SEC rules that Harrisburg misled investors

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Harrisburg, the capital city of Pennsylvania, was ordered by the Securities and Exchange Commission (SEC) to cease and desist its “misleading” practices directed at investors on the parasitic municipal bond market, on May 6, 2013. Mayor Linda Thompson, a Democrat who took office in 2010, tepidly said the allegations “are what they are.”

The SEC has accused Harrisburg of “material misrepresentations and omissions concerning its financial health.” George Canellos, co-chief of SEC enforcement, said in a statement, “In an information vacuum caused by Harrisburg’s failure to provide accurate information about its deteriorating financial condition, municipal investors had to rely on other public statements misrepresenting city finances.”

In 2009, Moody’s Investor Services Inc. downgraded “Harrisburg’s general obligation bonds from Baa2 to Ba2, citing in its report the difficulties Harrisburg had in paying its RRF (Resource Recovery Facility i.e. trash incinerator) debt as the primary reason for the downgrade.” Harrisburg omitted this from its Comprehensive Annual Financial Report. A year later, in 2010, Moody’s downgraded the bonds from a Ba2 to a B2. Harrisburg again failed to disclose the downgrade to investors, as declared by the SEC’s proceeding.

The federal government is adding its weight along with the Pennsylvania state government to ensure that the bondholders are paid at the expense of city services and public workers.

Harrisburg is saddled with more than $300 million in debts, most of which has accumulated from the disastrous attempt to remodel Harrisburg’s outdated and obsolete incinerator plant. Originally constructed in 1972, the plant was always plagued with problems and after operating for nearly 30 years, had been shut down because it released high levels of the poison dioxin into the air.

The fiasco began in 2003 when the City Council approved a plan with a newly founded Colorado company, Barlow Project Inc., which placed an initial price of $77 million for the remodeling efforts. Cost overruns and corruption lead to the cost being much higher. Subsequently, Barlow Project Inc. was terminated because of its incompetence, and currently a New Jersey-based company, Covanta Energy, is overseeing the remodeling of the incinerator with a new $25.5 million plan. Because the city never required Barlow to be bonded, the city is responsible for the debts. The incinerator is not yet 100 percent operational.

The federal government acknowledges that Harrisburg’s money woes come from its mountain of debt. The SEC writes, “Harrisburg is a near-bankrupt city under state receivership largely by virtue of approximately $260 million in outstanding debt. As of March 15, 2013, Harrisburg has found it necessary, on three occasions, to withhold approximately $13.9 million in general obligation debt service payments in order to have sufficient cash flow to meet essential services in the City.” The city has a population of 50,000 and generates annual revenue of roughly $55 million, making it impossible to pay the interest, let alone the principal on the dept.

The capital, as a result, filed for Chapter 9 municipal bankruptcy in 2011, but a federal judge ruled that to be unconstitutional under Pennsylvania law. The state passed a law that appointed a state receiver, presently Gen. William Lynch, who lacks a business or financial background, to oversee the financial situation of the city. David Unkovic had been the first state receiver before grooming Gen. Lynch for the job. The aim of the state is to force the city to repay all of its debts to the bondholders while cutting city services and slashing the wages and benefits of city workers. This can be likened to Detroit’s despotic emergency manager, Kevyn Orr, although Harrisburg hasn’t changed into an intense austerity dictatorship yet.

The municipal bond market has become the next bubble that could burst. The market has increased by 35 percent since 2007, now reaching $3.7 trillion, according to Bloomberg. Investment banks, real estate speculators, and construction firms, along with corrupt politicians, have pushed for cities to take on massive loans to fund questionable projects from which they make millions while leaving the cities piled high in debts they can't pay.

Many cities, though, have defaulted on their bonds. Last year, Stockton, California, Wenatchee, Washington, and Vadnais Heights, Minnesota, all defaulted.

Moody's has therefore said, "Attitudes toward debt and repayment appear to have changed; 'strategic default' may become more acceptable as a viable government strategy and no longer taboo." Since credit risk has increased, the credit agency has "actively lowered" municipal ratings.

Specifically, the SEC ruling will strengthen bondholders in suits against Harrisburg since they can now claim they were misled by the city.

The SEC filings against Harrisburg are part of its investigation into local government financing throughout the country. The Obama administration is siding, along with the courts and state governments, with the bondholders to force municipalities' governments to repay the bonds no matter what the cost is to workers and residents.