

Unregistered Broker Activity in EB-5 Capital Fund Raising SEC Imposes Cease-And-Desist Order¹

June 24, 2015

In an important development affecting the EB-5 financial community the SEC has imposed a cease-and-desist order with respect to fund raising activities conducted by two unregistered brokers and related persons in connection with their solicitation of investors for projects sponsored under the EB-5 visa program.² The administrative proceeding is a cautionary reminder to regional centers that they should avoid paying fees to finders and other industry participants that are not registered with the SEC as brokers or associated persons of brokers registered with the SEC. The Order contains valuable lessons for practitioners outside the EB-5 context by providing a summary of the type of activities that require a person to register with the SEC as a broker under Section 15(a) of the Securities Exchange Act of 1934.

Facts

Stephen Parnell and Andrew Bartlett formed Ireeco, LLC in 2006 and Ireeco Limited in 2012 (together, “Ireeco” or the “company”). Ireeco solicited foreign investors who wished to invest in the EB-5 visa program through regional centers. The company employed of four to five people in the United States and maintained a website (www.whicheb5.com) marketing its services to foreign individuals. The services were to assist potential investors in determining whether the EB-5 visa program was appropriate for them and then provide them with the information they would need in choosing the right regional center for their investment. The company’s website contained information about Parnell and Bartlett’s background and experience. On the website the company claimed that it had provided services to over 3,300 potential immigrant investors and touted its success in helping customers obtain their unconditional green card at the end of the petition process. The website cautioned potential investors that regional centers wanted investors to invest in their projects but accentuated the positive aspects “without making you aware of any potential negatives.”

¹ Release No. 75268 June 23, 2015, Administrative proceeding File No. 3-16647, In the Matter of Ireeco, LLC and Ireeco Limited Respondents.

² In a nutshell the EB-5 visa program provides an opportunity for persons to become lawful permanent residents of the United States by investing in a commercial enterprise that creates a specified number of full time jobs. A number of EB-5 visas are set aside for investments that are affiliated with a “regional center” designated by the United States Citizenship and Immigration Services (USCIS) to administer EB-5 investment projects based on proposals for promoting economic growth. In addition to their investment in the project (which is currently a minimum of \$500,000 if the project is located in a targeted employment areas), most regional centers require applicants to pay an administrative fee that is designed to offset legal fees, travel, and other expenses incurred by the regional center in establishing and administering the project.

Unregistered Broker Activity

The Order summarized the company's activities as follows:

1. Through the website the company offered to assist foreign investors in their selection of an EB-5 project. Potential investors would request information through the website and would be contacted by a representative of the company to ascertain their interest in the program and level of knowledge. The Order noted that, in at least ten instances, the potential investors were residing in the United States on a temporary visa when they were solicited.

2. After the initial call the company's representatives would reach out to discuss the next step in the EB-5 investment process. The company would e-mail the potential investor with information about the EB-5 program and marketing information touting Parnell's and Bartlett's experience and expertise in EB-5 investments. The company would send follow-up e-mails automatically three months after the first inquiry, and then again after 18 months.

3. In follow-up calls with potential investors who had indicated an interest, the company's representatives would talk to prospects to ascertain their background and visa status, their business experience and interest in a particular geographical area or a specific type of EB-5 project. Based on the information obtained, the company determined if the prospect qualified for the EB-5 project and what his or her investment preferences were.

4. The company would provide prospects with one or more EB-5 regional center projects as possible choices and background information about those centers. The company performed "due diligence" on each of the regional centers it selected for its clients.

5. Once a prospect identified which regional center was of most interest, the company "registered" the client with the applicable regional center by providing the name, contact information and visa status. The investors would deal directly with the regional center which would provide their offering documents to the prospective investors. Investors would contact the company from time to time if they had questions about the investments or offering materials.

6. The regional centers would compensate the company under "referral partner agreements" for each prospect who invested funds in an EB-5 offering. The fee was earned once the investor's I-526 petition (conditional green card) was approved by USCIS. The Order characterized the fee as a commission based on a fixed portion of the "administrative fee" the investor paid to the regional center and averaged around \$35,000 per investor.

7. The company was paid fees for actively soliciting over 158 foreign investors who invested a total of \$79 million in the regional centers. Most of the investors were referred to a limited number of regional centers.

Based on these activities the SEC determined that the company had willfully violated Section 15(a)(1) of the Exchange Act by engaging in the business of effecting transactions in, or inducing or attempting to induce the purchase or sale of, securities for the accounts of others without registering as a broker-dealer with the SEC or without associating with a broker-dealer registered with the SEC. Pursuant to the Order the company agreed to additional proceedings to determine whether it is appropriate to order disgorgement and/or civil penalties.

Takeaways

A. The EB-5 industry has been the subject of increased scrutiny from regulators in recent years as a result of a number of scandals involving misrepresentations made in connection with purported EB-5 projects.³ This Order is perhaps evidence of the clampdown by the SEC on unlawful offering practices that has been rumored for some time.⁴ The proceeding may be the first in a number of actions designed to ensure that investors in EB-5 offerings in the future receive the protections afforded by the United States securities laws, including administration of the investment process by licensed persons subject to SEC and FINRA oversight.

B. Regional centers and other sponsors of EB-5 projects have been cautioned previously through industry journals and conferences on the risks of using unlicensed persons in their fundraising efforts. However, to the author's knowledge, this is the first settlement order by the SEC involving an intermediary that has engaged in unlicensed activities. Industry participants should be reminded that Section 29(b) of the Exchange Act provides that any contract made in violation of any provision of the Exchange Act is void as to the rights of any person in violation of the relevant Exchange Act provision and may create rescission rights in favor of investors.

C. The factual summary in the Order highlights factors analyzed by the SEC in determining whether a person is engaged in broker activity. While practitioners may focus their analysis exclusively on the presence of transaction-based compensation, it is important to remember that other factors are relevant as well.⁵ In this case, in addition to the payment of fees that were contingent on the admission of the investor to the regional center program and USCIS approval of the I-526 petition, there was a pattern of solicitation conducted over an extended period, the provision of information and questions designed to assist the company's representative in forming a suitability determination for the investment opportunity, the presentation of regional centers that matched the investor's profile based on the background information provided and answering questions about the regional center's offering documents throughout the process. The company and its representatives participated at key points in the chain of distribution.

³ See, e.g., Investor Alert: Investment Scams Exploit Immigrant Investor Program, jointly issued by the SEC and USCIS, available at http://www.sec.gov/investor/alerts/ia_immigrant.htm.

⁴ See, e.g. Bloomberg News article published on February 13, 2015 entitled "SEC targets deals giving visas to rich foreign investors," available at <http://www.bloomberg.com/news/articles/2015-02-13/sec-said-to-target-deals-giving-visas-to-rich-foreign-investors>.

⁵ See footnote 6 to "A Few Observations in the Private Fund Space", a speech by David W. Blass, Chief Counsel, Division of Trading and Markets, U.S. Securities and Exchange Commission, American Bar Association, Trading and Markets Subcommittee, Washington, D.C. on April 5, 2013: "Although the receipt of compensation in connection with a purchase or sale of securities generally requires, as a practical matter, registration or association with a registered broker-dealer, it is important to understand that the receipt of transaction-based compensation in connection with securities transactions is not a necessary element to require broker-dealer registration. In other words, one can be acting as a broker-dealer without having received transaction-based compensation."



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