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EB-5 Visa Scandal Underscores the Critical Role Whistleblowers Play in Exposing EB-5 Fraud

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$50M EB-5 Visa Scheme

On April 5, 2017, federal authorities raided a business run by a California attorney and her father that is suspected of orchestrating a $50 million EB-5 visa scheme. According to the court filings, the father-daughter company, California Investment Immigration Fund, LLC (CIIF), raised money from more than 100 Chinese investors for several business projects. Under the EB-5 program, these Chinese investors would qualify for U.S. green cards if the business projects created at least ten jobs. However, rather than legitimately investing the funds, CIIF hired high school students to pose as full-time employees for fake projects and used the investors' funds to buy their own personal luxury items, including million-dollar homes, and for other improper uses.

The scheme began around 2008 and went undetected for years. Due to a lack of oversight of the EB-5 program, many of CIIF's investors were even able to improperly obtain U.S. green cards without investing in legitimate businesses or creating any jobs. Notably, three of the CIIF's investors who received green cards were fugitives wanted by the Chinese government.

This EB-5 visa scandal marks yet another misuse of the program, which has experienced widespread fraud in the past few years. Whistleblowers have played a critical role in exposing EB-5 fraud and the SEC Whistleblower Program provides a financial incentive for whistleblowers to expose EB-5 fraud.

How the EB-5 Investment Program Works

The EB-5 investment program, administered by the U.S. Citizenship and Immigration Services (USCIS), provides a path to legal residency for foreigners who invest directly in a U.S. business or private regional centers that promote economic development. The purpose of the EB-5 program is to stimulate the U.S. economy through job creation and capital investment by foreign investors.

Under the current program, foreigners are eligible to apply for a U.S. green card if:

- They invest $500,000 or $1 million in a qualifying project in the U.S.; and
- The project creates or preserves 10 permanent full-time jobs for qualified U.S. workers.

In the coming weeks, however, Congress will be forced to address the future of the EB-5 program as it is set to expire at the end of April 2017. Some lawyers want to reform the program by creating additional oversight and increasing the investment thresholds to $1.35 million and $1.8 million. Others wants to completely scrap the program due to frequent fraud and its failure to truly promote economic development.

This uncertainty about the EB-5 program has resulted in a dramatic increase in foreign investments in EB-5 projects. The pressure to quickly invest before April 30, 2017 has likely resulted in decreased due diligence by investors. This poses an increased risk to investors, especially Chinese investors who make up 85% of EB-5 investments, that their money may be used to fund the purchase of someone's yacht, rather than fund a qualified EB-5 project.

EB-5 Fraud

The EB-5 program has recently been plagued by fraud. Indeed, in just the last two year alone, the SEC has uncovered and halted numerous EB-5 schemes with investments well in excess of $50 million (see examples below). According to Wall Street Fraud Watchdog, the most susceptible markets to EB-5 fraud have been the luxury apartment markets, hotel, and resort type properties in Southern California, Seattle, Portland, Dallas, and Chicago.

In 2013, the SEC released an investor alert about EB-5 fraud. The SEC warned:

> The fact that a business is designated as a regional center by USCIS does not mean that USCIS, the SEC, or any other government agency has approved the investments offered by the business, or has otherwise expressed a view on the quality of the investment. The SEC and USCIS are

aware of attempts to misuse the EB-5 program as a means to carry out fraudulent securities offerings.

Indeed, the investor alert noted that the SEC has opened several emergency enforcement actions to stop fraudulent securities offerings made through EB-5, including a $156 million scheme. The largest EB-5 scheme to date involved nearly 300 Chinese investors and $912 million in investments.

In 2016, the U.S. Government Accountability Office (GAO) echoed the SEC's concerns in its report to congress about the EB-5 program. The GAO noted that while USCIS has taken steps to enhance its fraud detection, the efforts have not been adequate. The report recommended that USCIS develop a fraud risk profile that would allow the agency to better prioritize and respond to evolving fraud risks.

SEC Whistleblower Program

Under the SEC Whistleblower Program, whistleblowers may be eligible for monetary awards when they voluntarily provide the SEC with original information about violations of federal securities laws, including EB-5 fraud. Whistleblowers are eligible to receive between 10% and 30% of the monetary sanctions collected if their tip leads to a successful enforcement action resulting in monetary sanctions exceeding $1,000,000.

The SEC Whistleblower Program also protects the confidentiality of whistleblowers and does not disclose information that might directly or indirectly reveal a whistleblower's identity. In fact, whistleblowers can even submit a tip **anonymously** if represented by counsel.

Since the law went into effect, the SEC Whistleblower Office has awarded more than $149 million to 41 whistleblowers. The largest award to date is more than $30 million. In 2016, the office issued more than $57 million in awards to whistleblowers.

Examples of EB-5 Fraud and Recent SEC Enforcement Actions

There are many examples of EB-5 fraud that would qualify a whistleblower for an award. In the past two years, notable EB-5 enforcement actions that have resulted (or may result) in large monetary sanctions, include:

Falsely Advertising EB-5 Projects As "Risk-Free"

On July 26, 2016, the SEC obtained a **$63.8 million** judgment against an oil company for a scheme that targeted EB-5 investors. The SEC alleged in their complaint that Luca International Group, LLC and its entities (collectively, the "Luca Entities"), targeting investors in Asia to invest in unregistered offerings of securities. Luca Entities represented to investors that their money would be invested in oil and gas drilling operations, and that they could expect risk-free annual rates of return of 20-30 percent. Luca Entities deceived investors by misrepresenting that their operations as successful, all while knowing that the company was losing millions of dollars. Luca Entities maintained this deception by using money from new investors to make sham profit payments to earlier investors until its bankruptcy in August 2015.

Illegal Brokering of EB-5 Investments

On June 23, 2015, the SEC charged two firms (Ireeco LLC and Ireeco Limited) that illegally brokered more than **$79 million** of investments by EB-5 investors seeking U.S. residency. Ireeco LCC used its website to solicit EB-5 investors and provide them with the "information and education" they would need in choosing the right regional center to invest with. After securing foreign investors from the website, Ireeco LCC would then direct them to the same handful of regional centers that paid the company a commission averaging around $35,000 per investor. While raising money for EB-5 projects in the U.S., these two firms were not registered to legally operate as securities brokers. The SEC sought to disgorge all of the ill-gotten gains and subject the companies to civil penalties pursuant to Sections 21B and 21C of the Exchange Act.

Misusing EB-5 Investments: $72 Million

On December 27, 2016, the SEC charged a California-based attorney, Emilio Franscisco, with stealing money over $9.6 million from EB-5 investors. According to the SEC's complaint, Franscisco raised **$72 million** from investors in China to invest in EB-5 projects that included opening Caffe Primo restaurants, developing assisted living facilities, and renovating a production facility for environmentally friendly agriculture and cleaning products. Instead of using investors' funds for the EB-5 projects, Franscisco used the money to purchase a yacht, and finance his own businesses and luxury lifestyle.

Misusing EB-5 Investments: $136 Million

On January 11, 2017, the SEC received a settlement offer from real estate developer and former Tibetan monastery student, Lobsang Dargey, in a **$136 million** EB-5 fraud case. This could signal a possible resolution to the high-profile case. In late 2015, the SEC ordered an asset freeze against Dargey and his "Path America" companies after raising well over $135 million for two real estate projects. Instead of properly investing the money, Dargey diverted $14 million for unrelated real estate projects and $3 million for personal use including the purchase of his $2.5 million home and cash withdrawals at casinos.

Misusing EB-5 Investments: $100 Million

On January 18, 2017, the SEC charged California-based San Francisco Regional Center, LLC and owner Thomas Henderson with combining over **$100 million** he raised from Chinese investors into a general fund from which he allegedly misused at least $9.6 million to purchase his home and personal items and improperly fund several personal business projects that were unrelated to the companies he purportedly established to create jobs consistent with EB-5 requirements. Furthermore, Henderson used $7.5 million of investor money to pay overseas marketing agents, and he shuffled millions of dollars among the EB-5 businesses to obscure his fraudulent scheme.

Misusing EB-5 Investments: $26.9 Million

On February 16, 2017, the SEC recommended a **$65.7 million** penalty against a husband and wife who allegedly misappropriated the bulk of $26.9 million raised in an EB-5 investment project. According to the SEC's complaint, the couple defrauded at least 50 Chinese investors by falsely claiming that their monies would be invested in an approved EB-5 project to build and operate a proton therapy cancer treatment center (Beverly Proton Center, LLC) in Southern California. Rather than invest the money, the couple misappropriated at least $7.7 million for themselves and transferred more than $11.8 million to three marketing firms in China, including $3.5 million to a firm of which the husband is CEO and chairman of the board.

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