of using Forum Place as swing space for the remainder of the original term of the PennDOT lease, as well as for the additional one-year option period (Tr. 164-65, 196-97). Otherwise, the Commonwealth would have to issue a new RFP for swing space (Tr. 164-65). Crowell confirmed that PennDOT would leave behind desks, chairs, and partitions when it vacated Forum Place (Tr. 201, 215).

Crowell testified that he also discussed PennDOT's long-term plans for space leased in the Riverfront Office Building during the June 30 meeting (Tr. 159, 161). He noted that, if the Commonwealth exercised one or both of its options under the Riverfront lease, PennDOT could occupy the Riverfront Office Building for another fifteen to twenty years (Tr. 159, 161). In contrast, Fowler could not recall whether the subject of Riverfront ever came up at the meeting (Tr. 939).

The record is inconclusive as to what really happened at this meeting. There are no notes or written summaries. Fowler gave the broadest possible interpretation to Crowell's words, while Crowell gave the narrowest possible interpretation. Sweet was somewhere in the middle. However, I find that Fowler and Sweet understood that the Commonwealth could choose not to continue to lease space at Forum Place under future leases.

July 1-July 7, 1998

Fowler purportedly told Bradbury about the results of the June 30 meeting (Tr. 680, 694, 786, 964). However, Bradbury did not know how long the swing space program would last (Tr. 716). No member of the finance team told O'Neill or McErlane about the June 30 meeting or about PennDOT's plan to move out of Forum Place once the Keystone Building was completed (Tr. 116, 353-54, 368, 378, 920, 1014, 1282).

On July 7, O'Neill sent the first half of the revised POS and a draft purchase contract to Sweet for distribution to the Authority at its July 8 meeting (Tr. 358-59; DX 40).

July 8, 1998, DCGA Meeting

On July 8, the Authority conducted a public meeting that was attended by the Authority's members, Reese, Fowler, Sweet, and a lawyer from Hendershot's office (DX 24, DX 25).[16] Agenda items that day included approval of the Authority's purchase of Forum Place from Vartan, approval of the bond purchase contract with D&B, approval of the POS, and other related matters (DX 24 at 4-8, DX 25 at 3-6, DX 26 at 1-2).

[16] Bradbury, O'Neill, and Hendershot did not attend the July 8 meeting (Tr. 359, 1646-48; DX 24, DX 25).

At the meeting, there was a discussion that PennDOT would be leaving Forum Place and moving into the Keystone Building, once it was completed (Tr. 21-22; DX 24 at 5). Fowler also advised the Authority that he, Sweet, and Reese recently met with Crowell and that Crowell told them that the Commonwealth might use Forum Place as swing space for fifteen or twenty years (Tr. 20-22, 34, 961-63; DX 24 at 5, DX 26 at 1). Both Sweet and Reese remained silent as Fowler described to the Authority what had happened at the meeting with Crowell (Tr. 960, 962-63). Disclosure of PennDOT's intended move in the POS was not addressed during the July 8 meeting (Tr. 920, 954).[17]

PFC also prepared financial projections of anticipated tenant revenues at Forum Place through 2008 (Tr. 948-50; DX 13). Fowler presented these projections to the Authority to assure it that the future cash flow at Forum Place would be sufficient to service the debt and eventually retire the bonds (Tr. 948-50). Fowler further advised the Authority that D&B had sold all but $13 million of the bonds as of July 8 (DX 24 at 6).[18]

The Authority voted to approve the purchase of Forum Place and proceed with the bond offering (DX 24, DX 25) (Resolution 15-98). It reaffirmed the appointment of bond counsel and the financial advisor, and approved the appointment of the other professionals involved with the project (DX 24 at 8). The Authority also approved the content of the POS and authorized its distribution (DX 24, DX 25).

The members of the Authority did not actually read the POS page-by-page (Tr. 22-23, 946-47). Rather, they relied on the solicitor, bond counsel, and the financial advisor to review it for them (Tr. 22-23, 25-26, 36-37, 1408-09). There is no evidence that the Authority voted to approve the distribution of the financial projections to prospective investors.

There are two versions of the minutes of the July 8 meeting: DX 24 (long version, unsigned) and DX 25 (short version, signed). The differences between the versions are of two sorts. First, DX 24 shows Sweet as an active participant, making several comments during the meeting. In contrast, DX 25 omits most of Sweet's comments.[19] Second, DX 24 provides an

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[17] At a subsequent meeting, Fowler "indicated" or "represented" that the bondholders were taking the risk that Forum Place would remain full and that the Commonwealth would continue to use the vacated PennDOT space for other agencies as the Commonwealth conducted renovations (Tr. 953-54; RX 44, Minutes of Sept. 22, 1998, Executive Session at 2).

[18] This was an exaggeration, or at least imprecision, on Fowler's part. D&B may have received non-binding indications of interest from prospective investors, but the bonds were not D&B's to sell until the Authority executed the bond purchase agreement on July 8 (RX 31). Even at that juncture, the terms of the sale were generally known, but not final (Tr. 783-84).

[19] At the hearing, Sweet was unable to recall if the July 8 meeting included any discussion of the June 30 meeting with Crowell (Tr. 103-04, 139). He was also unable to recall the specifics of Fowler's presentation to the Authority (Tr. 131). Finally, Sweet was unable to remember the extent of his own remarks at the July 8 meeting (Tr. 104).

extensive summary of Fowler's comments regarding PennDOT's anticipated move and the information Fowler, Sweet, and Reese purportedly gained from their June 30 meeting with Crowell. DX 25 omits all of Fowler's comments on these subjects.

An Authority member and a memorandum prepared by a lawyer in Hendershot's office confirm that Fowler's discussion occurred at the July 8 meeting (Tr. 28, 41-42; DX 26 at 1-2). I find as a fact that the more complete and accurate minutes of what actually took place at the July 8 meeting is DX 24 (the unsigned long version) and not DX 25 (the signed short version).

After the July 8 meeting, McErlane finalized the OS. He added a more detailed summary of the tenant leases, including their expiration dates, to Appendix C (Tr. 384-86, 1277-80; DX 15, DX 16). The final version of the OS is dated July 17, 1998 (DX 16).

July 31, 1998, Closing

Closing on the Forum Place transaction took place on July 31, 1998. D&B purchased the Series A and Series B bonds from the Authority at a 1% discount from par value, or $753,500 (D&B Answer; Tr. 851; DX 13 at 1). PFC received a financial advisory fee of $80,000 from the Authority (Tr. 1008; DX 1, DX 13 at 2).

LWM, as underwriter's counsel, provided an opinion letter to D&B concerning compliance with Exchange Act Rule 15c2-12 (Tr. 363-66, 799, 1550-51; DX 27). LWM also informed D&B in negative terms ("nothing has come to our attention") that it was satisfied that the disclosure in the OS was adequate (RX 41 ¶¶ 79-89, 685). Pepper Hamilton, as bond counsel, provided a supplemental opinion letter to D&B, stating that certain sections of the OS fairly described the matters they discussed and that the tax matters discussed in the OS accurately reflected its opinion (Tr. 135-36, 795-99; DX 28; RX 31). GKS, as the Authority's solicitor, wrote an opinion letter to D&B and Pepper Hamilton affirming the Authority's power to issue the bonds and consummate the transaction (Tr. 799; RX 31 at 5-6). GKS's opinion letter also stated that the OS did not contain any untrue statement of a material fact with respect to the Authority (RX 31 at 5).

Some of the key participants in the Forum Place transaction were not in Pennsylvania for parts of the relevant period. Bradbury was in Georgia for several days as part of a long July 4 weekend (Tr. 682-84, 761-63, 782, 814-15, 1227). His vacation began on July 2 and continued at least through July 7 (Tr. 761; DX 40). Although Bradbury was not in his office during this period, he was accessible by cellular telephone and facsimile, and participated in a telephone conversation about the offering on July 6. O'Neill was on vacation from July 12 through July 26 (DX 40). McErlane covered for him during this period (DX 20, DX 40). Vartan was in Europe from mid-July through July 31 (Tr. 989; RX 16 at 8, 75). The parties pushed to complete the necessary documents so that Vartan could review them before he left on his trip (Tr. 989; DX 24 at 6). Hendershot did not attend the Authority's meeting on July 8 because his wife required emergency surgery (Tr. 1646). An associate from GKS attended the meeting in place of Hendershot (Tr. 1015, 1648; DX 26). Hendershot also did not attend the Authority's August 18 meeting because he was on vacation (Tr. 1648, 1653). The Authority withheld approval of the

minutes of its July 8 meeting until Hendershot returned on September 10 (Tr. 1653, 1664-66; RX 44, Minutes of Aug. 18, 1998, Meeting at 1, Minutes of Sept. 10, 1998, Meeting at 1).

2. Disclosure to Prospective Investors.

Late in June 1998, sales agents for D&B started contacting institutional investors to determine their level of interest in financing the purchase of Forum Place (Tr. 1450-51). Some of these institutional investors immediately declined when they learned of the "short-term lease vs. long-term bond" risk (Tr. 1186-87, 1450). Others expressed an interest and D&B assembled and distributed an information package to them. The package included the Authority's POS, the trust indenture, the existing Forum Place leases, an environmental report, the financial projections prepared by Fowler, and a building appraisal from March 1997 (Tr. 438, 485, 1188-90, 1219-20; DX 52). The OIP charges that the Authority's POS and OS, as well as Fowler's financial projections and the March 1997 appraisal, were materially misleading or omitted material information (OIP ¶ III.E).

The Purpose of the POS and OS

An official statement is a document or set of documents prepared by an issuer of municipal securities or its representative that is complete as of the date it is delivered to the participating underwriter. Exchange Act Rule 15c2-12(f)(3). As relevant to this proceeding, an official statement sets forth information material to an evaluation of the offering. In short, it describes the risks that an investor will take in purchasing the security (DX 94 ¶ 6). A preliminary official statement is an official statement prepared by or for an issuer of municipal securities for dissemination to potential customers prior to the availability of the final official statement. Exchange Act Rule 15c2-12(f)(6).

A participating underwriter must obtain and review a near-final official statement before it bids for, purchases, offers, or sells municipal securities in an offering. Exchange Act Rule 15c2-12(b)(1). After a participating underwriter has reached an understanding with an issuer of municipal securities that it will become a participating underwriter in an offering, and until a final official statement is available, the participating underwriter must promptly send to any potential customer, on request, a copy of the most recent preliminary official statement. Exchange Act Rule 15c2-12(b)(2).

The record in this proceeding contains an undated draft POS (DX 33); a POS, dated July 1, 1998 (DX 40, DX 87); a POS, dated July 8, 1998 (DX 15); and the OS, dated July 17, 1998 (DX 16). The Division alleges that the same material omissions occurred in every version of the POS and OS used here (Tr. 656; Div. Br. at 9 n.5, Div. Reply to PFC at 6 n.6, 15-16).

An offering document should be a "four-corner pronouncement" of all the information necessary for an investor to make an informed decision concerning whether or not to purchase a particular security (Tr. 276, 360-61, 1151, 1487; DX 94 ¶ 33). Investors, including institutional investors, should be able to rely on the assumption that the offering document contains all the information necessary to make an investment decision (Tr. 598-99, 1151-52). Pope, the Division's expert witness, opined that an offering document must provide complete disclosure to

any reasonable and intelligent reader, regardless of where the reader lives and with the assumption that the reader has no knowledge of any particular facts and circumstances not disclosed in the offering document (Tr. 1135; DX 94 ¶ 33).

Limiting Language in the POS and OS

The Authority cautioned prospective investors on page 4 of its POS and OS: "No dealer, broker, salesman or other person has been authorized to give information or to make any representation not contained in this [OS] and, if given or made, such other information or representation must not be relied upon" (DX 15 at 4, DX 16 at 4).

The POS and OS also explained that the Authority had retained PFC as its financial advisor in connection with the preparation, authorization, and issuance of the Forum Place bonds (DX 15 at 18, DX 16 at 20, DX 33 at 18, DX 40 at 18, DX 87 at 18). The Authority then stated that the scope of the financial advisor's engagement was limited:

> The Financial Advisor is not obligated to undertake, and has not undertaken to make, an independent verification or to assume responsibility for the accuracy, completeness, or fairness of the information contained in this Official Statement. The Financial Advisor is an independent advisory firm and is not engaged in the business of underwriting, trading or distributing municipal securities or other public securities.

The POS and OS Disclosed
That the Forum Place Offering Involved
Long-Term Bonds Secured by Short-Term Leases

The POS and OS clearly describe that the Forum Place bonds are limited obligations of the Authority. These documents also explain that the bonds are secured solely by the receipts and revenues received by the Authority from payment on various leases for space in the office building and parking facilities. The POS and OS make clear that neither the general credit of the Authority nor the credit or taxing power of Dauphin County is pledged as payment of the principal and interest on the Forum Place bonds (DX 16 at 1).

The OS conspicuously warned on the cover and on pages 11-13 that the Pennsylvania General Assembly was not required to appropriate the funds necessary to make the rental payments due under the current office or parking leases. The OS also explicitly cautioned that the Commonwealth's leases were scheduled to expire prior to the stated maturity of the 1998 Series A bonds, with page 13 repeating the warning that the leases would expire and that the Commonwealth did not have to extend or renew their terms. Page 13 of the OS identified the office leases by each Commonwealth agency tenant, including PennDOT, and directed the reader to Appendix C for a breakdown of the terms of each lease. Appendix C to the OS listed the leases and their expiration dates, including the PennDOT lease term ending on November 15, 2001, and its optional extension to November 15, 2002. Appendix C, read in conjunction with the remainder of the OS, reflects that the Commonwealth's lease for PennDOT's space expired

at least two years before any of the bonds matured and twenty-four years before most of the bonds matured.

Many of these warnings were emphasized by the use of bold fonts and capital letters. The POS and OS clearly stated:

> THE OFFICE LEASES ARE SCHEDULED TO EXPIRE PRIOR TO THE MATURITY OF THE 1998 BONDS; THERE IS NO COMMITMENT, REQUIREMENT OR GUARANTEE THAT THE COMMONWEALTH WILL RENEW OR EXTEND ANY OF THE OFFICE LEASES.

These warnings proved sufficient to dissuade several prospective investors (Tr. 544-45, 565, 1187, 1450, 1466).

The POS and OS Did Not Disclose PennDOT'S Intent to Move to the Keystone Building, Once It Was Ready

No version of the POS or OS disclosed PennDOT's plan to vacate Forum Place once the Keystone Building was constructed (DX 15, DX 16, DX 33, DX 40, DX 87).

Under the Division's theory of the case, this information was important to prospective investors because there was no certainty that PennDOT would remain at Forum Place and there was near certainty that PennDOT would vacate Forum Place in two or three years. Every investor representative to testify at the hearing considered such information important because the loss of the anchor tenant could impair future debt service on the bonds (Tr. 225, 270-71, 310-11, 336, 423, 487, 534, 548, 578-79). As a credit analyst for one purchaser explained: "[W]hile the bond documents highlighted the fact that the leases expired prior to the term of the bonds, from a credit perspective, there's a big difference between facing the potential loss of your biggest tenant and actually knowing that you'll have to replace your major tenant within three years" (Tr. 611).

Bradbury, Fowler, Sweet, O'Neill, and McErlane offered several post hoc rationalizations as to why PennDOT's planned move from Forum Place to the Keystone Building was omitted from the POS and OS: the contemplated move to an unconstructed building on an indeterminate date was speculative, not a known fact; construction on the Keystone Building had not yet started; and disclosure of PennDOT's planned move was already subsumed in the cautionary language about short-term leases with no guarantee of renewal (Tr. 104-05, 115-17, 122-23, 393-94, 404-05, 689, 739-40, 789-90, 1282-83).

Fowler, Sweet, and Bradbury each testified that: (1) the finance team knew in July 1998 that the POS and OS did not discuss PennDOT's planned move; and (2) they never discussed (or, at least, could not remember discussing) among themselves revision of the POS and OS to include such information. Fowler, Sweet, and O'Neill testified that, if they had to do it all over again, they would still omit any disclosure of PennDOT's planned move (Tr. 102, 104-05, 115-23, 135, 367-68, 393-95, 404-05, 411, 919-20, 952-54, 973-75).

Fowler's Financial Projections

Fowler prepared financial projections of the revenues and expenses at Forum Place that took existing leases and occupants and extrapolated these data for a period of ten years (1998-2008), regardless of the actual lease expiration dates (Tr. 729; DX 13). He presented his projections to the Authority on July 8, 1998, to demonstrate that the cash flow at Forum Place would be sufficient to service the debt and eventually retire the bonds (Tr. 948-50; DX 13 at 8-9). Although Fowler maintained that he prepared the financial projections only for distribution to the Authority, PFC also sent the projections to prospective investors (Tr. 501, 529-30, 942, 985; DX 57).

Fowler did not prepare a written explanation of the assumptions underlying his cash flow analysis, including the assumption that the existing occupants would extend without interruption or be immediately replaced by other qualified tenants at similar rates (DX 94 ¶¶ 12, 64).

Bradbury asked Fowler about the assumptions underlying the financial projections, concluded that the assumptions were reasonable, and added explanatory footnotes (Tr. 806, 853-55). As relevant to this proceeding, footnote 1 to the financial projections states: "Revenues based on actual Commonwealth of Pennsylvania, U.S. Government, and other leases now in effect at the time of Closing and assumes all leases will continue to specific date or renew on similar terms (see Lease Terms and Options on page 5)" (Tr. 451; DX 53 at 4). D&B then circulated the financial projections with footnotes to prospective investors (Tr. 450, 629, 1116).

Neither version of the financial projections was included in the POS or OS (DX 94 ¶ 14). Neither version contained any disclaimer about whether Fowler's assumptions were realistic. Neither version provided any information about circumstances that might prevent the achievement of the forecasted results. Neither version explained that the Commonwealth was unlikely to renew or extend the lease for the PennDOT space (DX 94 ¶¶ 13, 53).

I find as a fact that DCGA never authorized distribution of Fowler's financial projections to prospective investors (DX 24-DX 26). O'Neill did not know that D&B was distributing financial projections to prospective investors (Tr. 360-61). Consequently, O'Neill never reviewed the financial projections (Tr. 363).

Based on the footnoted financial projections that D&B sent to investors, Keith Lowe (Lowe), a representative of Evergreen Fund, assumed that "there was a possibility" that PennDOT could continue to remain at Forum Place through 2008 (Tr. 449-52). Representatives of two other institutional investors did not make the same assumption as Lowe (Tr. 507-09, 630-31). In the judgment of the expert witness for D&B and Bradbury, it was not unreasonable for Lowe to draw the conclusion that he did (Tr. 1561-62).

1997 Appraisal of Forum Place

Early in 1997, a bank owned by Vartan engaged an independent appraiser to determine the present day fair market value of Forum Place (DX 4; RX 16 at 108-09). Vartan sought the

appraisal in connection with a mortgage loan application (Tr. 975-76; RX 16 at 105-06, 109-10). Among other things, the appraiser determined that occupancy rates for Class A office space in Harrisburg's Central Business District were 97% to 99% (DX 4 at 42).[20] In June and July 1998, D&B distributed the appraisal to prospective investors in the Forum Place bonds. By then, of course, the appraisal was fifteen months old.

According to the OIP, the vacancy rate information in the appraisal, together with the misleading OS and financial projections, misled prospective investors into concluding that PennDOT would not leave Forum Place because there was no single block of available office space in downtown Harrisburg large enough to accommodate its needs (OIP ¶ III.E.11).[21]

Lowe testified that page 42 of the appraisal was important to him as he considered the credit worthiness of the bond offering (Tr. 417-19). Susan McCormack (McCormack), a credit analyst for Putnam Investments, thought there was very little office space available in Harrisburg (Tr. 492). She received the appraisal and her notes reflect that she learned of the 1% vacancy rate for Class A space (Tr. 485; DX 55). David Gilliand (Gilliand), a high yield bond analyst at PaineWebber, based PaineWebber's credit summary, in part, on information he drew from the appraisal (Tr. 610-11, 640-41, 644; DX 36).

D. The Buy Side of the Forum Place Transaction.

D&B sold Series A bonds to four institutions: Putnam Investments purchased $27 million of the bonds on July 10; Evergreen Funds purchased $26.7 million of the bonds on July 10; PaineWebber purchased $13 million of the bonds on July 10; and Merrill Lynch purchased $5.6 million of the bonds on July 14 (DX 21-DX 23). These were conditional trade dates. The bonds were a "when-issued" transaction, and did not actually settle until the closing on July 31, 1998.[22]

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[20] The appraisal stated (DX 4 at 42): "Class 'A' occupancy rates increased several percentage points to a 99% occupancy level. . . . The recently constructed Forum Place and the PennDOT facility were recently completed. The bulk of the space in both of these buildings [has] been leased to the Commonwealth of Pennsylvania (a variety of agencies). . . . Both of these two facilities due to their state oriented lease arrangements have not been included in the statistical data associated with the downtown office market analysis." The appraisal's oblique reference to "the PennDOT facility" meant the Riverfront Office Center (Tr. 700, 1565).

[21] The Division attempts to argue that the appraisal was also false and misleading because Fowler and others believed that it overvalued Forum Place (Div. Prop. Find. # 106, Div. Br. at 6 n.2). There is no such allegation in the OIP, as the Division has previously acknowledged (Prehearing Conference of May 26, 2004, at 27-28). The Division also suggests that the appraisal was somehow tainted because Vartan's bank paid for it (Tr. 975-76; Div. Prop. Find. ## 107-08). There is no such allegation in the OIP. See infra note 32.

[22] The term "when issued" is a short form of "when, as, and if issued." It refers to a transaction made conditionally because a security, although authorized, has not yet been issued. New issues

D&B sold about two-thirds of the subordinated Series B bonds to Wilmington Trust Bank (DX 22). D&B sold the remainder of the Series B bonds to close friends of Bradbury or retained them for its own account (Tr. 819-20).

As a part of its sales solicitation, D&B arranged for prospective investors to tour Forum Place (Tr. 420-21, 453-56, 1191, 1309-10, 1454). Vartan conducted two tours on July 7. The tours were comprehensive and lasted one to two hours each (Tr. 454, 511-12, 1192). No subject was "off limits" to prospective investors (Tr. 455, 515-16). Representatives of Putnam Investments and Evergreen Funds, the institutions that purchased the largest quantity of bonds, took a tour (Tr. 454-56, 490, 520, 1309-10). Representatives of Merrill Lynch and PaineWebber, the institutions that purchased the smallest quantity of bonds, did not (Tr. 281, 610).

Institutional Investors vs. "Retail Customers"

The Forum Place offering was a public offering. The bonds were in small denominations ($5,000) and there were no restrictions barring their sale or resale to the public at large (Tr. 87-88, 728-29, 852-53, 1156-57; DX 16, DX 59, DX 94 ¶ 45). A commercial printer billed DCGA for 200 copies of the OS (Tr. 731-32; DX 89).

D&B thought the institutions that bought the Class A bonds were doing so for the mutual funds they managed (Tr. 801, 806, 1225). With the exception of PaineWebber, D&B was correct (Tr. 221, 269, 307, 547, 580; DX 49). The institutions in question were highly sophisticated investors (Tr. 807-08, 1182, 1445). They were represented by analysts or supervisors with advanced business degrees (Tr. 299, 415, 482, 541-42, 568, 600-01, 1182, 1216). Because interest rates were low during 1998, such institutions were very receptive to unrated, high-yield bond offerings (Tr. 1185-86, 1216, 1223, 1449).

The OIP alleges that one of the institutions that purchased Forum Place bonds from D&B "promptly" resold the bonds to its retail customers (OIP ¶ III.D.6). It is unclear if the intended reference is to PaineWebber or Wilmington Trust Bank. According to the charging document, by the closing on July 31, 1998, "retail investors located across the nation had purchased over $1 million of the bonds" (OIP ¶ III.D.6). There is no evidence in the record to quantify the sale of Forum Place bonds to "retail investors" before July 31, 1998.

There is some evidence that PaineWebber resold an unspecified quantity of the Series A bonds to its retail clients on unknown dates (Tr. 646, 652). Likewise, Wilmington Trust Bank eventually may have resold its Series B bonds to its high net worth clients, although there is no evidence of that in the record (Tr. 819-20).

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of bonds are traded on a "when issued" basis. See Barron's Dictionary of Financial and Investment Terms 653 (4th ed. 1995).

Putnam Investments

With one exception, the institutional investors that purchased Series A bonds from D&B did not know of PennDOT's anticipated move when they made their investment decisions (Tr. 578-79). The exception, Putnam Investments, had actual knowledge of PennDOT's intended move to the Keystone Building and nevertheless became the single largest purchaser of the Forum Place bonds (Tr. 529, 531). McCormack learned of PennDOT's plans to leave Forum Place. Although she could not initially remember whether this information came from Fowler or Bradbury, I find that it most likely came from Bradbury (Tr. 486-87, 523-26, 859-60; DX 54 at 3, DX 55). McCormack also learned from either Fowler or Bradbury that the Commonwealth might use Forum Place for its swing space program, although there was no guarantee that it would do so (Tr. 487-90, 492-93, 518, 525-27, 531, 1079-81). McCormack's report and notes reflect that the Commonwealth's swing space program was tentative: "[T]here is no assurance that the Department of Finance will indeed move into Forum Place" (DX 54, DX 55).

Putnam Investments enlisted its outside counsel, a law firm in Boston, Massachusetts, to review the draft POS and the draft trust indenture for Forum Place (Tr. 496-98, 521-23, 532-33; DX 56, DX 90). The law firm recommended certain language changes to the draft trust indenture (DX 90). However, neither Putnam Investments nor its outside counsel recommended any language additions to the POS concerning PennDOT's anticipated move to the Keystone Building.

Merrill Lynch

Steven Syfert (Syfert), a sales agent at D&B, solicited a Merrill Lynch portfolio manager to purchase Forum Place bonds during the initial offering (Tr. 275-76, 1450).

James Loffredo (Loffredo) is the director of research for Merrill Lynch's Municipal Products Group (Tr. 301). In July 1998, the Merrill Lynch portfolio manager asked Loffredo to evaluate the Forum Place bond offering (Tr. 301-03). Loffredo assigned the task to Christopher Fornal (Fornal), a junior analyst-in-training (Tr. 302-03). Loffredo handed Fornal a copy of the POS and told him to prepare a credit worthiness report (Tr. 221, 301-03). Merrill Lynch policy required such a report before a bond purchase could be considered (Tr. 225, 302).

Fornal never spoke with anyone at D&B or toured Forum Place (Tr. 222-23). Although Loffredo edited Fornal's report, Loffredo could not recall if he personally read the POS. He testified that, "most likely," he did review parts of it (Tr. 304). Neither Fornal nor Loffredo knew of PennDOT's intended move when they wrote the report (Tr. 225, 309).

Paragraph III.E.12 of the OIP asserts that Merrill Lynch learned "in September 1998" of PennDOT's planned move to the Keystone Building and "promptly" sold its entire position of Forum Place bonds in the secondary market.

There is a considerable degree of embellishment here. Merrill Lynch learned of PennDOT's planned move early in August 1998 (Tr. 270-71, 282-86, 296). Merrill Lynch then investigated the matter thoroughly (Tr. 270-71, 288, 309-10; DX 71). James Schwartz

(Schwartz), a Merrill Lynch senior research analyst, telephoned Crowell, who immediately confirmed PennDOT's intent to move (Tr. 268, 288-89). Schwartz then purportedly complained to Syfert about the omission of PennDOT's anticipated move from the OS (Tr. 291-92). Syfert did not remember such a conversation and I credit his testimony over that of Schwartz (Tr. 1461-62). Fornal and Loffredo next made several revisions to the credit worthiness report that they had written in July 1998 (Tr. 223-24, 228-29, 238-39, 306; DX 49). In the process of revising their original report, Fornal and Loffredo used language that tracked, without attribution, the February 1998 newspaper article discussing PennDOT's intended move from Forum Place (Tr. 247-48; RX 22). In addition, Fornal and Loffredo either omitted or deleted the date of the report's revision (Tr. 238-39; DX 49).

In mid-September 1998, Merrill Lynch sold its entire inventory of Forum Place bonds to PaineWebber and Maxcor Financial (Tr. 252-55, 292-95; DX 50). Merrill Lynch, which had purchased the bonds for $99.625 per $100 of par value two months earlier, sold them at prices ranging from $99.71 to $100.261 per $100 of par value (DX 21, DX 50). Merrill Lynch found that it was "pretty easy" to sell the bonds (Tr. 331-32). The timing of Merrill Lynch's sales cannot fairly be described as prompt (Tr. 270-71, 292).

PaineWebber: Undisclosed Dealer

Gilliand learned of the Forum Place offering from a colleague who worked for PFC (Tr. 602-03, 649). The colleague encouraged D&B to contact Gilliand, which it did (Tr. 604-06, 1216; DX 32, DX 51). D&B had conducted business with PaineWebber before July 1998, but it had dealt with another individual who purchased credits for PaineWebber's high-yield municipal bond fund (Tr. 816). Gilliand was new to PaineWebber, having joined the firm in March 1998 (Tr. 617).

PaineWebber moved quickly. Gilliand's first contact with D&B occurred on July 7. By July 10, PaineWebber had taken all the Forum Place bonds that were available (Tr. 1221-24; DX 23, DX 32, DX 51). By July 13, Gilliand had authored PaineWebber's credit report on the Forum Place bonds (DX 36).

D&B denied knowing that PaineWebber was buying Forum Place bonds to resell them to others (Tr. 815-16, 862, 1225). The POS and OS did not identify PaineWebber as a participating underwriter or dealer in the distribution of the bonds. PaineWebber did not seek or receive a dealer's concession on the bonds it purchased from D&B (Tr. 817, 1225, 1461). In fact, PaineWebber paid D&B the same price for the bonds as did Putnam, Evergreen, and Merrill Lynch (DX 21, DX 22, DX 23). PaineWebber's profits on Forum Place bonds came from mark-ups on the resale (DX 60, DX 61). Such markups reduced the yield to investors (RX 41 ¶ 230).

D&B paid its sales agent, Wendy Bradbury Armstrong (Armstrong), a commission on the bonds she sold to PaineWebber (Tr. 1225-26, 1234-35). If PaineWebber had identified itself as a dealer and received a dealer's concession, Armstrong would not have earned a commission (Tr. 817-18, 1225-26).

According to Gilliand, Bradbury told him "there [were] several institutions that [D&B] did not want [PaineWebber] to approach," ostensibly because D&B already had orders from those institutions (Tr. 614). If true, Gilliand's testimony would completely undercut Bradbury's claim that he never knew PaineWebber would be acting as a dealer. Gilliand specifically identified Putnam Investments and Delaware Investments as two institutions that D&B did not want PaineWebber to approach (Tr. 614). Both Bradbury and Armstrong denied making any such statements to PaineWebber (Tr. 815, 1226). Gilliand's identification of Delaware Investments as a firm that had already placed an order with D&B is puzzling. Delaware Investments did not receive an allotment in the Forum Place bond offering and only purchased Forum Place bonds later in the secondary market (Tr. 775; DX 21, DX 22; RX 41 ¶ 225). In these circumstances, I credit the testimony of Bradbury and Armstrong and reject the contrary testimony of Gilliand.

Van Kampen Investments

Barnett Sherman (Sherman), a senior municipal analyst with Van Kampen Investments, was responsible for reviewing potential bond investments and making recommendations to the portfolio managers of Van Kampen's mutual funds (Tr. 543). Dan Kluger (Kluger), a sales agent for D&B, sent Sherman a POS and some supporting documents on the Forum Place transaction (Tr. 543, 550). Sherman reviewed the POS, asked questions of Kluger and Bradbury, and ultimately informed D&B that Van Kampen was not interested in purchasing Forum Place bonds (Tr. 543-45, 559-61, 565). Sherman then went on vacation.

Unknown to Sherman at the time, Van Kampen bought $4 million in Forum Place bonds from PaineWebber on July 28 and July 29, 1998 (Tr. 569-72, 586; DX 60, DX 61). Wayne Godlin (Godlin), a portfolio manager for Van Kampen's high-yield municipal bond fund and Sherman's supervisor, decided to purchase the bonds that his subordinate had rejected (Tr. 547, 566, 568, 572). Godlin did not speak with Sherman before buying the bonds (Tr. 566, 583-84).

Godlin learned of the Forum Place offering from PaineWebber (Tr. 569-71). Gilliand sent Godlin a copy of PaineWebber's credit report on Forum Place and discussed the transaction with Godlin "at length" (Tr. 570-71; DX 59). Godlin then requested and reviewed the POS or OS, although he could not remember which one (Tr. 570, 573, 581). Godlin also requested "any other pertinent documentation" or "additional documentation" about the transaction (Tr. 570-71, 576). However, there is no credible evidence that Godlin ever saw Fowler's financial projections or the 1997 appraisal.

Godlin had spoken with Kluger, D&B's sales representative, in connection with some previous bond offerings. However, neither Godlin nor Kluger could remember speaking to each other about the Forum Place transaction (Tr. 571, 588-89, 1199-1201). I find as a fact that Godlin and Kluger did not speak to each other about Forum Place. Godlin did not speak to Fowler (Tr. 595). There is no evidence that Godlin spoke to Bradbury, either.

In deciding to buy the bonds, Godlin relied, in part, on the credit report that Gilliand had authored for PaineWebber (Tr. 569-70, 580-81, 586; DX 36, DX 59). The credit report makes several representations about the Forum Place bonds that do not appear in any documents

authored, reviewed, or distributed by D&B. In addition, the credit report contains several inaccuracies (RX 41 ¶¶ 33, 232, 246, 481). Godlin possessed a great deal of misinformation about the Forum Place bond offering. He believed that PennDOT had an AA credit rating, that PennDOT was responsible for repaying the bonds, and that PennDOT had invested a considerable amount of money in improvements to Forum Place (Tr. 577-78, 590-92). There is no evidence that this misinformation came from the POS, OS, or anyone at D&B.

E. Developments After Closing.

August 1998-December 1999

On August 1, 1998, one day after the Forum Place bond closing, the T&S Building was imploded (Tr. 107, 192, 1497-98, 1571).

Late in August 1998, Fowler received $20,150 from IMAGE for advisory and analytical services regarding the investment of certain proceeds of the Forum Place bonds (PFC Answer; Tr. 1008).[23] To the extent that the OIP alleges that this payment came "from the Authority," it is in error (OIP ¶ III.D.7).

Reese, DCGA's long-time executive director, retired at the end of September 1998 (Tr. 1299, 1319; RX 44, Minutes of June 23, 1998, Executive Session at 2, Minutes of Aug. 18, 1998, Executive Session at 2, Minutes of Sept. 10, 1998, Meeting at 9). Ricci resigned as the Authority's chairman and succeeded Reese as executive director on October 1, 1998 (Tr. 1299-1300, 1319).

For the remainder of 1998 and through 1999, there were no problems filling Forum Place with Commonwealth agency tenants (Tr. 1325). DGS increased the square footage of one lease and extended the term of the lease for two years (Tr. 202-03; RX 23). Vartan, as property manager, was also able to replace one departing government tenant with another government tenant (Tr. 1324-25).

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[23] IMAGE is Investment Management Advisory Group, Inc., of Pottstown, Pennsylvania, a structuring specialist and pricing agent for investments and interest rate management tools. DCGA's procedure for investing the proceeds of a bond closing is described in the record and summarized here (RX 33 at 6, RX 44, Minutes of July 21, 1998, Meeting at 2, Minutes of Aug. 18, 1998, Meeting at 9).

The Forum Place trust indenture provides that the trustee may invest the proceeds of the bond offering in certain securities (DX 16, Appendix A at 14-15). Once the trustee had funds available for investment, he would ask the Authority for directions on how to proceed. After the Riverfront transaction closed, the Authority delegated PASI and Fowler, as program administrator, to assist the trustee in making a selection (RX 44, Minutes of July 21, 1998, Meeting at 2). Fowler then solicited bids, in consultation with IMAGE. IMAGE received a commission from the successful bidder and shared its commission with PASI. Fowler made appropriate disclosure of PASI's commission to the Authority.

January 2000-December 2000

Members of the Authority serve at the pleasure of the Dauphin County Commissioners (Tr. 31, 826-27, 1303). November 1999 produced a sea change in the composition of the Dauphin County Commission, as two sitting Commissioners retired and two new Commissioners were elected (Tr. 1328). After the election, the newly constituted Commission demanded that the sitting Authority members (with one exception) resign, which they did (Tr. 1328-29). The new Commissioners then appointed their own people to the Authority (RX 16 at 88).

Respondents contend that the eventual bond default was, in significant part, a result of the decision of certain new DCGA members to change Authority policies after the closing of the Forum Place bond transaction (RX 41 ¶¶ 162-66, 485-514, 542-54).

The newly constituted Authority fired Vartan as the manager of Forum Place early in 2000 (Tr. 1325-27; RX 16 at 83-87).[24] The Authority had no one of equal competence to replace Vartan (RX 16 at 86). As a result, the Authority itself assumed management of Forum Place, despite the fact that its staff lacked experience in property management (Tr. 823-24, 1331-32). This proved unsettling, because Vartan, Bradbury, and DCGA (as constituted in July 1998) expected that Vartan (the Series C bondholder) would continue to manage Forum Place and work to ensure that it was occupied by Commonwealth agency tenants (Tr. 37, 39-40, 753-55, 823-24, 1318-19; DX 24 at 5; RX 16 at 84).

The bondholders also assumed that Vartan or someone of equal competence would continue to manage Forum Place and they were disappointed when he was dismissed (Tr. 454, 457, 860-61, 1201; DX 54 at 7; RX 26).[25] As grounds for its decision to fire Vartan, the new Authority Board asserted that Vartan's management fee of $180,000 per year was excessive (Tr. 1268; RX 16 at 84, 100-01). However, the Authority's management fee was 5% of gross revenues, a larger amount (Tr. 1355; RX 32 at 13-14, RX 38 at 2, RX 41 ¶¶ 495, 514).

On September 22, 2000, the Commonwealth released its Master Space Plan (DX 91; RX 25). In relevant part, the document characterized Forum Place as "available, flexible, [and] conveniently located" (DX 91 at iv; RX 25 at iv). The Master Space Plan "strongly recommended" Forum Place as "the best swing space location" while the Finance Building was

[24] At about the same time, the new DCGA Board replaced GKS and Hendershot as its solicitor (Tr. 1645).

[25] The Division contends that Vartan's continued management of Forum Place could not possibly have been important to the bondholders because it was not specifically mentioned in the POS or OS (Tr. 841-42, 861-62, 1117; Div. Reply to D&B at 20-21). However, the subject appears in the notes of two investor representatives (DX 54; RX 27). Moreover, the trust indenture required the Authority to maintain the premises at Forum Place in good working order at all times (DX 16, Appendix A at 9). It also required the Authority not to take any actions that would impair or diminish the rights of bondholders (DX 16, Appendix A at 7, DX 54 at 4).

being renovated (DX 91 at iv; RX 25 at iv). Among its Long Term Recommendations, the Master Space Plan counseled against continuing the Commonwealth's practice of leasing small blocks of office space (RX 25 at 69) ("Forum Place illustrates the value of large blocks of space. . . . [I]t was usable by [PennDOT] and other groups and now, it can be appropriately re-used as swing space—or as permanent space—by other Commonwealth functions.").

PennDot vacated most of its space in Forum Place late in 2000 and moved into the newly completed Keystone Building (Tr. 158-59, 213).

2001-2002

Paragraph III.A of the OIP alleges that the Authority has been "unable" to replace PennDOT as a tenant. Respondents contend that this is a half-truth, and that it would be more accurate to say that the new Authority Board has been unwilling to replace PennDOT (RX 41 ¶¶ 162-66, 485-514, 542-54). In their posthearing pleadings, Respondents contend that the new Authority Board "directly caused" the default of the bonds and any resulting loss to the bondholders (D&B Br. at 33, PFC Br. at 30).

The Commonwealth continued to pay rent on the vacant PennDOT space until the lease expired on November 15, 2001 (Tr. 213, 1334).

By November 2001, the market for leasing office space in Harrisburg to the Commonwealth was "very soft" (Tr. 1613-14; DX 100). DGS anticipated that the Commonwealth would not have any large-block office space needs in the Harrisburg area, i.e., requests to lease space in blocks at and above 35,000 to 50,000 square feet (Tr. 1615-16; DX 100). Rather, DGS expected that it would issue only three or four RFPs per year for office leases, and that those RFPs would be in the range of 10,000 to 20,000 square feet each (Tr. 1615-17; DX 100). At about the same time as PennDOT vacated its space in Forum Place, the rates the Commonwealth paid for leasing office space in Harrisburg began to fall (Tr. 1617-18; DX 100). By December 2001, Forum Place was 55% empty (RX 37 at 17).

There is conflicting evidence as to whether DCGA diligently competed for new government tenants at Forum Place. Michael Adams (Adams), Director of DGS's Bureau of Real Estate after January 1998, was not aware of any significant RFPs for leased space that DCGA failed to pursue (Tr. 1603-04, 1619). However, Adams candidly acknowledged that he did not make a practice of checking on DCGA's responses to RFPs (Tr. 1619). In contrast, Fowler and Bradbury observed that the Commonwealth's Housing and Finance Agency was looking for 160,000 square feet of space, and that DCGA did not even know of that fact until Fowler brought it to the Authority's attention (Tr. 826, 988-89; RX 41 ¶ 505). Fowler's and Bradbury's testimony about DCGA's passive approach to finding new tenants for Forum Place is corroborated by Vartan (RX 16 at 97-98). I credit Fowler's and Bradbury's testimony on this point over Adams's more generalized recollection.

DGS issued and then withdrew a RFP for approximately 50,000 square feet of office space for the Commonwealth's Department of State in 2001 (Tr. 1621-23). Forum Place had been the successful bidder on this RFP, and a final lease had been presented for DCGA's

approval. Instead of leasing space at Forum Place, however, the Department of State moved into Commonwealth-owned space in the North Office Building (Tr. 1620-22).

Respondents argue that DCGA's dilatory conduct allowed negotiations over space for the Department of State to collapse. The Authority twice sent Ricci back to renegotiate the terms of the Department of State lease, but DGS refused to renegotiate (RX 32 at 9-12, 15, RX 33 at 22, 27-28, RX 34 at 1, 4, 8, 12-13, RX 35 at 1, 5-6, RX 37 at 12). Ricci and others cautioned the Authority that its hard-nosed approach to reopening negotiations might prompt DGS to debar it from bidding on future Commonwealth lease proposals (RX 34 at 1, 8).

Some members of the new Authority Board wanted to lease Forum Place at higher "market rates" and not at rates similar to those in place in July 1998. Ricci, the former Authority Board chairman and current executive director, expressed an obligation to bondholders to lease space in the building at lower rates that would at least permit bondholder debt service (Tr. 1341-47; RX 32, RX 34, RX 37).

At public meetings during 2001, members of the Authority expressed the view that perhaps defaulting on the Forum Place bonds, so as to force a sale of the property, might be the best way to proceed (Tr. 1382-83; DX 32 at 13-14, DX 34 at 5-6, DX 37 at 13-14, 18). One member of the Authority and the Authority's new solicitor engaged in a discussion suggesting that the financial advisor and the underwriter could be held accountable in the event of a default (Tr. 1386-87; RX 37 at 19).

In September 2001, the Authority forced Ricci to resign as executive director and appointed William Hawk (Hawk) as his successor (Tr. 1330, 1387-88, 1394-95, 1397; RX 38 at 9). Hawk sought, and eventually obtained, a letter from Adams stating that DCGA and DGS's Bureau of Real Estate enjoyed a good working relationship (Tr. 1619-20, 1633-34; DX 100). Upon close questioning, Adams acknowledged that "there were issues" between DGS and DCGA and that Hawk "wrote down . . . what he wanted to see" in the letter (Tr. 1620, 1634). I find as a fact that the working relationship between DCGA and DGS was not good at the time, and that Adams's letter, drafted in relevant part by Hawk, did not accurately reflect the reality of the situation.

In 2002, after the Pennsylvania legislature enacted a law that increased the size of the Department of State, DGS issued a new RFP for bids on 70,000 square feet of leased space for that agency (Tr. 1623). Ten or eleven bids were submitted in response to the RFP (Tr. 1623-24). DGS then narrowed the responsive proposals to three and submitted those three to the Department of State for evaluation (Tr. 1623-24). Forum Place was one of the final contenders (Tr. 1624).

Although Forum Place's proposal was extremely competitive, the Department of State chose the competing proposal of a new building on the site of the former Polyclinic Hospital (Polyclinic) (Tr. 1625, 1639-40). Consultants on the Commonwealth's Master Space Plan had recommended that the Department of State's consolidated site should be located away from the Capitol Complex (DX 91 at 70). Polyclinic is ten to twelve blocks from the Capitol Complex (Tr. 1640).

The Series A bonds have been in technical default since July 2002. In violation of the trust indenture, DCGA has tapped the debt service reserve fund to make payments of interest and principal to the Series A bondholders (Tr. 424, 473-74; DX 16, Appendix A). The Series B bonds are in default. DCGA has not paid interest or principal on the Series B bonds since July 2002 (D&B Answer; Tr. 424; DX 3).

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The bondholders eventually forced Forum Place into receivership (Tr. 425, 473). See Manufacturers and Traders Trust Co., Trustee, v. Dauphin Co. Gen. Auth., Dauphin County Court of Common Pleas, Equity Action No. 2003-EQ-0040 (official notice). On July 21, 2003, the Dauphin County Court of Common Pleas appointed Robert E. Chernicoff (Chernicoff) as the receiver for Forum Place. On August 1, 2003, Chernicoff engaged Vartan Management, Inc. (Vartan Management), to resume management of Forum Place (Tr. 1247-48, 1260).

Vartan Management inspected the property and identified several problems (Tr. 1248-54). These included out-of-date fire extinguishers, deficient sprinkler heads, non-functioning smoke and heat detectors, and a disabled alarm system. The inspection also determined that painting, sanding, and general cleaning had been deferred during the two and one-half years that DCGA had managed the property. After addressing these health, safety, and cleanliness issues, Vartan Management began a marketing campaign to attract eligible tenants to Forum Place (Tr. 1255-57).

Since August 1, 2003, Vartan Management has had some success in filling Forum Place's vacant office space with new tenants and in persuading existing tenants to renew their leases (Tr. 1255-59). In 2004, for example, Vartan Management successfully negotiated a ten-year lease for the use of 32,000 square feet by the Commonwealth's Department of Labor & Industry and another ten-year lease for the use of 35,000 square feet by DGS's Procurement Division (Tr. 1257-58). In addition, Vartan Management persuaded an existing tenant, the Pennsylvania Local Government Commission, to renew for ten years its lease of 5,000 square feet (Tr. 1257).

At the time of the hearing, the occupancy rate for Forum Place was about 55% and the Series A bonds traded at approximately half of their par value (Tr. 424, 426; DX 21).

F. The Hearing Record.

Exhibits

The minutes of the Authority's meetings were transcribed from tapes (Tr. 1336-39, 1390-91, 1647-50). With the exception of DX 25, which I have previously discussed, I consider these detailed minutes to be extremely reliable exhibits (DX 5, DX 24; RX 32-RX 40, RX 43-RX 45). I also consider McCormack's report and notes to be very reliable (DX 54, DX 55). DX 20 is LWM's bill to D&B for $13,425. Undisputed testimony establishes that Bradbury paid LWM triple that amount to compensate for prior transactions that had collapsed (Tr. 675, 1283-84).

Witnesses

It was almost four years from the bond closing to the commencement of the Division's investigation and more than six years from the bond closing to the start of the hearing. For that reason, there was a considerable amount of "I don't remember" or "I don't recall" testimony by various witnesses. This vague testimony was not confined to witnesses who might have an incentive to "forget" (O'Neill, Sweet). It also came from witnesses with no real stake in the outcome (Milke). Bradbury could not remember certain exculpatory details, even after the exhibits and the testimony of other witnesses had established them as facts (Tr. 782, 811-13).

Adams, Milke, McErlane, and Yingling were generally credible witnesses. Pope and Robert W. Doty (Doty), the expert witnesses for the Division and D&B, respectively, were extremely well qualified. It was dismaying to hear that Pope gave little regard to the allegations in the OIP as he drafted his direct testimony (Tr. 1087, 1091, 1133-34). Instead, he concentrated on issues identified by the Division in private conversations (Tr. 1091, 1133). His report opines on several matters that were not specifically identified as grounds for liability in the OIP. That has needlessly confused the issues that are a proper basis for a decision. Doty frequently drew legal conclusions on ultimate issues, and I have not relied on those aspects of his report in reaching my decision.

I have evaluated the investor testimony with a mild degree of skepticism. First, with the exception of Godlin, the investor representatives who testified were not the portfolio managers who decided to purchase the bonds. Rather, they were the credit analysts who made recommendations to the portfolio managers. As a group, the institutional investors were quite aggressive in snapping up the riskier bond offerings during 1998, a period of low interest rates. Second, some of the institutional investors are now involved in litigation against the Authority, through their bondholder committee. Such investors stand to benefit financially if this proceeding results in an order requiring the payment of substantial civil penalties, disgorgement, and prejudgment interest to an investor fund. Third, there is at least a touch of scapegoating here. To the extent that the investor witnesses can exculpate themselves of responsibility for an ill-advised purchase, they will have less to explain to their supervisors and their supervisors will have less to explain to the shareholders of the mutual funds they advise.

I was troubled by the testimony of the Merrill Lynch witnesses (Fornal, Schwartz, and Loffredo). They left the impression that a Merrill Lynch portfolio manager had tentatively decided to buy Forum Place bonds, but, because of a Merrill Lynch internal policy, needed Loffredo and Fornal to "paper the transaction" by preparing a credit worthiness report. I am persuaded that Merrill Lynch later engaged in a deliberate effort to "muddy the trail" by revising Loffredo and Fornal's report after learning of PennDOT's intended move. It then sold its Forum Place bonds at a profit.

The Division failed to address two facts arising from Godlin's testimony: first, PaineWebber, not D&B, solicited Godlin; and second, Godlin's decision to buy Forum Place bonds was based in part on misinformation that the Division could not attribute to D&B.

Among the investor witnesses, I found McCormack and Sherman to be very credible. Lowe was generally credible. Gilliand, Fornal, Schwartz, Loffredo, and Godlin were only marginally credible.

Kluger and Syfert, D&B's sales agents, were generally credible. There are gaps in the record concerning what happened during conversations between Armstrong and Gilliand, and then between Bradbury and Gilliand. The Division has devoted very little of its posthearing pleadings to explaining this aspect of its case. In July 1998, Armstrong had just become a registered representative. Forum Place was her first bond sale and she was thrilled to earn a big commission. However, these facts hardly warrant an inference that she was incredible.

Ricci offered a partisan view of his dealings with the newly constituted Authority after the November 1999 election. In general, he portrayed himself as a responsible official who advocated for the bondholders' interest, and he depicted the new members of the Authority as irresponsible officials who changed the Authority's policies to the detriment of the bondholders. According to Ricci, the new members also micromanaged his actions because they did not trust him (Tr. 1351 ("it was like pulling teeth with this Board"), Tr. 1395 ("they thought I couldn't negotiate my way out of a paper bag")). I have evaluated Ricci's testimony with these factors in mind. Ricci was generally credible in discussing events before November 1999.

Vartan did not testify in person. He was ill with throat cancer and had a limited ability to travel. The cancer makes it difficult for Vartan to speak above a whisper and, thus, difficult for listeners to understand him (Tr. 1244). The Division did not object to the introduction of Vartan's investigative testimony (Tr. 1245). The Division also said it was prepared to cross-examine Yingling, president of Vartan Management, as a substitute witness (Tr. 1246-47). In these circumstances, I give little regard to the Division insinuation that Vartan was a malingerer (Div. Prop. Find. # 15). Because I did not observe Vartan, I make no demeanor-based credibility findings. However, I have relied on Vartan's investigative testimony to the extent that I find it logical, persuasive, and corroborative of the testimony of others.

Crowell was a reliable witness on matters concerning the T&S Building, the Commonwealth's RFP process, and the leasing of space at Riverfront and Forum Place in 1995-96. He was only marginally reliable as to the events of June 30, 1998, and the swing space program. My general impression is that Crowell attempted to ingratiate himself to whomever he was addressing at a given moment, whether it was Vartan in 1995; a newspaper reporter in February 1998; Fowler, Reese, and Sweet on June 30, 1998; or the Division at the hearing. When Crowell was telling the press about the swing space program in February 1998, the program was growing. According to Crowell's hearing testimony, the swing space program was nearly completed by June 30, 1998. The lack of funding is not a satisfactory explanation for these discrepancies.

Crowell's hearing testimony about the events of June 30 makes it difficult to distinguish between what he now knows to be true (with the benefit of hindsight) and what he told Fowler, Reese, and Sweet at the time (as he looked into the future). Accordingly, I do not accept the Division's argument that Crowell's hearing testimony was a more accurate summary of the June

30 meeting than the accounts offered by Fowler and Sweet. As previously noted, the record is inconclusive as to what actually happened at this meeting.

The Division did not take Crowell's testimony under oath during its investigation. Rather, it took notes, for which it now claims privilege, and then sculpted an affidavit that Crowell signed without change (Supplement to Division's Withheld Document List, dated May 27, 2004, items 7k, 7l, 7o, 7s; Tr. 214-15; DX 65). While this is certainly permissible, see United States v. Lieberman, 608 F.2d 889, 897 (1st Cir. 1979), it suggests that the Division may have had some concerns about the credibility of this important witness and was not anxious to create materials that Respondents could use to impeach him at the hearing.

O'Neill's poor memory at the hearing was refreshed and/or impeached by references to his investigative testimony. To the extent that the conflicts were not resolved, I have given more weight to O'Neill's investigative testimony. There were also conflicts between Bradbury's hearing testimony and his investigative testimony, but I do not agree with the Division that Bradbury's investigative testimony should always trump his hearing testimony. For example, during the hearing, Bradbury testified that he added footnotes to Fowler's financial projections (Tr. 806, 853). During the investigation, he could not remember doing so. I find Bradbury's hearing testimony on this point to be more reliable. I have considered Bradbury's and Fowler's testimony throughout this decision, and noted when I find it incredible.

Sweet's poor memory at the hearing cannot be explained by the age of the case alone. Sweet purportedly could not remember who arranged the June 30 meeting with Crowell (Tr. 99, 147), although he knew Crowell well, considered himself a lobbyist, and volunteered to act as the finance team's liaison with the Commonwealth. There is little doubt that Sweet arranged the meeting. Sweet also portrayed himself as more of a bystander than a participant in the June 30 meeting and could not remember the precise conversation at that meeting about PennDOT's plans to vacate Forum Place (Tr. 95). He could not remember his June 22 telephone conversation with Bradbury and O'Neill (Tr. 79) or telling Bradbury about the June 30 meeting with Crowell (Tr. 132). As to the July 8 meeting of the Authority, Sweet did not remember if the Crowell meeting was discussed (Tr. 103-04, 139), the specifics of Fowler's presentation (Tr. 131, 139), or even if he personally made extensive remarks that day (Tr. 104). Finally, Sweet did not remember talking with the Boston law firm representing Putnam Investments about revising the trust indenture (Tr. 133-34, 148). I consider this witness to be thoroughly disingenuous.

Hendershot was a minor witness, but he, too, was generally unreliable. The Division called Hendershot to rebut the contention that he had revised the minutes of the Authority's July 8 meeting. The Division suggested that Fowler shortened the minutes (Div. Prop. Find. ## 191-92), while Fowler argued that Hendershot was the culprit (PFC Prop. Find. ## 18, 146).

Hendershot's efforts to distance himself from the minutes of the July 8 meeting were unrelenting (Tr. 1652 ("I had nothing to do with either set of these minutes"), Tr. 1660 (purging his partner's handwritten notes of the July 8 meeting from GKS's files), Tr. 1665-66 (disavowing the significance of his own handwritten note, showing approval of the July 8 minutes), Tr. 1667 ("I don't know if I was present . . . I often came . . . late. I'm not sure I was in the room when

that motion was adopted."), Tr. 1670 ("Steve's limitation is that he was never really schooled in municipal finance. . . . It could be inaccurate. It could be incomplete.")). I agree with Fowler that the longer version of the minutes helps him, and I see no motive for Fowler to have acted as the Division alleges he did. Beyond that, I express no view as to who made the revisions.

The Division urges me to find that Bradbury, Fowler, and Sweet were not testifying truthfully when they claimed that the finance team never discussed the need to disclose PennDOT's anticipated move (Div. Br. at 27). This is a major request, because it would fundamentally change the character of the case. If I were to make such an adverse group credibility finding, Bradbury's scienter and Fowler's role in reviewing the disclosure language in the POS could almost be assumed. Such a finding would also imply that Bradbury, Fowler, and Sweet conspired during the investigation to cover up the true extent of their discussions. Such an adverse group credibility finding, if sustained on appeal to the Commission and the court of appeals, would virtually guarantee the Division a back-door victory. If the Division had evidence of such a conspiracy, it should have alleged it in the OIP and proven it at the hearing. I decline to make the requested adverse group credibility finding.

Inappropriate Argument in Posthearing Pleadings

PFC's Brief addresses several documents that are not part of the record, including the minutes of five Authority meetings (December 1999 through March 2001) and various newspaper articles (PFC Br. at 36-38, 48). The Division objects to any consideration of these documents. I agree with the Division.

The Division also strays beyond the record at times. During the hearing, the Division read into the record a passage of investigative testimony to test the validity of Doty's opinions (Tr. 1502-05). It was entirely proper for the Division to use the investigative testimony for this limited purpose. Cf. Fed. R. Evid. 105, 703. However, in its posthearing pleadings, the Division now treats the investigative testimony as if it had been given at the hearing, and as if it were admissible as substantive evidence for all purposes (Div. Prop. Find. ## 105, 252). This is inappropriate. Cf. Fed. R. Evid. 105, 703. The Division cites Pope's report as support for certain proposed factual findings (Div. Prop. Find. ## 4-5). This is also inappropriate. Pope based his opinions on his understanding of the facts, as developed during the Division's investigation (DX 94 ¶ 4 and Exhibit C). However, Pope's report never identified the specific facts upon which it was based (Tr. 1047-48). The Division cannot assume that the "facts" from the investigation are the facts adjudicated at the hearing.

The Division's Reply to PFC's Brief also raises several new factual allegations that lack record support and presents argument on matters that are beyond the scope of the OIP. For example, the OIP does not allege that PFC and Fowler directly violated Sections 17(a)(2) and 17(a)(3) of the Securities Act. It only alleges that they caused the Authority's violations of these provisions. When the Commission wants to charge an individual as both a direct violator and as a cause of the violation of another actor, it knows how to do so. See Paragraph II.F of the OIP in Admin. Pro. No. 3-11462, Ira Weiss (Apr. 22, 2004). Accordingly, the Division's arguments of direct liability by PFC and Fowler will not be considered further.

DISCUSSION AND CONCLUSIONS

A. Applicable Legal Standards.

Congress exempted offerings of municipal securities from the registration requirements and civil liability provisions of the Securities Act and the periodic reporting requirements of the Exchange Act. See Section 3(a)(2) of the Securities Act; Section 3(a)(12) of the Exchange Act. However, Congress did not exempt municipal securities transactions from the antifraud provisions of those statutes.

In 1975, Congress enacted the Securities Acts Amendments of 1975, Pub. L. No. 94-29, 89 Stat. 97 (1975). The 1975 Amendments created the MSRB and provided a system of regulation for both municipal securities professionals and the municipal securities markets.

In 1988, the Commission sought comments on a proposal to prevent fraud by enhancing the timely access of underwriters, public investors, and other interested persons to municipal official statements. See Municipal Securities Disclosure, 41 SEC Docket 1402 (Sept. 22, 1988). At the same time, the Commission published its interpretation of an underwriter's obligation to have a reasonable basis for its implied recommendation of any municipal securities that it underwrites. Id. at 1411-15 (1988 Interpretive Statement). The Commission also invited comments on its interpretation. Id. at 1414.

In 1989, the Commission adopted Exchange Act Rule 15c2-12, which requires underwriters to obtain and review a municipal issuer's official statement prior to selling bonds, and to provide official statements to investors and potential investors. Municipal Securities Disclosure, 43 SEC Docket 2245 (June 28, 1989). At the same time, the Commission modified, in limited respects, its previously published interpretation of the legal obligations of municipal securities underwriters under the antifraud provisions of the federal securities laws. Id. at 2257-58 (1989 Interpretive Statement).

In March 1994, the Commission issued another interpretation. Statement of the Commission Regarding Disclosure Obligations of Municipal Securities Issuers and Others, 56 SEC Docket 596, 597 (Mar. 9, 1994) (1994 Interpretive Statement). As relevant to this proceeding, the Commission stated that increased attention needed to be directed at disclosure of the risks of the securities being offered. In November 1994, the Commission adopted amendments to Rule 15c2-12 to prohibit the underwriting of municipal issues unless continuing information covenants are provided by the issuer. Municipal Securities Disclosure, 57 SEC Docket 2993 (Nov. 10, 1994).

Primary Violations of the Antifraud Provisions

Paragraph III.F.1 of the OIP alleges that the Authority violated Sections 17(a)(2) and 17(a)(3) of the Securities Act. Paragraph III.F.3 of the OIP alleges that D&B and Bradbury

willfully violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder.[26]

Section 17(a) of the Securities Act proscribes fraudulent conduct in the offer or sale of securities and Section 10(b) of the Exchange Act and Rule 10b-5 proscribe fraudulent conduct in connection with the purchase or sale of securities. These provisions prohibit essentially the same type of conduct. See United States v. Naftalin, 441 U.S. 768, 773 n.4, 777-78 (1979). To prevail under Section 17(a)(1) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5, the Division must show: (1) misstatements or omissions of material facts or other fraudulent devices; (2) made in connection with the offer, sale, or purchase of securities; and (3) that respondents acted with scienter. See Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n.12 (1976). No scienter requirement exists for violations of Sections 17(a)(2) or 17(a)(3) of the Securities Act; negligence alone is sufficient. Aaron v. SEC, 446 U.S. 680, 701-02 (1980); Pagel, Inc. v. SEC, 803 F.2d 942, 946 (8th Cir. 1986).

Scienter is defined as "a mental state embracing intent to deceive, manipulate, or defraud." Hochfelder, 425 U.S. at 193 n.12. It may be established by a showing of recklessness. David Disner, 52 S.E.C. 1217, 1222 & n.20 (1997) (citing Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1568-69 (9th Cir. 1990) (en banc)). The en banc Ninth Circuit adopted the standard of recklessness articulated by the Seventh Circuit in Sundstrand Corp. v. Sun Chem. Corp., 553 F.2d 1033, 1044-45 (7th Cir. 1977): "[A] highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it." Scienter is a question of fact and can be proved by circumstantial evidence. SEC v. Hasho, 784 F. Supp. 1059, 1107 (S.D.N.Y. 1992) (collecting cases).

An omission is material if there is a substantial likelihood that a reasonable investor would have considered the omitted fact important in making an investment decision and disclosure of the omitted fact would have significantly altered the total mix of information available. Basic Inc. v. Levinson, 485 U.S. 224, 231-32 (1988); TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976); SEC v. First Jersey Secs., Inc., 101 F.3d 1450, 1466 (2d Cir. 1996). Materiality presents a mixed question of law and fact. TSC Indus., 426 U.S. at 450.

Willfulness is shown where a person intends to commit an act that constitutes a violation. There is no requirement that the actor must also be aware that he is violating any statutes or regulations. Wonsover v. SEC, 205 F.3d 408, 414 (D.C. Cir. 2000); Tager v. SEC, 344 F.2d 5, 8 (2d Cir. 1965).

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[26] Although the Division is primarily concerned with violations of Section 17(a)(1), it also alleges that D&B and Bradbury violated Sections 17(a)(2) and 17(a)(3) (Prehearing Conference of Aug. 5, 2004, at 12-13; Tr. 1031). By invoking Section 17(a) in its entirety, the OIP gave appropriate notice that all subsections would be in issue. I reject D&B and Bradbury's claim of surprise as to the allegations under Sections 17(a)(2) and 17(a)(3).

The jurisdictional requirements of the antifraud provisions are interpreted broadly, and are satisfied by intrastate telephone calls and even the most ancillary mailings. SEC v. Softpoint, Inc., 958 F. Supp. 846, 865 (S.D.N.Y. 1997), aff'd, 159 F.3d 1348 (2d Cir. 1998). There is no dispute that the jurisdictional requirements have been satisfied in this proceeding.

Causing Violations of
Sections 17(a)(2) and 17(a)(3)

Paragraph III.F.2 of the OIP alleges that PFC and Fowler caused the Authority's violations of Section 17(a)(2) and 17(a)(3) of the Exchange Act.

The Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 101-429, 104 Stat. 931 (1990) (Remedies Act), created a distinct class of secondary liability, causing liability, and made it subject to a new administrative remedy, a cease-and-desist order. As here relevant, Section 8A of the Securities Act and Section 21C(a) of the Exchange Act specify that a respondent is a cause of another's violation if the respondent knew or should have known that his or her act or omission would contribute to such violation.

The Commission has determined that causing liability under these statutory provisions requires findings that: (1) a primary violation occurred; (2) an act or omission by the respondent caused the violation; and (3) the respondent knew, or should have known, that his or her conduct would contribute to the violation. See Robert M. Fuller, 80 SEC Docket 3539, 3545 (Aug. 25, 2003), pet. denied, 2004 U.S. App. LEXIS 12893 (D.C. Cir. Apr. 23, 2004); Erik W. Chan, 77 SEC Docket 851, 859-60 (Apr. 4, 2002).

Negligence is sufficient to establish liability for causing a primary violation that does not require scienter. Howard v. SEC, 376 F.3d 1136, 1141 (D.C. Cir. 2004); KPMG Peat Marwick LLP, 54 S.E.C. 1135, 1175 (2001), recon. denied, 74 SEC Docket 1351 (Mar. 8, 2001), pet. denied, 289 F.3d 109 (D.C. Cir. 2002). Negligence is the failure to exercise reasonable care or competence. Byron G. Borgardt, 80 SEC Docket 3559, 3577 & n.35 (Aug. 25, 2003).

The Commission has yet to announce the criteria it will use in deciding whether a secondary actor should have known that specific acts or omissions "would contribute to" a primary violation for purposes of Section 8A(a) of the Securities Act or Section 21C(a) of the Exchange Act. However, a proceeding involving this issue is now pending on the Commission's docket. See Jeffrey M. Steinberg, 76 SEC Docket 1538, 1582-89 (Dec. 20, 2001) (Initial Decision) (rejecting the Division's argument that any act that contributes to a primary violation is a cause of that violation for purposes of Section 21C(a) of the Exchange Act; and also requiring the Division to establish "a sufficient nexus between the respondents' alleged conduct and the underlying violation"), review granted; see also Simon M. Lorne & W. Hardy Callcott, Administrative Actions Against Lawyers Before the SEC, 50 Bus. Law. 1293, 1308 (Aug. 1995) ("'Causing' liability under the Remedies Act poses several questions that the SEC has not yet finally resolved. . . . [One question] is the issue of how close a nexus must there be between the 'cause' and the underlying violation.").

Primary Violations of MSRB Rule G-17
and Section 15B(c)(1) of the Exchange Act

Paragraph III.F.5 of the OIP alleges that D&B and Bradbury willfully violated MSRB Rule G-17.[27] The applicable version of that provision requires that, in the conduct of its municipal securities business, "each broker, dealer, and municipal securities dealer shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice."

The state of mind necessary to establish a violation of MSRB Rule G-17 presents an open question. See Wheat, 80 SEC Docket at 3425 & n.42 ("We believe that Rule G-17 requires a showing of at least negligence to establish an unfair practice violation.") (emphasis added). The Commission determined that, even if proof of scienter were required, the respondents had acted with scienter. Id.

In SEC v. GLT Dain Rauscher, Inc., 254 F.3d 852, 856 (9th Cir. 2001), the court observed that the parties before it did not dispute that negligence was the standard by which MSRB Rule G-17 liability should be evaluated. The court also cited a settled administrative proceeding, Merrill Lynch, Pierce, Fenner & Smith, Inc., 67 SEC Docket 2487, 2501-02 (Aug. 24, 1998), which identified negligence as the appropriate standard.

The present OIP covers all the bases: it alleges that D&B and Bradbury willfully violated MSRB Rule G-17 by knowing, reckless, or negligent conduct (OIP ¶ III.F.5). The parties disagree about the applicable legal standard (Div. Prehearing Br. at 17; D&B Br. at 7-9; Div. Reply to D&B at 23). Because Wheat leaves the issue unresolved, I will make a determination under both the negligence and scienter standards.

Paragraph III.F.4 of the OIP alleges that D&B willfully violated Section 15B(c)(1) of the Exchange Act. Section 15B(c)(1) prohibits any broker, dealer, or municipal securities dealer from using the mails or interstate commerce "to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any municipal security in contravention of any rule" of the MSRB, including MSRB Rule G-17. Negligence is sufficient to violate Section 15B(c)(1). See SEC v. Fitzgerald, 135 F. Supp. 2d 992, 1027 nn.11-12 (N.D. Cal. 2001).

Aiding and Abetting Violations of Section
15B(c)(1) of the Exchange Act

Paragraph III.F.4 of the OIP alleges that Bradbury willfully aided and abetted D&B's violations of Section 15B(c)(1) of the Exchange Act.[28] To show that one respondent willfully

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[27] Bradbury is charged as a primary violator of MSRB Rule G-17 on the theory that MSRB Rule D-11 expressly includes "associated persons" within the definitions of brokers, dealers, and municipal securities dealers for purposes of all other MSRB Rules. See Wheat, First Sec's, Inc., 80 SEC Docket 3406, 3421 n.29 (Aug. 20, 2003).

[28] Paragraph III.F.4 of the OIP also alleges that Bradbury caused D&B's violation of Section 15B(c)(1) of the Exchange Act. In Dominick & Dominick, Inc., 50 S.E.C. 571, 578 n.11 (1991),

aided and abetted the violation of another, the Commission requires the Division to establish three elements: (1) another party has committed a securities law violation; (2) the accused aider and abetter has a general awareness that his role was part of an overall activity that was improper or illegal; and (3) the accused aider and abetter knowingly and substantially assisted the principal violation. See Orlando Joseph Jett, 82 SEC Docket 1211, 1256 n.46 (Mar. 5, 2004); Abraham & Sons, 75 SEC Docket at 1492 (citing Graham v. SEC, 222 F.3d 994, 1000 (D.C. Cir. 2000)); Donald T. Sheldon, 51 S.E.C. 59, 66 (1992), aff'd, 45 F.3d 1515 (11th Cir. 1995).

The Commission has held that a showing of recklessness will satisfy the "substantial assistance" prong of the aiding and abetting test. See Graham, 53 S.E.C. at 1084-85 & n.33; Russo Sec's., Inc., 53 S.E.C. 271, 278-79 & n.16 (1997); but see Howard, 376 F.3d at 1143 (holding that "extreme recklessness" may support aiding and abetting liability, but concluding that "aiding and abetting liability cannot rest on the proposition that the person 'should have known' that he was assisting violations of the securities laws.").

Irrespective of the level of proof required to establish the primary violation, the Commission has made clear that the accused aider and abetter must have acted with scienter. See Zion Capital Mgmt. LLC, 81 SEC Docket 3063, 3076-77 & n.35 (Dec. 11, 2003); Terence Michael Coxon, 80 SEC Docket 3288, 3300 n.32 (Aug. 21, 2003), appeal pending, No. 03-73732 (9th Cir. filed Oct. 13, 2003); Kingsley, Jennison, McNulty & Morse, Inc., 51 S.E.C. 904, 911 & n.28 (1993).

B. Preliminary Issues.

D&B and Bradbury assert that they are the victims of selective prosecution. They claim unfairness in the fact that the Commission has charged them with misconduct, even though it brought no charges against the Authority's solicitor, bond counsel, or the underwriter's counsel. They also argue that the Commission "merely slapped the Authority's wrist in a sweetheart consent order" despite the Authority's truly disturbing record of reckless behavior between November 1999 and July 2003 (D&B Br. at 6). They further contend that there is no apparent basis for such discriminatory enforcement action.

To prevail on a claim of improper selective prosecution, Respondents must establish that they were singled out for enforcement action while others similarly situated were not, and that their prosecution was motivated by arbitrary and unjust considerations. See United States v. Huff, 959 F.2d 731, 735 (8th Cir. 1992); Barry C. Wilson, 52 S.E.C. 1070, 1074 (1996); Richard J. Puccio, 52 S.E.C. 1041, 1046 (1996).

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a settled proceeding, the Commission concluded that one who aids and abets a primary violation is necessarily a cause of the violation. The Commission has subsequently followed that approach in contested cases raising the same issue. See Abraham & Sons Capital, Inc., 75 SEC Docket 1481, 1492 & n.25 (July 31, 2001); Sharon M. Graham, 53 S.E.C. 1072, 1085 n.35 (1998), aff'd, 222 F.3d 994 (D.C. Cir. 2000); Adrian C. Havill, 53 S.E.C. 1060, 1070 n.26 (1998).

In accepting the Authority's settlement offer, the Commission identified the turnover in the membership of the Authority, the replacement of the Authority's financial advisor and solicitor, the Authority's prompt remedial actions, and the cooperation the Authority afforded the Commission's staff as factors it had considered. See Dauphin Co. Gen. Auth., 82 SEC Docket at 2887-88. The Division views the Authority as less culpable because its members were inexperienced and relied on their professionals (Tr. 1031; Div. Br. at 36-37). Doty opined that the Commission approaches municipal securities regulation in important respects through underwriters, due to statutory limits and "considerations of intergovernmental comity and the political process" (RX 41 ¶ 197).

The Division believes that O'Neill and Hendershot had limited engagements in the Forum Place transaction (Tr. 364-65, 1296; Div. Prop. Find. ## 58, 93, 300). Conversely, the Division contends that the Authority relied heavily on Sweet, as well as Respondents, to ensure that the OS was complete, accurate, and contained all necessary disclosures (Div. Prop. Find. # 246).[29] Respondents included Sweet's Wells Submission on their list of proposed exhibits, but elected not to offer that document into evidence. The Wells Submission might have shed light on why the Commission did not bring charges against Sweet. I find that Respondents have not met their burden as to the second prong of the test for showing improper selective prosecution.

PFC and Fowler argue that the Authority is not a "person" within the meaning of Section 17(a) of the Securities Act. However, Section 2(a)(2) of the Securities Act defines the term "person" as including "a corporation" and "a government or political subdivision thereof." The record demonstrates that the Authority is both a public corporation engaged in the civil administration of government and a political subdivision of the Commonwealth. Accordingly, the Authority is subject to Section 17(a) of the Securities Act.

PFC and Fowler also argue that the Division cannot satisfy Section 17(a)'s requirement that misconduct occur "in the offer or sale of any securities." They contend that they had nothing to do with the actual offer or sale of the bonds. A similar argument was raised by the financial advisors in another proceeding, but the Chief Administrative Law Judge rejected it. See County of Nevada, 70 SEC Docket 3303, 3321-22 (Oct. 29, 1999), final, 71 SEC Docket 519 (Dec. 2, 1999). I see no reason to reach a different conclusion here. The relevant statutory language should be construed broadly, consistent with the remedial purposes of the antifraud provisions of the federal securities laws. See SEC v. Zandford, 535 U.S. 813, 820-25 (2002); Naftalin, 441 U.S. at 773. PFC and Fowler played a major role in the Forum Place bond offering. Furthermore, PFC and Fowler have been charged with causing the Authority's primary violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act. As the issuer of the bonds, the Authority's conduct occurred in the offer or sale of a security.

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[29] In arguing that the Authority relied on Sweet, the Division clashes with the views of its own expert (Tr. 1104) ("I don't think most bond counsel would say that their retention as bond counsel makes them responsible for the [OS]").

C. Materiality of the Omissions and the Need to Disclose Them.

The function of the materiality requirement is to weed out claims based on trivial or tangential omissions. An analysis of materiality should include an evaluation of both the meaning of the information that allegedly should have been disclosed and the "total mix of information made available" to the reasonable investor.

In conducting this analysis, it is irrelevant that Respondents were marketing the bonds to sophisticated institutional investors. The antifraud provisions of the federal securities laws apply with equal force to all investors, including those who are experienced and sophisticated. See Brian A. Schmidt, 76 SEC Docket 2255, 2271 & n.40 (Jan. 24, 2002); Jay Houston Meadows, 52 S.E.C. 778, 785 (1996).

The Forum Place bonds represented only the third public offering of securities of their type in the central Pennsylvania region. They required a long-term investment in a specialized office building project. The financial success of the project would be directly dependent on the issuer's ability over many years to keep the project substantially full under short-term and intermediate-term leases with the Commonwealth. Pope and Doty had never previously encountered a bond offering of this sort (Tr. 1059, 1155, 1534; DX 94 ¶¶ 11, 27). I agree with Pope that there was a need for careful disclosure of unusual risks in these circumstances (DX 94 ¶¶ 11, 27-28).

1. Material Omissions Identified in the OIP as Grounds for Liability.

The OIP alleges that the POS and OS should have disclosed PennDOT's anticipated move to the Keystone Building. It also asserts that Fowler's financial projections were misleading, even after Bradbury had added explanatory footnotes. Finally, the OIP contends that the appraisal was misleading, insofar as it discussed a 1% vacancy rate for Class A office space in Harrisburg's downtown business district.

As to PennDOT's anticipated move, the disclosure provided in the POS and OS was inadequate because it told only half the story. There is a significant difference between stating that there is no guarantee that any lease would be extended or renewed and stating that the agency occupying 79% of the space and generating 60% of the total lease revenues was nearly certain to leave within two or three years. The PennDOT information was known to Respondents before the offering. It should have been disclosed explicitly in the POS and OS. See Johnston v. HBO Film Mgmt., Inc., 265 F.3d 178, 192-93 (3d Cir. 2001) (discussing omissions that made affirmative representations misleading); cf. Swickard v. A.G. Edwards & Sons, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,522 at 30,275 (Mar. 7, 1985) (holding that half of the truth may amount to a lie if it is understood to be the whole).

Similarly, the footnoted financial projections set forth anticipated revenues for ten years, without identifying PennDOT's intended move and without evaluating the likelihood that PennDOT would be replaced immediately by another eligible tenant paying comparable rates. The evidence supporting the misleading nature of the footnoted financial projections is not nearly as strong as the evidence concerning PennDOT's anticipated move. It depends on the

less-than-forceful testimony of one investor ("there was a possibility") and a concession by D&B's expert ("not unreasonable"). Nonetheless, I find it sufficient. Respondents do not dispute that the first two omissions identified above involved information that would have been important to a reasonable investor. On that basis, and after considering the record, I conclude that both of these omissions were material.

PennDOT's Proposed Move to the Keystone
Building Was Not Publicly Available Information

When allegedly undisclosed material information is readily accessible in the public domain, a respondent may not be held liable for failing to disclose it. See In re Keyspan Corp. Sec's. Litig., 2003 U.S. Dist LEXIS 20746, at *49-51 (E.D.N.Y. Mar. 18, 2003) (collecting cases). "It is pointless and costly to compel firms to reprint information already in the public domain." Weilgos v. Comm. Edison Co., 892 F.2d 509, 517 (7th Cir. 1989). "Although the underlying philosophy of federal securities regulations is that of full disclosure, . . . there is no duty to disclose information to one who reasonably should already be aware of it." Seibert v. Sperry Rand Corp., 586 F.2d 949, 952 (2d Cir. 1978).

Respondents argue that PennDOT's anticipated move to the Keystone Building was publicly available information during June and July 1998 because it had been reported in certain Pennsylvania newspapers, discussed at the Authority's public meeting on July 8, 1998, and was freely shared by DGS with anyone who asked (D&B Br. at 15, 26-28; PFC Br. at 47-50). As to the newspaper articles, I reject this argument because the publications in question were not widely available outside of central Pennsylvania (DX 68, DX 69, DX 101).[30] See In re Apple Computer Sec's. Litig., 886 F.2d 1109, 1116 (9th Cir. 1989) ("Even in a fraud on the market case, corporate insiders are not relieved of their duty to disclose material information where that information has received only brief mention in a few poorly-circulated . . . publications."); Seibert, 586 F.2d at 952 (holding that information was a matter of general public knowledge because it was reported nationwide in the press, on radio, and on television, was discussed in Congress, and was analyzed in published administrative and judicial opinions); United Paperworkers Int'l Union v. Int'l Paper Co., 801 F. Supp. 1134, 1142 (S.D.N.Y. 1992) ("[T]horough and intensive news reporting . . . is required for media coverage to be included in the 'total mix' of information available to shareholders."), aff'd, 985 F.2d 1190 (2d Cir. 1993). Respondents' alternative arguments also lack merit. I decline to hold that prospective investors had a duty to attend the Authority's public meeting or to contact Crowell to obtain information that properly belonged in the POS and OS distributed at about the same time.

[30] The record contains only one newspaper article discussing the proposed Keystone Building (RX 22). Nonetheless, the Division acknowledges that the Harrisburg Patriot News "repeatedly referred" to that subject during the period in question (Div. Br. at 13 n.6). Other Pennsylvania newspapers also covered the Commonwealth's initial announcement of plans to construct the Keystone Building (Tr. 218-19). However, that newspaper coverage occurred more than two years before the Forum Place offering. Doty conceded that an underwriter could not properly assume that a potential investor read the local Harrisburg newspaper (Tr. 1488).

The "Bespeaks Caution" Doctrine
Is Inapplicable Here

D&B and Bradbury contend that the cautionary statements in the POS and OS related to the precise topic the Division claims should have been disclosed—namely, that the PennDOT lease would not be renewed. They invoke the "bespeaks caution" doctrine to argue that further disclosures would not have been material (D&B Br. at 25-26). The Division counters that the "bespeaks caution" doctrine applies only to forward-looking statements, and does not excuse the failure to disclose known material facts (Div. Reply to D&B at 10-13).

The "bespeaks caution" doctrine recognizes that the text of an offering document must be read in context. In re Donald J. Trump Casino Sec's. Litig., 7 F.3d 357, 371 (3d Cir. 1993). The doctrine is equally applicable to allegations of both affirmative misrepresentations and omissions of "soft information."[31] Id.

When an offering document's forecasts, projections, or opinions are accompanied by cautionary statements that are substantive and tailored to the soft information allegedly misrepresented or omitted, the alleged misrepresentations or omissions are rendered immaterial as a matter or law. In re Adams Golf, Inc., Sec's. Litig., 381 F.2d 267, 279 (3d Cir. 2004); Trump, 7 F.3d at 371. A vague or boilerplate/blanket disclaimer that merely warns the reader that the investment has risks will ordinarily be inadequate to prevent the document from being misleading. Trump, 7 F.3d at 371.

The Forum Place POS and OS did not disclose PennDOT's plan to vacate Forum Place upon completion of the Keystone Building. Although the timing of this move was uncertain as of July 1998, the issue is intent, not timing. The Commonwealth was quite likely to move PennDOT within two or three years. In short, PennDOT's plan to vacate was a then-present factual condition during July 1998 (Tr. 1571-72). See Shaw v. Digital Equip. Corp., 82 F.3d 1194, 1213 (1st Cir. 1996) (finding statement of company's current intent to be representation of present fact); Harden v. Raffensperger, 65 F.3d 1392, 1405-06 (7th Cir. 1994) (concluding that company's statement of "plans to restore profitability" to be statement of present existing fact and not the type of "soft information" to which the "bespeaks caution" doctrine applies); see also 1994 Interpretive Statement, 56 SEC Docket at 601 & n.59.

Accordingly, I conclude that PennDOT's intended move was an undisclosed fact, and not undisclosed "soft information" covered by the "bespeaks caution" doctrine. As such, the doctrine is inapplicable to the omissions at issue here and therefore does not shield D&B and Bradbury from liability. See EP Medsystems, Inc. v. Echocath, Inc., 235 F.3d 865, 874, 876 (3d

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[31] The term "soft information" refers to statements of subjective analysis or extrapolation, such as opinions, motives, and intentions, or forward-looking statements, such as projections, estimates, and forecasts. Trump, 7 F.3d at 368 n.11; see also Section 27A(i)(1) of the Securities Act (defining forward-looking statements as statements of projections, plans or objectives for future performance, future economic performance, and assumptions underlying or relating to the above).

Cir. 2000); Grossman v. Novell, Inc., 120 F.3d 1112, 1123 (10th Cir. 1997); Shaw, 82 F.3d at 1213.

The Appraisal Was Not Materially Misleading,
Either by Itself or When Considered as
Part of the Total Mix of Information Available

The parties vigorously dispute the importance of the appraisal to a reasonable investor (Div. Br. at 6, 19; D&B Reply at 15-16; PFC Reply at 9).

The OIP alleges that the Class A vacancy rate information in the appraisal, when considered along with the OS and financial projections, misled investors into believing that PennDOT might renew its lease at Forum Place because there was no other office space available in downtown Harrisburg (OIP ¶ III.E.11). With respect to the appraisal, this is the only issue properly before me.[32]

The concept of "Class A, B, or C" office space is loose terminology in the real estate market. Such classifications are based on vague and subjective evaluations (Tr. 1264-65). The record does not show that everyone who used the term "Class A office space" in this proceeding shared a common understanding of what it meant. For example, some witnesses considered Forum Place to be Class A space, while the Division believed it was Class B or B+ (Tr. 419, 1265-66; RX 16 at 115-16). Indeed, the Division missed no opportunity to disparage Forum Place (Div. Br. at 3 (characterizing Forum Place as a parking garage that had been temporarily converted into an office building), 7 (asserting that Forum Place is at a competitive disadvantage because it is a converted parking garage and located in congested downtown Harrisburg)). The Division cannot have it both ways.

On a more fundamental level, the Division has not even shown that the vacancy rate for the Class A market has any bearing on the demand for office space by the Commonwealth or other eligible tenants. Fowler explained that the Commonwealth did not typically lease Class A office space (Tr. 1003-04). Although the Commonwealth was "trading up" and moving from substandard space into better space during 1998, some of these moves were from Class C to Class B space (Tr. 1003-05). The Division's assumption that Commonwealth agencies, including PennDOT, require nothing less sumptuous than Class A office space lacks record support.

The Division never asked Fornal, Gilliand, Lowe, McCormack, or Doty to explain their understanding of Class A office space. Nor did the Division explore with the witnesses its assumption that the Harrisburg market for Class A office space was relevant to the demand for

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[32] I decline to consider the Division's belated claims that the appraisal was also misleading because it overvalued Forum Place and did not take into account the limits on "bad use" imposed by the federal tax code (Div. Br. at 6, 19). These specific defects in the appraisal were not identified in the OIP. See supra note 21.

office space by eligible tenants. For these reasons, I give little regard to the testimony on this subject.

2. Material Omissions Not Identified in the OIP as Grounds for Liability.

The Division's theories of liability have evolved and expanded since the proceeding began. See supra notes 21, 32. The Division's current position is that there are three other material omissions that would have been important to a reasonable investor and should have been disclosed in the POS and OS: (1) the vagueness of the Commonwealth's swing space program; (2) the limited number of eligible tenants in the Harrisburg area; and (3) the risks that might jeopardize the non-taxable status of the bonds. The OIP recited facts about the first two of these omissions, but it did not separately charge that the failure to disclose such facts could result in a finding of liability. In this regard, the Division has created a predicament similar to the one it created in Borgardt, 80 SEC Docket at 3567-70.

With the benefit of hindsight, it is easy to understand how this situation developed. At the first prehearing conference, I told the Division that its expert testimony should be "specifically targeted to the offenses alleged in the OIP" (Prehearing Conference of May 26, 2004, at 18). I then ordered the Division to identify its expert and provide the information required by Rules 222(a) and (b) of the Commission's Rules of Practice (Scheduling Order of May 27, 2004, at 2). The Division asked me to "clarify" and "provide guidance" on whether it had to provide a brief summary of its expert's expected testimony, as required by Rule 222(a)(4) (Letter of June 7, 2004, from Division counsel to ALJ). The Division stated that it had not contemplated summarizing its expert's opinion so soon. I found this letter highly unusual, but provided the requested clarification in an attempt to focus attention on the issues in dispute. My Order of June 8, 2004, at 2, stated (emphasis in original):

> As to Rule 222(a)(4), I do not expect the parties to summarize the expected testimony and the expected conclusions of their experts. However, the parties must identify the specific issues their experts will address. For example, if the Division states on June 14 that its expert will offer opinion testimony on Issues A, B, and C, then Respondents may rely on that statement in choosing their expert and preparing their defense. I would not expect the Division's expert to address Issues D, E, and F when that expert submits his testimony on July 19.

This turned out to be a poor choice of words on my part. Instead of saying "Issues A, B, and C," I should have said "Material Omissions A, B, and C." When the Division identified the subjects its expert would address, it stated only that the expert would opine on "[w]hether the [POS and OS] omitted information that would have been important to the reasonable investor" (Declaration of Division counsel, dated June 14, 2004, at 1-2). Respondents did not react to this lack of specificity at the time, and neither did I.

Four weeks before the start of the hearing, the Division filed the report of its expert witness (DX 94). Pope developed a broad list of information that, in his judgment, should have been disclosed in the POS and OS (Tr. 1065-66, 1105-06, 1133-34, 1142-43). His report roamed

well beyond the grounds for liability identified in the OIP, perhaps because he prepared his report without consulting the OIP more than once or twice (Tr. 1087, 1091, 1133-34).

Rule 200(d)(1) of the Commission's Rules of Practice provides that the Commission may amend an OIP at any time to include new matters of fact or law. Rule 200(d)(2) of the Commission's Rules of Practice provides that an Administrative Law Judge may amend an OIP at any time before filing an Initial Decision to include new matters of fact or law that are within the scope of the original OIP. In both instances, a motion by a party is required. The Division prudently moved to amend the OIP in Borgardt, which resolved the problem in that proceeding. The Division has not moved to amend the OIP here.

D&B and Bradbury argued that reliance on Pope's extraneous opinions would be unfair and a violation of due process (Tr. 1157-58). I denied their motion to strike, without prejudice to renewal in the posthearing pleadings (Tr. 1158). D&B and Bradbury have not renewed their motion to strike.

The rules of practice of several federal agencies provide that, when issues not raised by the pleadings are tried by the express or implied consent of the parties, the issues shall be treated in all respects as if they had been raised in the pleadings.[33] The SEC's Rules of Practice have no comparable provision. However, the Commission determined in Wheat, 80 SEC Docket at 3424, that due process is satisfied where the party against whom a proceeding is brought understands the issues and has an opportunity to meet the charges. The Commission reasoned that the question on review is not solely the adequacy of the particular pleading, but the fairness of the entire proceeding.[34] Id.

Respondents have not suffered substantial prejudice here. They received Pope's report well in advance of the hearing. Respondents have defended on the theory that PennDOT's anticipated move was immaterial because of the Commonwealth's swing space intentions (D&B Prehearing Br. at 25; D&B Br. at 16; D&B Reply Br. at 2; PFC Prehearing Br. at 24; PFC Reply Br. at 5). Doty spent a considerable amount of time parsing the OIP to determine what was being alleged (Tr. 1581-83). He ultimately arrived at a definition of "subject information" that was quite broad and included the matters set forth above (RX 41 ¶ 67.KKK). Doty then assumed that all of the "subject information" would have been important to a reasonable investor (Tr.

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[33] Comptroller of the Currency (12 C.F.R. § 19.20(b)); Federal Reserve System (12 C.F.R. § 263.20); Federal Deposit Insurance Corporation (12 C.F.R. § 308.20(b)); Federal Trade Commission (16 C.F.R. § 3.15(a)(2)); Commodity Futures Trading Commission (17 C.F.R. § 10.24(d)).

[34] The Commission also stated that administrative pleadings are "very liberally" construed, and that courts grant agencies considerable latitude in "interpreting" charging documents. I do not understand this to mean that the Division is free to ignore the conventions of "plain English" when it drafts an OIP for the Commission's consideration. Nor do I understand it to mean that the Division is entitled to Chevron deference when "interpreting" its inartfully phrased work product.

1483-84). In short, he conceded this information was material and focused his attention on whether D&B and Bradbury had acted reasonably in deciding not to disclose it (Tr. 1484). Doty's approach does not bind PFC and Fowler, but those two Respondents have remained silent on the "lack of fair notice" issue.

I conclude that these three omissions involved matters that were important to reasonable investors, and should have been disclosed in the POS and OS.

D. Liability of D&B and Bradbury.

The Underwriter's Responsibility
for Reviewing a POS and OS

Under the Commission's 1989 and 1994 Interpretive Statements, an issuer is primarily responsible for the content of its disclosure document, while an underwriter is a reviewer of that document with affirmative investigatory responsibilities. The underwriter is thus a crucial element in the municipal securities disclosure process.

Underwriters purchase municipal securities from issuers and resell them to public investors. The Commission considers such underwriters to be recommending to the investing public the municipal securities they offer and sell, and it requires them to have a reasonable basis for their recommendations. Under Rule 15c2-12, underwriters of municipal securities are required to review in a professional manner the issuer's OS for possible inaccuracies and omissions. Underwriters are required to conduct an affirmative investigation or inquiry that is sufficient to form a reasonable basis for belief in the accuracy and completeness of the "key representations" in the OS.[35] In offering and selling municipal securities, underwriters cannot merely accept at face value the issuer's key representations. In addition, underwriters of municipal securities have a responsibility to disclose material information of which they are aware (RX 41 ¶¶ 21, 74).

Bradbury is a very experienced underwriter of municipal bonds. By 1998, he had worked as a public finance investment banker for approximately thirty years (Tr. 662-63). D&B was one of the leading underwriters of municipal securities in Pennsylvania (Tr. 838-39; RX 28). In addition, Bradbury was a driving force behind the concept of having municipal authorities acquire office buildings that lease space to qualified tenants on short-term and intermediate-term leases, and then financing the acquisition through long-term non-taxable bonds. By June 1998, having just underwritten the Capitol Associates and Riverfront transactions, Bradbury had particular knowledge of the risks involved in issuing long-term bonds secured by short-term and intermediate-term leases. He also knew what potential investors considered important

[35] Rule 15c2-12 governs an underwriter's review of an OS, but it does not extend to Bradbury's review of Fowler's financial projections or the appraisal. Those documents were not a part of the OS (Tr. 1558). Of course, the antifraud provisions of the federal securities laws still apply, but without the gloss provided by Rule 15c2-12 and the Commission's Interpretive Statements.

information in evaluating those risks (Tr. 709). Finally, Bradbury knew of PennDOT's anticipated move from Forum Place to the Keystone Building.

Bradbury Has Not Presented Credible
Evidence of Good Faith Reliance on Counsel

As underwriter for the bonds, D&B did not obtain from the Authority or any other source a general representation as to the accuracy and completeness of the OS taken as a whole (DX 94 ¶¶ 56, 69.f). To compensate for that, Bradbury argues that he was entitled to "rely upon, or certainly take into account" the fact that no member of the finance team ever discussed with him whether PennDOT's anticipated move should be disclosed in the POS or OS (D&B Br. at 15-18). He maintains that his lack of scienter is demonstrated by the fact that Sweet thought about the need to disclose PennDOT's anticipated move, concluded that it need not be disclosed, and proceeded with the transaction.[36] Bradbury also offers a broad reading of bond counsel's supplemental opinion letter, and contends that he took that letter into consideration, as well.

In considering assertions of reliance on the advice of counsel, the Commission looks to see whether four factors have been established: (1) a request to counsel for advice on the legality of a proposed action, (2) full disclosure to counsel of the relevant facts, (3) receipt of advice that the action to be taken will be legal, and (4) reliance in good faith on counsel's advice. Borgardt, 80 SEC Docket at 3578 & n.37. "[R]eliance on the advice of counsel need not be a formal defense; it is simply evidence of good faith, a relevant consideration in evaluating a defendant's scienter." Howard, 376 F.3d at 1147.

Doty attempted to distinguish between "relying on" the opinion of counsel and "taking into consideration" the opinion of counsel (RX 41 ¶¶ 637-39, 642). He suggested that "taking into account" the opinion of counsel "may be a more useful measure" for evaluating a respondent's alleged recklessness than "relying on" the opinion of counsel (RX 41 ¶ 642). I disagree. Adopting Doty's distinction would completely eviscerate the Commission's existing test, because the Commission considers reliance on counsel evidence only when the underlying violation involves scienter. See McLaughlin, Piven, Vogel, Sec., Inc., 52 S.E.C. 1164, 1168 n.14 (1996); David M. Haber, 52 S.E.C. 201, 206 (1995). If D&B and Bradbury believe that "reliance lite" should be the proper standard, they must present their argument to the Commission.

Pepper Hamilton, through Sweet, was bond counsel for the Authority. The Division goes too far when it argues that Bradbury could not in good faith rely on the advice of someone else's attorney. As Pope acknowledged, Sweet had just finished serving as underwriter's counsel for D&B in the Riverfront transaction and it would have been appropriate for Bradbury to consider

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[36] Bradbury has abandoned any claim that he relied on O'Neill's advice. Bradbury failed to make a complete disclosure of the facts to O'Neill. O'Neill did not know about PennDOT's anticipated move, the June 30 meeting with Crowell, or D&B's distribution of financial projections to prospective investors (Tr. 354, 360-61, 363). Bradbury has also abandoned any claim that he relied on Hendershot or Fowler.

Sweet's conduct and opinions in the Forum Place transaction (Tr. 1152). Instead of resting my decision on this basis, I reject D&B's argument on narrower grounds.

The record does not show that Sweet ever gave Bradbury any legal advice about the facts omitted from disclosure. Sweet could not recall sharing his views on whether the OS should disclose PennDOT's anticipated move with any member of the finance team (Tr. 102, 104-05, 116-18, 690-93). Doty assumes that Bradbury learned of Sweet's views indirectly, but his reasoning is strained (Tr. 1545).

Sweet and Pope disputed Bradbury's and Doty's broad reading of the supplemental bond counsel opinion letter (Tr. 70-72, 1111, 1143-44, 1540-43, 1547-49; DX 28; RX 41 ¶¶ 94, 130, 368, 375-94, 719-56). At issue is the language of the last paragraph of the supplemental opinion letter. Pepper Hamilton's role as bond counsel required Sweet to make fair and accurate summaries of the documentation (Tr. 397). The customary purpose of the language in the supplemental opinion letter is to provide comfort that the summaries or descriptions of the document provisions governing the security were adequate and fair (Tr. 1108). It is not to provide an opinion that there is no information relating to those provisions that should be the subject of disclosure (Tr. 1108). Bradbury's and Doty's reading of the supplemental opinion letter is unreasonable.

I conclude that Bradbury could not, in good faith, have relied on the legal advice purportedly given to him by Sweet.

Bradbury Acted Recklessly

There is no evidence that D&B or Bradbury attempted to restrict the free flow of information to prospective investors. On the contrary, if D&B did not have the information an investor needed, the firm referred the investor to Fowler, Sweet, and/or Crowell. D&B also arranged tours of Forum Place and invited prospective investors to speak freely with Vartan. Bradbury orally informed Putnam Investments, the single largest purchaser of the bonds, about PennDOT's anticipated move from Forum Place. It is not plausible to conclude that, if other investors had asked, he would have intentionally withheld the same information from them.

The POS and OS disclosed the short-term nature of the leases, the fact that the leases expired before the bonds matured, and the fact that there was no commitment, requirement or guarantee that the Commonwealth would renew or extend any of its leases. In conveying this disclosure, the POS and OS used bold fonts and capital letters. Although this Initial Decision finds that the disclosure was incomplete, this was not a situation where there was no disclosure at all. Likewise, Bradbury added explanatory footnotes to Fowler's financial projections before circulating them to prospective investors. I agree with the Division that the footnote disclosure should have been more extensive. Nevertheless, Bradbury did not take Fowler's document and attempt to make it more deceptive. The fact that Bradbury supplemented Fowler's document is entitled to some weight in negating scienter.

There is no evidence that Bradbury consciously rejected a suggestion from other members of the finance team to disclose material information in the POS or OS. Finally, it is

counterintuitive to think that Bradbury would intentionally defraud his best customers or that he would knowingly involve his daughter, who had just earned her securities licenses, in a scheme to defraud.

D&B bought subordinated Series B bonds for its own portfolio. The Series B bonds carried greater risk than the Series A bonds sold to the investors who testified at the hearing. Respondents argue that it is highly unlikely that Bradbury would have made this purchase if he had been engaged in a scheme to defraud. I would agree if D&B had retained these bonds in its portfolio; however, it sold them a few months later in the secondary market (Tr. 820-21). The Series B bond purchase is entitled to limited weight in evaluating Bradbury's state of mind.

The Division is not required to show that a respondent acted knowingly or intentionally in order to prevail. A lesser showing of recklessness is sufficient. The weight of the evidence persuades me that Bradbury acted recklessly.

Bradbury was reckless in failing to inform O'Neill, the lawyer he hired to draft the disclosure document, about PennDOT's anticipated move to the Keystone Building and the near certainty that PennDOT would not renew its lease at Forum Place. He was reckless in allowing O'Neill to draft the POS without correcting two of O'Neill's assumptions: first, that the short-term leases at Forum Place would not be a problem because "that's the way business is done in Harrisburg;" and second, that institutional investors were already satisfied with the transaction before they read a POS with appropriate disclosure (Tr. 351).

Bradbury claims to have been told by Fowler that the June 30 meeting with Crowell resulted in no guarantees as to Forum Place's future use as swing space (Tr. 719-20). Bradbury never knew for how long the Commonwealth might use Forum Place as swing space (Tr. 716). Bradbury did not attempt to verify Fowler's report. He did not discuss the swing space program directly with Crowell to determine what could be fairly said about it to investors, or even to understand the scope of the program, the likelihood of funding, or the period of time for which it would produce demand for space at Forum Place (DX 94 ¶ 42). In my judgment, this was reckless. Bradbury was also reckless in telling a prospective investor that there would generally be a lot of demand at Forum Place and that departing government agencies would be quickly replaced (Tr. 545-46).

Bradbury did not organize or participate in any substantial discussions with the finance team to analyze the accuracy or completeness of the POS. He did not conduct a page-by-page review of the POS as a device to raise questions and promote full and complete disclosure. Such a detailed review is customary in the industry (DX 94 ¶¶ 23-24, 44). Bradbury's review of the POS was cursory, at best.

The single most important date in this proceeding was August 1, 1998. It is no coincidence that the Forum Place transaction closed one day before the T&S Building was imploded. I credit testimony that the Forum Place offering was somewhat rushed, and pushed to closing by July 31, 1998 (Tr. 23-24, 347-49, 1275). I give significant weight to the fact that Bradbury failed to inquire about the construction schedule for the Keystone Building while he was marketing the bonds to public investors (Tr. 689-90). I find that Bradbury's failure to

inquire about the construction schedule was deliberate—he simply did not want to know this readily available information. Before the implosion of the T&S Building and without actual knowledge of the construction schedule for the Keystone Building, Bradbury could plausibly maintain that PennDOT's anticipated move to the Keystone Building was still uncertain. If the bond offering had closed after August 1, 1998, or if Bradbury had actual knowledge of the construction schedule, he could not have done so.

Bradbury's professed readiness to disclose material information if an investor asked the right questions cannot excuse the failure to disclose such information in the POS and OS. "Readiness and willingness to disclose are not equivalent to disclosure." Hughes v. SEC, 174 F.2d 969, 976 (D.C. Cir. 1949). McCormack learned of PennDOT's anticipated move only because she dug for the information in what she characterized as "an iterative process" (Tr. 486). I am persuaded that Bradbury's commitment to full disclosure in the POS and OS was grudging. In essence, Bradbury's approach was: If a prospective investor asks a direct question, I will answer it truthfully; however, there is no need to volunteer information if the prospective investor does not ask. On the whole, I find that Bradbury was reckless.

Bradbury's recklessness may be imputed to D&B. See In re Sunbeam Sec. Litig., 89 F. Supp. 2d 1326, 1340 (S.D. Fla. 1999); SEC v. Blinder, Robinson & Co., 542 F. Supp. 468, 476 n.3 (D. Colo. 1982).

D&B's and Bradbury's Violations

I conclude that D&B and Bradbury willfully violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder, in that they recklessly offered and sold Forum Place bonds to investors on the basis of a materially misleading POS, OS, and financial projections.

I also conclude that D&B and Bradbury willfully violated MSRB Rule G-17 by failing to deal fairly with all persons and by engaging in a deceptive, dishonest, or unfair practice, namely, failing to disclose all material facts concerning a municipal securities transaction. I conclude that they failed to exercise reasonable care and competence, and thus were negligent. I further conclude that they were reckless within the meaning of Sundstrand.

Finally, I conclude that D&B willfully violated Section 15B(c)(1) of the Exchange Act by inducing the purchase and sale of Forum Place bonds in contravention of MSRB Rule G-17. D&B's conduct was at least negligent. In addition, Bradbury knowingly and substantially participated in D&B's violation of Section 15B(c)(1) through conduct that was extremely reckless within the meaning of Howard. Accordingly, I conclude that Bradbury willfully aided and abetted and caused D&B's violation of Section 15B(c)(1).

E. Liability of PFC and Fowler.

The Authority Committed Primary Violations of
Sections 17(a)(2) and 17(a)(3) of the Securities Act

The Commission has explained that municipal securities "issuers are primarily responsible for the content of their disclosure documents and may be held liable under the federal securities laws for misleading disclosure." 1989 Interpretive Statement, 43 SEC Docket at 2257 n.84. Here, the Authority negligently omitted to state material information in its POS and OS for the Forum Place bonds.

On July 8, 1998, the Authority met to discuss the Forum Place transaction, approve the issuance and sale of the bonds to D&B, ratify the content of the POS, and authorize the distribution of the POS and OS. The Authority had actual knowledge of PennDOT's anticipated move and was aware of the potential effect of that move on the viability of the bond offering. Nonetheless, the Authority never discussed whether prospective investors should be advised of PennDOT's anticipated move. The Authority approved the distribution of the POS and OS without taking steps to ensure that those documents were not misleading and contained all the necessary disclosures of material information.[37] Accordingly, I conclude that the Authority negligently violated Sections 17(a)(2) and 17(a)(3) of the Securities Act.

PFC's and Fowler's Liability for
Causing the Authority's Violations

OIP ¶ III.D.4 alleges that Fowler had a fiduciary relationship, or a similar relationship of trust and confidence, with the Authority. It further asserts that the Authority members "trusted and relied upon PFC and Fowler to ensure that . . . all documents, including the [OS], were complete, accurate, and contained all necessary disclosures." OIP ¶ III.E.9 claims that Fowler did not discuss with the Authority at the July 8 meeting or at any other time "that the [OS] was misleading and required disclosure of PennDOT's scheduled move to the Keystone Building." It also charges that Fowler, who is not an attorney, "did not inform the Authority of its potential liability for failing to disclose the existence of the Keystone Building or PennDOT's scheduled move."

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[37] The Authority did not authorize the distribution of Fowler's financial projections or the March 1997 appraisal to prospective investors, and my conclusions about the Authority's violations do not extend to those two documents. Although an OS may consist of a "set of documents," see Exchange Act Rule 15c2-12(f)(3), the Division has not tried this case on the theory that the financial projections and the appraisal should be considered as a part of a set of documents that collectively comprised the OS. The OIP consistently treats these three documents as entirely separate, as does Pope (DX 94 ¶ 14). Moreover, the Authority informed prospective investors that "no . . . person has been authorized to give information or to make any representation not contained in this OS and, if given or made, such other information or representation must not be relied upon" (DX 16 at 4). Because the Authority committed no primary violations as to these two documents, PFC and Fowler cannot be liable for "causing" such violations.

It Is Not Enough for the Division to
Argue that Fowler Was a Fiduciary

The term "financial advisor" is not defined in the federal securities laws. While MSRB Rule G-23(b) defines a "financial advisory relationship" for brokers, dealers, and municipal securities dealers, the MSRB Rules are not applicable to financial advisors who are not brokers, dealers, or municipal securities dealers.[38] The plain language of Exchange Act Rule 15c2-12 applies to underwriters of municipal securities, but it does not extend to financial advisors. The Commission's Interpretive Statements do not address the question of whether financial advisors in negotiated offerings have obligations to review issuer disclosure.[39]

The Division appears to assume that it will prevail against PFC and Fowler if it simply labels them as fiduciaries. It further assumes that, if PFC and Fowler were fiduciaries for any purpose and at any time, they must have been fiduciaries for all purposes and at all times. However, the Restatements of the law and judicial opinions applying them clearly require more.

"An agent is a fiduciary with respect to matters within the scope of his agency." Restatement (Second) of Agency § 13 (1957). "An agent is not . . . in a fiduciary relation with the principal as to matters in which he is not employed." Id. § 390, comment d at 211; cf. Restatement (Second) of Trusts § 2, comment b (1959) ("A person in a fiduciary relation to another is under a duty to act for the benefit of the other as to matters within the scope of the relation.").

"[T]o say that a man is a fiduciary only begins the analysis, it gives direction to further inquiry. To whom is he a fiduciary? What obligations does he owe as a fiduciary?" SEC v. Chenery, 318 U.S. 80, 85-86 (1943). "[A]fter establishing that a fiduciary relationship exists, it is still necessary to determine whether the conduct at issue falls within the scope of that

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[38] The Division relies on Wheat, 80 SEC Docket at 3419 & n.26, which defines a financial advisor's fiduciary duty to a municipal issuer by reference to MSRB Rule G-17 and a settlement order involving a broker-dealer functioning as a financial advisor. The Division improperly ignores other language in Wheat, 80 SEC Docket at 3424, which construes MSRB Rule G-17 as applying only to financial advisors who are registered brokers, dealers, and municipal securities dealers, but not to financial advisors who are not so registered.

[39] The Commission recognized that issuers often employ financial advisors to assure the accuracy and completeness of disclosure in competitively bid offerings. See 1988 Interpretive Statement, 41 SEC Docket at 4114 n.92. It observed that where such financial advisors participate in drafting the disclosure documents, they will have an obligation under the antifraud provisions, comparable to that of the underwriter, to inquire into the completeness and accuracy of disclosure presented during the bidding process. Id. Nothing in the 1988 Interpretive Statement addresses the disclosure role of financial advisors in negotiated transactions, such as Forum Place. Nothing in the Interpretive Statement addresses the role of financial advisors who are not registrants and who do not participate in drafting disclosure documents.

relationship and whether the conduct is inconsistent with fiduciary obligations arising from that relationship." E.F. Hutton & Co., 49 S.E.C. 829, 837 n.10 (1988) (Chairman Ruder, concurring). "Nothing . . . in the general principles of agency law indicates that an agent's fiduciary obligations extend to matters not included in the agent's employment or contractual relationship." Productive Automated Sys. Corp. v. CPI Sys., Inc., 61 F.3d 620, 622 (8th Cir. 1995). "A fiduciary duty . . . cannot be defined by asking the jury to determine simply whether the principal reposed 'trust and confidence' in the agent. The jury should have been instructed to decide first what [the purported agent] had agreed to do for [the purported principal] and then to determine whether [the purported agent] executed those tasks properly." Hill v. Bache Halsey Stuart Shields, Inc., 790 F. 2d 817, 824 (10th Cir. 1986).

The Scope of the Typical Financial Advisor's
Relationship to the Typical Municipal Issuer

The general rule is that the "existence and extent of the duties of the agent to the principal are determined by the terms of the agreement between the parties, interpreted in light of the circumstances under which it is made." Restatement (Second) of Agency § 376 (1957).

The testimony in this proceeding was consistent with the general rule. Pope opined that the precise role of a financial advisor in a municipal securities offering "varies widely" and is effectively determined by the agreement or other understanding between the advisor and the issuer that retains the advisor (DX 94 ¶ 19). The issuer may look to the advisor to participate in all aspects of a transaction, including the production of disclosure, or the issuer instead may employ the advisor for a limited purpose (DX 94 ¶ 19).

Pope further opined that financial advisors frequently play "a particularly large and important role" in serving special purpose authorities (DX 94 ¶ 20). He explained that such authorities "frequently rely extensively and sometimes exclusively on financial advisors for a wide range of issues" (DX 94 ¶ 20). Such tasks "frequently include . . . reviewing disclosure language for offering documents" (DX 94 ¶ 20). When asked if authorities typically look to their financial advisors for financial advice and their legal advisors for legal advice, Pope responded: "Yes. There's a lot of overlap there, but yes, I agree with that" (Tr. 1136-37).

Fowler's Course of Dealing
with the Authority and Other Issuers

In 1998, Fowler was an experienced financial advisor who had worked as a public finance investment banker, held himself out as an expert in the structuring of municipal bond issues, and provided assistance to special governmental authorities. He had a long-standing relationship with the Authority, which looked to him for advice on matters relating to structuring and issuing bonds. Earlier in his career, Fowler had written offering documents. Fowler typically reviewed the financial terms in offering documents and informed the issuers whether they were reasonable (Tr. 874-75).

Fowler explained that PFC's role as a financial advisor varies from transaction to transaction, and "depends upon . . . what we're asked of by the issuer" (Tr. 873). Sometimes,

PFC would earn an advisory fee of $1,000 or less; on other occasions, its advisory fee would be as high as $200,000 or $220,000 (DX 1). Fowler explained that PFC had no typical role in advising the Authority (Tr. 926). On some transactions, the Authority would ask PFC to take a quick look at one or two documents (Tr. 926). On other transactions, PFC was heavily involved in structuring and document review (Tr. 926-27).

Over the years, the Authority relied on Fowler to perform a wide range of duties. At one time or another, these duties included soliciting potential bond transactions, reviewing potential bond transactions identified by others, ensuring that the transactions were properly structured, making the necessary contacts with interested parties, developing and collecting information, calculating debt service coverage, recommending the underwriter and bond counsel, and assessing the viability of the transactions. However, the record does not support a finding that Fowler performed each of these duties on each transaction for which PFC served as financial advisor to the Authority.

The Scope of Fowler's Engagement with
the Authority on the Forum Place Transaction

The issue for decision is whether the Authority relied on Fowler to alert it to inadequate disclosure language in the Forum Place POS and OS and to inform it of its potential liability for inadequate disclosure.

Fowler believed that the Authority was relying on him to review the OS in the Forum Place transaction (Tr. 920). However, just as there is no common understanding in this proceeding as to what "Class A office space" means, there is no common understanding of what "review" of a POS and OS means. The Division assumes that a financial advisor's duty to "review" the accuracy of an issuer's disclosure document is just as broad as an underwriter's duty to "review" it under Exchange Act Rule 15c2-12 and the Commission's Interpretive Statements.[40]

Fowler did not read the POS line-by-line. Instead, he looked at the description of the Authority in the POS to ensure that names were spelled correctly. He verified that the numbers were correct (Tr. 918). He also determined that the POS had the same type of disclosure information that appeared in the earlier Capitol Associates and Riverfront disclosure documents (Tr. 918-20). During his review of the POS, Fowler was aware that PennDOT's anticipated move to the Keystone Building was not disclosed (Tr. 919-20). He did not discuss with the Authority the fact that the POS did not include any reference to PennDOT's proposed move (Tr. 920).

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[40] Not all document reviews are equal in intensity. At one time, the Commission's staff used four different levels of review when examining registration statements. See Securities Act Rel. No. 5231, The Division of Corporation Finance's Procedures Designed to Curtail Time in Registration Under the Securities Act of 1933, 37 F.R. 4327 (Mar. 2, 1972) (describing deferred review, cursory review, summary review, and customary review procedures).

The Terms of the Agreement Between Fowler and the Authority. The first point to consider is the terms negotiated between the Authority and Fowler. Although Fowler's relationship with the Authority was based on a handshake, one aspect of the Forum Place engagement agreement was memorialized by a contemporaneous writing. In its POS and OS, the Authority stated unequivocally that PFC "is not obligated to undertake, and has not undertaken to make, an independent verification or to assume responsibility for the accuracy, completeness, or fairness of the information contained in this [POS and OS]" (DX 15 at 18, DX 16 at 20). The Division and PFC did not develop the record as to whether this language was routinely a part of the Authority's offering documents or if it was highly unusual. Nor did they develop the record as to whether the language was originally crafted by the Authority or by PFC, or as to what sort of negotiations (if any) may have preceded its inclusion in the POS and OS.

Fowler believes that this language is strong evidence that the scope of his engagement was limited. He has raised this argument throughout the proceeding (PFC Answer; PFC Prehearing Br. at 2-3; PFC Br. at 8, 27, 32-35; PFC Reply Br. at 6-8). Unfortunately, Pope ignored this language in his report, and the Division devoted only two sentences to the issue in its posthearing pleadings (Div. Reply to PFC at 17). Neither of the Division's arguments is persuasive.[41]

The Commission encountered similar language limiting the responsibilities of the financial advisors to a municipal bond issuer in City of Miami, 79 SEC Docket 3362, 3379-80 n.45 (Mar. 21, 2003). However, it did not reach the issue of whether the financial advisors in that proceeding fulfilled their responsibilities with respect to the offerings. Id.

In County of Nevada, 70 SEC Docket at 3328, the OS stated that it should not be considered a representation of the financial advisor. However, in that proceeding, the financial advisor and the issuer executed a written contract that required the financial advisor to prepare the POS and OS. Id. at 3310-11. In effect, the financial advisor assumed the underwriter's responsibilities under Exchange Act Rule 15c2-12. Under those circumstances, the Chief Administrative Law Judge was not persuaded by the limiting language in the OS.

The Commission has cautioned underwriters not to disclaim responsibility for an issuer's representations in an OS. See 1994 Interpretive Statement, 56 SEC Docket at 606 n.103. The Commission's warning did not extend to financial advisors.

I conclude that the language in the POS and OS defined the limits of PFC and Fowler's engagement on the Forum Place transaction in that Fowler was under no duty to speak to the

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[41] The Division contends that the language applies only to whether PFC and Fowler have any direct responsibility to investors. It is not clear what direct responsibility to investors might entail, inasmuch as there is no implied private right of action under Section 17(a) of the Securities Act. See In re Washington Pub. Power Supply Sys., 823 F.2d 1349, 1358 (9th Cir. 1987) (en banc). The Division also contends that the language is irrelevant to PFC's and Fowler's obligations to the Authority. I consider the language in question to be highly relevant to determining the scope of PFC's and Fowler's obligations to the Authority.

Authority about perceived disclosure deficiencies in the offering document.[42] I further conclude that the limiting language did not operate as a prospective waiver of liability for acts that were within the scope of Fowler's engagement. Accordingly, I do not consider the language to be an exculpatory clause.[43]

Congress has not forbidden such limiting language by statute and the Commission has not forbidden it by regulation, interpretive statement, or adjudicatory opinion. Accordingly, I conclude that the language in the POS and OS should be treated just like any other negotiated term. The Authority had sufficient financial savvy to become the second largest bond issuer in Pennsylvania. It had enough hubris to attempt to change its name to the "General Authority of Pennsylvania." I conclude that the Authority should have been able to understand the language defining the scope of Fowler's engagement and, if it did not like the language, should have negotiated something different. If the Authority had insisted that Fowler perform a broader range of duties, Fowler could have negotiated a higher fee or withdrawn from the engagement.

There can be no serious argument that Fowler sneaked this language past the Authority on July 8, 1998, when the members of the Authority did not have enough time to consider it. Nor can there be a suggestion that the language originated with O'Neill. Identical language appeared in the Authority's POS for the Riverfront transaction (DX 18 at 19) and in the Harrisburg Authority's OS for the Capitol Associates transaction (DX 19 at 20). There is no evidence that the issuers in these earlier transactions lacked an opportunity to consider carefully the wording of their disclosure documents.

<u>The Surrounding Facts and Circumstances.</u> The second task is to interpret the terms of an agreement in light of the circumstances under which it was made. Here, the inquiry depends on the faded six-year-old memories of Ricci and Milke. It is also restricted by the principle that no one member of the Authority can purport to speak for the Authority as a body.[44]

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[42] A fiduciary relationship creates a duty to speak. <u>See</u> <u>Chiarella v. United States</u>, 445 U.S. 222, 228 (1980). However, to establish the parameters of a fiduciary relationship, the Division must first establish the scope of the underlying principal-agent relationship. Labeling Fowler a fiduciary for the purpose of creating a duty to speak is bootstrapping.

[43] If the Division believed the language to be an exculpatory clause, it might have developed the record and presented argument on whether exculpatory clauses are considered valid and enforceable under Pennsylvania law. <u>See</u> <u>Keystone Aeronautics Corp. v. R.J. Enstrom Corp.</u>, 499 F.2d 146, 149-50 (3d Cir. 1974); <u>Neuchatel Insur. v. ADT Security Sys., Inc.</u>, 1998 U.S. Dist. LEXIS 17692 at *13-16 (E.D. Pa. Nov. 6, 1998). The Division elected not to do so.

[44] If the negotiated terms memorialized in the POS are considered to be a written contract, there is also a question as to whether Pennsylvania's parol evidence rule applies. In addition, there is a question as to whether any views a federal administrative agency might express about Pennsylvania contract law would receive deference on judicial review. <u>Cf.</u> <u>Anspacher & Assoc., Inc. v. Henderson</u>, 854 F.2d 941, 947 n.2 (7th Cir. 1988).

When Ricci was asked if he relied on Fowler to review the bond offering documents, Ricci explained: "I relied on everybody when it came to documents . . . I looked to everyone in the room and not just Mr. Fowler" (Tr. 1408-09). I did not find this testimony particularly helpful in understanding the scope of Fowler's agency. It was merely another version of Pope's observation that "there's a lot of overlap there." The Division never asked Ricci whether he expected Fowler to review the POS and OS for all purposes or for the specific purpose of evaluating the sufficiency of the disclosure language.[45] Ricci also stated that Fowler "probably always asked questions beyond his scope because of his experience in the area" (Tr. 1408). Asking questions is not the same as assuming duties.

Milke had three opportunities to shed light on the scope of Fowler's engagement with the Authority. First, she stated: "We relied on either our solicitor to have reviewed [disclosure in the OS] or bond counsel to know what the material was in there. And I guess I would have thought that Mr. Fowler would know that as well" (Tr. 23) (emphasis added). Second, Milke stated: "[W]e relied on our professionals to determine what should be disclosed in the [Forum Place OS], as we would with any other bond issue" (Tr. 25). When asked to identify the professionals, she responded: "Our solicitor, Mr. Hendershot, who should have reviewed the documents on our behalf, our financial advisor, who would have known all of the information, and the bond counsel for the issue" (Tr. 26). However, when Milke was then asked whether the Authority relied on Fowler for legal advice, she answered "no" (Tr. 27).

Milke's testimony that the Authority did not rely on Fowler for legal advice is consistent with anecdotal evidence provided by Fowler. Approximately six or seven months before the Forum Place offering, the Authority engaged PFC to act as its financial advisor on a large health care pool bond transaction (Tr. 879-80, 985-86). Fowler became uncomfortable with the structure of that transaction and advised the Authority not to proceed. According to Fowler, that advice led to a confrontation between PFC and the bond counsel on the offering. The attorney delivered an ultimatum to the Authority: "I guess the Authority is going to have to decide whether [it] take[s its] legal advice from [me] or from [PFC]" (Tr. 986). The Authority chose to proceed with the transaction and PFC resigned as financial advisor (Tr. 879-80, 985-86). In light of that earlier confrontation, Fowler could reasonably expect that the Authority would not rely on him for legal advice on subsequent bond offerings.

The language in the POS and OS describing the limits of Fowler's engagement, coupled with Milke's testimony that the Authority did not rely on Fowler for legal advice, demonstrates the Authority's expectations as to the actual scope of Fowler's responsibilities. Fowler's confrontation with bond counsel and his resignation as financial advisor on a previous transaction demonstrates Fowler's expectations about the actual scope of his responsibilities. PFC and Fowler are entitled to the benefit of the bargain they struck with the Authority limiting the scope of their engagement on Forum Place.

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[45] Div. Prop. Find. # 305 asserts that the Authority looked to PFC and Fowler to participate in all aspects of the Forum Place transaction, including the production of disclosure. The transcript page cited by the Division does not support the assertion.

Based on the hearing record, I conclude that it was beyond the scope of PFC's and Fowler's engagement to advise the Authority about the accuracy, completeness, or fairness of the disclosure language in the Forum Place POS and OS.[46] It was also beyond the scope of their engagement to inform the Authority of its potential liability for failing to disclose material information. I further conclude that the weight of the evidence fails to demonstrate that the Authority relied on PFC and Fowler for these purposes, or that PFC and Fowler were fiduciaries for these purposes. Finally, I conclude that Fowler had no duty to speak on disclosure issues on July 8, 1998, or at any other time. The Division has failed to prove a sufficient nexus between Fowler's silence and the Authority's violations.

On that basis, I conclude that PFC and Fowler were not shown to be "a cause" of the Authority's violations of Sections 17(a)(2) and 17(a)(3) of the Securities Act.

F. The Actions of the Authority, November 1999 to July 2003.

As a final matter, Respondents contend that the Authority mismanaged Forum Place between November 1999 and July 2003. They argue that this mismanagement, and not any disclosure defects in the POS and OS, proximately caused the default of the bonds and the losses sustained by the bondholders (D&B Br. at 33-35, PFC Br. at 35-39).

The question of intervening causation is not relevant to the liability issues in the case: whether the POS, OS, financial projections, and appraisal were materially misleading to prospective investors. The resolution of the liability issues is not changed in any way by events occurring after July 31, 1998.[47]

The question of intervening causation is also irrelevant to the proposed disgorgement of ill-gotten gains. See SEC v. Bilzerian, 29 F.3d 689, 697 (D.C. Cir. 1994) ("Whether or not [Respondents'] securities violations injured others is irrelevant to the question of whether disgorgement is appropriate.").

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[46] Doty opined that Bradbury lacked scienter because Bradbury relied on Fowler's review of the POS. To support that opinion, Doty quoted passages from Fowler's investigative testimony (RX 41 ¶¶ 445-48). In other tribunals, mutually antagonistic defenses of this sort might entitle PFC and Fowler to a severance. See United States v. Zafiro, 506 U.S. 534, 539 (1993) (discussing the danger of reducing the prosecutor's burden by turning a co-defendant into a second prosecutor). Doty's opinion on this subject is no longer an active issue in the case. See supra note 36. However, to dispel any confusion, I find that the investigative testimony Doty cited to support his opinion is not properly a part of the hearing record for determining the liability of PFC and Fowler. Cf. Fed. R. Evid. 105, 703. All parties were aware that investigative testimony would not be considered as substantive evidence against Respondents unless the individual in question was confronted with his investigative testimony and given an opportunity to explain it. The Division never confronted Fowler with this aspect of his investigative testimony.

[47] Doty opined that relative fault disproves recklessness (RX 41 ¶¶ 38-39, 488). I do not find his reasoning persuasive. Moreover, D&B and Bradbury have abandoned this argument in their posthearing pleadings.

The question of intervening causation was relevant to the Division's request for third-tier civil monetary penalties at an earlier stage of the proceeding. At that juncture, the Division based its claim for third-tier penalties solely on the theory that D&B and Bradbury's antifraud violations "resulted in substantial losses" (Div. Prehearing Br. at 24). However, as the Division now observes, third-tier civil penalties may also be imposed on alternative grounds; namely, that the antifraud violations "created a significant risk of substantial losses to other persons" (Tr. 1253-54; Div. Br. at 41). If an alternative prong of the test is satisfied, see infra p. 68, then there is no need to engage in an extended discussion of whether the antifraud violations also may have "resulted in substantial losses." Thus, the Authority's alleged mismanagement of Forum Place is no longer a potential barrier to the imposition of third-tier civil penalties.

That does not necessarily end the inquiry, however, because the Division has requested that any civil penalties imposed against D&B and Bradbury be made payable to a distribution fund for the benefit of defrauded investors. The Commission has explained that such funds "must be disbursed to the investors harmed by the securities law violations at issue." Adoption of Amendments to the Rules of Practice and Delegation of Authority to the Commission, 82 SEC Docket 1744, 1746 (Mar. 12, 2004). Arguably, proof that investors were harmed by the securities law violations at issue would require a determination that intervening harm caused by others, such as the newly constituted Authority, should be ruled out. Because this Initial Decision declines to set up the proposed distribution fund, see infra p. 70, there is no need to consider whether the Authority's alleged mismanagement of Forum Place is an intervening and superseding cause of the harm suffered by investors. If the Division presses the Commission to establish such a distribution fund, Respondents may renew their arguments on appeal.

SANCTIONS

The Division seeks the imposition of cease-and-desist orders, disgorgement of ill-gotten gains, and prejudgment interest against all Respondents. In addition, the Division requests third-tier civil monetary penalties against D&B and Bradbury. Although the OIP also identified a registration revocation against D&B and an associational bar against Bradbury as possible sanctions under Sections 15(b) and 15B of the Exchange Act, the Division has never requested such sanctions in its pleadings (OIP ¶ IV.G; Div. Prehearing Br. at 21-25; Div. Prop. Find. at 105-10; Div. Br. at 39-42; Div. Reply to D&B at 24-25). I decline to impose a registration revocation or an associational bar on my own motion.

Cease-and-Desist Orders

Section 8A(a) of the Securities Act and Section 21C(a) of the Exchange Act authorize the Commission to impose a cease-and-desist order upon any person who "is violating, has violated, or is about to violate" any provision of the Securities Act, the Exchange Act, or the rules and regulations thereunder. The Commission may also impose a cease-and-desist order against any person that "is, was, or would be a cause of [a] violation" due to an act or omission the person "knew or should have known would contribute to such a violation."

The Commission has determined that the five-year limitation period of 28 U.S.C. § 2462 does not apply to cease-and-desist orders. See Coxon, 80 SEC Docket at 3314 n.60; Herbert Moskowitz, 77 SEC Docket 481, 500-02 (Mar. 21, 2002).

In KPMG, 54 S.E.C. at 1183-92, the Commission addressed the standard for issuing cease-and-desist relief. It explained that the Division must show some risk of future violations. However, it also ruled that such a showing should be "significantly less than" that required for an injunction and that, "absent evidence to the contrary," a single past violation ordinarily suffices to raise a sufficient risk of future violations. Id. at 1185, 1191.

Along with the risk of future violations, the Commission considers the seriousness of the violation, the isolated or recurrent nature of the violation, the respondent's state of mind, the sincerity of the respondent's assurances against future violations, the respondent's recognition of the wrongful nature of his or her conduct, and the respondent's opportunity to commit future violations. Id. at 1192. In addition, the Commission considers whether the violation is recent, the degree of harm to investors or the marketplace resulting from the violation, and the remedial function to be served by the cease-and-desist order in the context of any other sanctions being sought in the same proceeding. Id. The Commission weighs these factors in light of the entire record, and no one factor is dispositive.

The U.S. Court of Appeals for the District of Columbia Circuit has insisted that the Commission adhere to the standards it announced in KPMG. See WHX Corp. v. SEC, 362 F.3d 854, 859-60 (D.C. Cir. 2004) (rejecting the Commission's explanation of the risk of future violations and vacating a cease-and-desist order).

Addressing these factors here, I conclude that the violations were serious and created a substantial risk of loss to investors. D&B and Bradbury acted recklessly. Bradbury has not recognized the wrongful nature of his conduct and he has offered no assurances against future violations. D&B and Bradbury remain active in the industry, and there is both an opportunity for and a risk of future violations. The age and isolated nature of the violations and D&B's and Bradbury's otherwise clean disciplinary record militate against cease-and-desist relief, but overall, I believe these factors are outweighed by the other relevant considerations. I will grant the Division's request for cease-and-desist orders.[48]

Disgorgement

Section 8A(e) of the Securities Act and Section 21C(e) of the Exchange Act provide that the Commission may enter an order requiring disgorgement, including reasonable interest. Disgorgement seeks to deprive the wrongdoer of his ill-gotten gains. See SEC v. First City Fin. Corp., 890 F.2d 1215, 1230-32 (D.C. Cir. 1989). It returns the violator to where he would have

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[48] The Commission has not yet addressed the issue of whether an MSRB rule violation can be the basis for a cease-and-desist order under Section 21C of the Exchange Act. See Wheat, 80 SEC Docket at 3434-35 n.73. Accordingly, the wording of the cease-and-desist order here will follow the language the Commission used in Wheat.

been absent the violations. An order to disgorge a certain amount need only be a reasonable approximation of the profits causally connected to the violation. Id. at 1231.

Once the Division shows that its disgorgement figure reasonably approximates the amount of unjust enrichment, the burden of going forward shifts to the respondent to demonstrate clearly that the Division's disgorgement figure is not a reasonable approximation. SEC v. Lorin, 76 F.3d 458, 462 (2d Cir. 1996); SEC v. Patel, 61 F.3d 137, 140 (2d Cir. 1995). Any risk of uncertainty as to the disgorgement amount falls on the wrongdoer whose illegal conduct created the uncertainty. First City, 890 F.2d at 1232.

The five-year limitation period of 28 U.S.C. § 2462 does not apply to disgorgement relief. Johnson v. SEC, 87 F.3d 484, 489-91 (D.C. Cir. 1996); Feeley & Willcox Asset Mgmt. Corp., 80 SEC Docket 2075, 2101 n.65 (July 10, 2003); Joseph J. Barbato, 53 S.E.C. 1259, 1279 & n.27 (1999).

D&B purchased $3.1 million of Series B bonds from the Authority at a 1% discount from par and then resold those bonds at par (Tr. 851). Accordingly, for the Series B bonds, the proper amount of disgorgement by D&B and Bradbury is $3.1 million x .01 = $31,000.

D&B also purchased $72.25 million of Series A bonds from the Authority at a 1% discount from par. However, there is no evidence that D&B resold the Series A bonds at par and a great deal of evidence shows that D&B resold them at a discount of 3/8 of 1% from par (Tr. 424, 1239; DX 21-DX 23).[49] The weight of the evidence also shows that the resale price of the Series A bonds was determined by the marketplace in arms-length negotiations between D&B, on the one hand, and four institutional purchasers, on the other hand (Tr. 720-27). Accordingly, for the Series A bonds, the proper methodology for computing disgorgement by D&B and Bradbury is 5/8 of 1%, the difference between the purchase price and the resale price.[50] This equates to $451,562.50 (or $72.25 million x .00625).

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[49] The evidence of resale at $99.625 is persuasive as to the $55.6 million in Series A bonds maturing in 2025 (Tr. 1239; DX 21-DX 23). The evidence of the resale price is somewhat less persuasive as to the $16.65 million in Series A bonds maturing in 2003, 2008, and 2010 (Tr. 424, 726-27).

The issue is which party properly bears the burden of proof. Given the evidence that Evergreen Fund purchased all the Series A bonds of shorter maturities at less than par (Tr. 424, 726-27; DX 21-DX 23), the Division could not simply assume that D&B sold these bonds to Evergreen Fund at par. Accordingly, I conclude that the Division has failed to offer a "reasonable approximation" of the commissions earned on the Series A bonds of shorter maturities.

[50] Par is the nominal face value of the bonds, i.e., the amount at which the Authority promised to redeem the bonds at maturity. As to the Series A bonds, the difference between the purchase price and par was not D&B's profit at closing. See First Fidelity Secs. Group, 61 SEC Docket 68, 71 n.2 (Jan. 9, 1996) (settled case) (defining the underwriter's discount as the difference

I will order D&B and Bradbury to disgorge $482,562.50 (or $31,000 + $451,562.50). Liability is joint and several. I reject the Division's claim that D&B and Bradbury should disgorge a greater amount.

Prejudgment Interest

Section 8A(e) of the Securities Act and Sections 21B(e) and 21C(e) of the Exchange Act provide that the Commission may order disgorgement, "including reasonable interest," in any administrative proceeding in which a cease-and-desist order is sought or a civil monetary penalty could be imposed. These statutory provisions also authorize the Commission to adopt rules and regulations and issue orders concerning rates of interest and periods of accrual. The Commission promulgated Rule 600 of its Rules of Practice, Interest On Sums Disgorged, in 1995.

I agree with the Division that the starting date for the computation of prejudgment interest should be August 1, 1998, as to D&B and Bradbury. Because the Division's calculation of the sum to be disgorged must be adjusted downward, it follows that the Division's calculation of prejudgment interest must also be adjusted downward. I will require the Division to file and serve a revised computation of prejudgment interest within seven days after the service of this Initial Decision.

Civil Monetary Penalties

An order of disgorgement (even with prejudgment interest) merely requires the return of wrongfully obtained profits. Disgorgement does not result in any actual economic penalty or act as a financial disincentive to engage in securities fraud. See SEC v. Morgan, 944 F. Supp. 286, 296 (S.D.N.Y. 1996) (citing the legislative history of the Remedies Act). The Division therefore argues that substantial monetary penalties, in addition to the disgorgement of illicit profits, is necessary to punish D&B and Bradbury and deter others from engaging in securities law violations that otherwise may provide significant financial returns to the violator.

Under Section 21B(a) of the Exchange Act, the Commission may assess a civil monetary penalty if a respondent has willfully violated or willfully aided and abetted any violations of the Securities Act, the Exchange Act, or the rules or regulations thereunder. The Commission must also find that such a penalty is in the public interest. Six factors are relevant to the public interest determination: (1) fraud, or the deliberate or reckless disregard of a regulatory requirement; (2) harm to others; (3) unjust enrichment; (4) prior violations; (5) deterrence; and (6) such other factors as justice may require. See Section 21B(c) of the Exchange Act. Not all factors may be relevant in a given case, and the factors need not all carry equal weight.

Section 21B(b) of the Exchange Act specifies a three-tier system identifying the maximum amount of a penalty. All of the violations in this proceeding occurred after December

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between the purchase price that the underwriter pays to the issuer to buy the bonds and the offering price at which the underwriter resells the bonds to the public).

9, 1996, and before February 3, 2001.[51] For each such "act or omission" by a corporation, the adjusted maximum amount of a penalty is $55,000 in the first tier; $275,000 in the second tier; and $550,000 in the third tier. For each such "act or omission" by a natural person, the adjusted maximum amount of a penalty is $5,500 in the first tier; $55,000 in the second tier; and $110,000 in the third tier. A second-tier penalty is permissible if the act or omission involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement. A third-tier penalty not only must have involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement, but also must have "directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons or resulted in substantial pecuniary gain to the person who committed the act or omission." The proven violations here involved fraud and the reckless disregard of regulatory requirements. I conclude that the "significant risk of substantial losses" prong of the third-tier civil penalty test has been satisfied as well.

The adjusted statutory maximum amount is not an overall limitation, but a limitation per violation. See Mark David Anderson, 80 SEC Docket 3250, 3270 (Aug. 15, 2003) (imposing a civil penalty of $1,000 for each of the respondent's ninety-six violations); cf. United States v. Reader's Digest Ass'n., 662 F.2d 955, 966, 970 (3d Cir. 1981) (holding that each individual mailing constitutes a separate violation of an FTC consent order). Because multiple acts and omissions are involved here, the Division's requests for penalties of $550,000 against D&B and $110,000 against Bradbury are well within the statutory ceiling.

The five-year limitation period of 28 U.S.C. § 2462 applies to civil monetary penalties. However, D&B and Bradbury have signed tolling agreements (Declaration of Mark R. Zehner Concerning Tolling Agreements, dated June 1, 2004, Exhibits B-D).

Addressing the six factors that guide the public interest analysis under Section 21B, I conclude that the proven violations involved fraud and the reckless disregard of regulatory requirements. They created a significant risk of harm to others. Because I am ordering disgorgement and prejudgment interest, any unjust enrichment will be eliminated. The Division's request for penalties of $550,000 against D&B and $110,000 against Bradbury is excessive. First, the Division has not proven its entire case. The appraisal was not shown to be materially misleading. The evidence that footnoted financial projections were materially misleading, while sufficient to satisfy the preponderance of the evidence test, was not strong. Second, apart from this proceeding, both D&B and Bradbury have enjoyed spotless disciplinary records for decades. That fact is entitled to substantial weight in setting penalties.

I will impose a civil penalty of $82,000 against Bradbury and a civil penalty of $400,000 against D&B. Collectively, these penalties are approximately equal to the amount ordered to be disgorged by these two Respondents, jointly and severally. Penalties at this level will provide appropriate deterrence against misconduct by others.

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[51] As required by the Debt Collection Improvement Act of 1996, the Commission increased the maximum penalty amounts for violations occurring after December 9, 1996, and, again, for violations occurring after February 2, 2001. See 17 C.F.R. §§ 201.1001, .1002.

No Issue of Inability to Pay

Under Section 21B(d) of the Exchange Act, in any case in which the Commission may impose a civil penalty, a respondent may present evidence of the respondent's ability to pay the penalty. The Commission may, in its discretion, consider such evidence in determining whether a civil penalty is in the public interest. Such evidence may relate to the extent of the respondent's ability to continue in business and the collectability of the penalty, taking into account any other claims of the United States or of third parties on the respondent's assets and the amount of the respondent's assets.

Although no statutory requirement addresses inability to pay disgorgement or interest, the Commission may also consider evidence of ability to pay as a factor in determining whether a respondent should be required to pay disgorgement and interest. See Rule 630(a) of the Commission's Rules of Practice.

Well before the hearing, I advised Respondents that, if they intended to claim inability to pay disgorgement, interest, or civil penalties, they were required to submit sworn financial statements, as well as supporting income tax returns, at the hearing (Prehearing Conference of May 26, 2004, at 38-40; Order of May 27, 2004). See Rule 630 of the Commission's Rules of Practice; Terry T. Steen, 53 S.E.C. 618, 626-28 (1998) (holding that an ALJ may require the filing of sworn financial statements). Respondents did not submit sworn financial statements or income tax returns. I conclude that Respondents have waived any claim of inability to pay.

Investor Fund

As a final matter, the Division seeks an order directing that payment of the sums to be disgorged and the civil penalties be made to a distribution fund established for the benefit of defrauded investors (Div. Prehearing Br. at 24-25; Div. Br. at 42). The Division argues that such an order should include a requirement that none of the funds go to pay counsel fees. The Division also urges that all amounts in the fund be paid to the current bond trustee (and any successor) because, now that the bonds are in default, the bond trustee serves as the official representative of the bondholders.[52]

If the Division intended to invoke the Federal Account for Investor Restitution Fund (FAIR Fund) provision in Section 308 of the Sarbanes Oxley Act and Subpart F of the Commission's Rules of Practice, FAIR Funds and Disgorgement Plans, 17 C.F.R. §§ 201.1100-06, it should have done so with specificity.[53] If the Division has some other statutory basis for its request, it should so state.

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[52] In its final pleadings, the Division amended its request, asking that the funds be paid to Chernicoff, the receiver (Div. Reply to D&B at 25, Div. Reply to PFC at 19).

[53] The Part 1100 Rules became effective on April 19, 2004, one week before the Commission issued the OIP in this matter. See Adoption of Amendments to the Rules of Practice and Delegation of Authority to the Commission, 82 SEC Docket 1744 (Mar. 12, 2004).

I am not persuaded that the Commission intended for Administrative Law Judges, as distinguished from Commission itself, to order the creation of FAIR Funds. Accord Steven E. Muth, Initial Dec. Rel. No. 262 at 42, 2004 SEC Lexis 2320 at *107-08 (Oct. 8, 2004), review granted. Therefore, I respectfully defer to the Commission on this issue. I deny the Division's request, without prejudice to the Division's renewing it before the Commission.

So that the Commission may have a more complete record to consider the Division's request, I will require the Division to file and serve a supplemental statement within seven days after the issuance of this Initial Decision, explaining the particulars of its proposal. The Division shall address three matters:

First, the Division shall clarify the statutory basis for its request and explain whether it intends the bond trustee or the receiver to be the custodian of the proposed investor fund.

Second, the Division shall state whether the proposed custodian has agreed to perform the role the Division describes, on the terms the Division sets forth (no counsel fees).

Third, the Division shall explain whether any sums deposited in the proposed investor fund will be used to pay only the bondholders who testified at the hearing, see Barbato, 53 S.E.C. at 1279-80, or other bondholders as well. If the Division chooses the latter, it shall clarify whether the fund will reimburse those who bought Forum Place bonds in the secondary market, as well as those who bought in the public offering, and whether the Series B bondholders will stand in line behind all the Series A bondholders (including such secondary market Series A bond purchasers as Fowler, Bradbury's mother, and Vartan).

RECORD CERTIFICATION

Pursuant to Rule 351(b) of the Commission's Rules of Practice, I certify that the record includes the items set forth in the record index issued by the Secretary of the Commission on October 18, 2004, as updated on February 25, 2005.

ORDER

Based on the findings and conclusions set forth above:

IT IS ORDERED THAT the proceeding is dismissed as to Public Finance Consultants, Inc., and Robert D. Fowler;

IT IS FURTHER ORDERED THAT, pursuant to Section 8A of the Securities Act of 1933 and Section 21C of the Securities Exchange Act of 1934, Dolphin & Bradbury, Inc., and Robert J. Bradbury shall cease and desist from committing or causing any violations or future violations of Section 17(a) of the Securities Act of 1933, Sections 10(b) and 15B(c)(1) of the Securities Exchange Act of 1934, including failing to deal fairly with all persons and engaging in any deceptive, dishonest, or unfair practice under Rule G-17 of the Municipal Securities Rulemaking Board, and Exchange Act Rule 10b-5;

IT IS FURTHER ORDERED THAT, pursuant to Section 8A of the Securities Act of 1933 and Section 21C of the Securities Exchange Act of 1934, Dolphin & Bradbury, Inc., and Robert J. Bradbury, jointly and severally, shall disgorge $482,562.50, plus prejudgment interest computed as set forth in Rule 600 of the Commission's Rules of Practice, with prejudgment interest starting to run on August 1, 1998;

IT IS FURTHER ORDERED THAT, pursuant to Section 21B of the Securities Exchange Act of 1934, Dolphin & Bradbury, Inc., shall pay a civil penalty of $400,000 and Robert J. Bradbury shall pay a civil penalty of $82,000;

IT IS FURTHER ORDERED THAT, as to Dolphin & Bradbury, Inc., and Robert J. Bradbury, no sanction shall be imposed pursuant to Sections 15(b) and 15B of the Securities Exchange Act of 1934; and

IT IS FURTHER ORDERED THAT, within seven days after the service of this Initial Decision, the Division of Enforcement of the Securities and Exchange Commission shall file and serve (a) a chart showing its computation of prejudgment interest on the sums to be disgorged and (b) a supplemental statement of its proposal for an investor restitution fund, addressing the issues identified in this Initial Decision.

Payment of the civil penalties, disgorgement, and prejudgment interest shall be made on the first day following the day this Initial Decision becomes final. Payment shall be made by wire transfer, certified check, United States Postal money order, bank cashier's check, or bank money order, payable to the Securities and Exchange Commission. The payments, and a cover letter identifying the Respondents and the proceeding designation, shall be delivered to the Comptroller, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, Virginia 22312. A copy of the cover letter and the instrument of payment shall be sent to the Commission's Division of Enforcement, directed to the attention of counsel of record.

This Initial Decision shall become effective in accordance with and subject to the provisions of Rule 360 of the Commission's Rules of Practice. Pursuant to that Rule, a party may file a petition for review of this Initial Decision within twenty-one days after service of the Initial Decision. A party may also file a motion to correct a manifest error of fact within ten days of the Initial Decision pursuant to Rule 111 of the Commission's Rules of Practice. If a motion to correct a manifest error of fact is filed by a party, then that party shall have twenty-one days to file a petition for review from the date of the undersigned's order resolving such motion to correct a manifest error of fact.

The Initial Decision will not become final until the Commission enters an order of finality. The Commission will enter an order of finality unless a party files a petition for review or a motion to correct a manifest error of fact, or unless the Commission determines on its own initiative to review this Initial Decision as to any party. If any of these events occur, the Initial Decision shall not become final as to that party.

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James T. Kelly
Administrative Law Judge