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City of Miami spending big bucks to defend against SEC probe

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Almost two years since federal authorities began poking around in the city of Miami's finances, the city has spent $1.4 million defending itself, and most of the senior managers who have given testimony are gone.

With no timetable set by the U.S. Securities and Exchange Commission, city attorneys recently told commissioners in the already cash-strapped city to brace for even more costs associated with the probe and pumped up the legal department's budget by another $2 million for outside counsel.

"They are still taking testimony," city attorney Julie Bru told commissioners during last month's budget hearing. "To play it safe, we're still budgeting that amount."

Bru told commissioners that the expertise of outside lawyers was needed to help gather documents and advise the city's finance chiefs — most of whom have left the city already — during depositions. She said she would update the commission on the investigation within this month.

So just how long can this go on?

"Two years for an investigation is probably not inconsistent," said Fort Lauderdale securities-fraud attorney David Chase, who is not involved in the case. "Once you push beyond two years in any case, internally they're going to ask: 'What's going on?' "

If Chase is right, local SEC investigators could be nearing a decision. Chase said that if investigators find wrongdoing, they typically give the party under review the opportunity to hear the findings and decide whether to settle or fight. If no resolution is reached, the matter moves to the securities commission in Washington, D.C.

"Before smearing their good name," Chase said, "it gives the side a chance to come in and say 'you're wrong' or settle."

The SEC began its wide-ranging probe into Miami's finances in December 2009, after a series of Miami Herald articles outlined the questionable transfer of $26.4 million from capital accounts to the city's general fund in 2007 and 2008, which helped balance its budget.

The agency demanded thousands of pages of records — including emails, computer logs, opinions, reports, presentations and calculations — on more than $250 million in bond deals dating back to 2006.

The SEC wanted to know if bond buyers might have been misled about the health of the city's finances when those bonds were purchased.

Another red flag: Even during the boom years in the middle of the last decade, the city was bleeding its once-flush reserve fund dry. In 2003, the reserve was stuffed with $141 million. Yet even before the economic slide, close to $100 million of the reserve was spent to help balance the city's books.

Since the investigation began, about a half-dozen top-tier managers have given depositions. Almost all of them are gone, including budget director Michael Boudreaux, Chief Financial Officer Larry Spring, finance director Diana Gomez, City Manager Pete Hernandez and Assistant City Manager Roger Hernstadt.

Also gone is internal auditor Victor Igwe, whose contract was not renewed.

Defending the city has been costly. City records show that four outside law firms have been paid more than $1.4 million over the past two years at rates ranging from $315 to $450 an hour. The law firm Morgan Lewis & Bockus has been paid the most, at $1.1 million. Next is White & Case at $285,328, then attorney Kenny Nachwalter at $58,106, and finally Broad & Cassel at $24,708.

Whether individuals or the city will be accused of wrongdoing is not clear. Bru has repeatedly declined to discuss the investigation.

A decade ago, Miami found itself on similar footing when the SEC issued a cease-and-desist order after finding that city leaders had defrauded bondholders by failing to disclose the depth of the city's financial issues. An administrative judge said investors were misled in 1995 when the city created the appearance of a balanced budget by transferring restricted money into the city's general fund.

Miami was later discovered to have a $68 million deficit, and a state oversight board took over the city's finances for the next five years.

The cease-and-desist notice essentially told the city not to repeat its prior mistakes. The SEC often stops short of fining municipalities when it uncovers wrongdoing because that only hurts the taxpayers.

Lately, however, the agency has gone directly after city officials.

Last year, for the first time, the SEC brought civil penalties against four San Diego officials for misleading bond investors. Three of the officials agreed to pay $25,000 each, and a fourth paid $5,000. In all, San Diego spent more than $2.5 million defending its former employees.