

## INTEGRITY SPOTLIGHT

# EB-5 Fund Administration:

## Considerations in Light of Increased Interest in Transparency and Third Party Oversight for EB-5 Transactions



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In 2017, EB-5 dealmakers may be welcoming a new member to the deal team to provide a check on how EB-5 investment flows from investment accounts to deployment for job creation. Although there are a few exceptions, generally accepted business practices for most EB-5 deals do not call for the engagement of a third party to act as an usher of EB-5 funds through the investment and deployment cycles. As such, a mandate for independent signatories may cause many in our industry to start the search for the right qualified professional(s) to perform these services for their transactions. In this Integrity Spotlight article, we begin exploring a category of service provider that might be worth evaluating as a contender – an independent fund administrator.

Section (P) (Account Transparency Requirement) of H.R. 5992, a bill introduced in the House of Representatives in late September 2016, proposes that each new commercial enterprise (NCE) create a separate account to hold EB-5 investments at third-party banks or other financial institutions and that independent authorized signatories provide written consent before EB-5 investments are transferred – whether back to the investor, to the NCE, or to the job creating entity (JCE). The bill calls for the authorized signatory to be “independent of, and not directly or indirectly related to” the NCE, regional center associated with the NCE, JCE, or any of the principals or managers of these entities and either: (1) an officer at the bank or financial institution where the account is maintained;

(2) an attorney, (3) a CPA, (4) a broker-dealer, or (5) a signatory otherwise authorized by the Director of USCIS. See Section 203(b)(5) of H.R. 5992. Although not specifically included in the enumerated list of authorized signatory candidates, an independent fund administrator may be eligible for authorization by the Director and may be among the most well-equipped professionals to provide oversight and signatory services to the EB-5 industry if Section (P) becomes law. Further, there has been an indication that future proposed bills may even go so far as to require that a fund administrator be engaged by an NCE to perform co-signatory and other functions in connection with the administration of EB-5 investment funds.

Based on review of a 2009 report prepared by the Alternative Investment Management Association (AIMA), Guide to Sound Practices for Hedge Fund Administrators, fund administrator engagements can be viewed in terms of phases of the fund’s life cycle. The report lists five primary phases of engagement – Start-up Phase, Interaction with Investors, NAV Calculation, Completing the Service, and Support and Review. The report provides a best practice-based educational overview of the types of services that could fall within these five phases of fund administration. One takeaway from this report is that a fund administrator’s role is defined by its service listing, which can vary based on the customer and should be tailored on a fund-by-fund basis.

Fund administrators are essentially monitors and reconcilers. They are typically engaged to track money coming in and out of the fund, maintain records, document income and expense allocation among members of the fund, and prepare reports for investors. Many fund administrators perform a fund accounting function to produce financial statements for the fund by helping them to complete their bookkeeping cycle and prepare tax returns. A fund administrator engagement may also include assistance with tracking assets, liabilities, income, and expenses of the fund. If the fund’s operative documents call for an annual audit of its financial statements, the fund administrator may serve as a liaison between the fund and the auditor. Although the NCE’s manager remains responsible, fund administration services may allow an NCE to outsource many of the in-house, back-office tasks that would otherwise fall on NCE managers to perform or oversee.

Examples of the roles and functions that are often undertaken by a fund administrator, depending upon the administrator’s competencies, may include:

### 1. *Regulatory Administration and Compliance Support Services*

- Compiling data for the fund’s annual reports
- Preparing and reviewing the fund’s financial statements

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- Upon advice and direction from fund's counsel, preparing regulatory forms
- Developing with the fund's counsel, agendas for meetings
- Attending meetings and preparing minutes
- Preparing a compliance calendar for the fund

## 2. *Financial Accounting and Investor Reporting*

- Preparing administrative and procedural process
- Establishing and maintaining general ledgers
- Reconciling and confirming investor contributions
- Establishing, reconciling, and maintaining investor capital accounts and effecting all appropriate allocations
- Calculating management fees and incentive allocations
- Generating financing reporting packages
- Generating and distributing capital account statements
- Distributing offering and subscription materials per the fund's direction in accordance with marketing arrangements
- Coordinating processing of new investor subscriptions, which may include: coordinating receipt of funds, providing fund with status reports for wires and subscription agreements, coordinating fund transfers with escrow agent; coordinating holdback calculations and tracking per in-

vestor; returning investments to subscribers whose subscriptions have not been accepted; and sending acceptance letters to new investors

## 3. *Audit Coordination*

- Conducting audit planning and coordination
- Preparing work papers and schedules for auditors
- Preparing financial statements, footnotes, and report drafts
- Acting as a liaison between auditors and the fund

An independent fund administrator in the context of an EB-5 transaction could assume, in part, the role of an independent third party trustee that would help comfort EB-5 investors that their interests are being looked after through execution of the agreed upon process and procedure. Further, if Section (P) of HR 5992 becomes law, fund administrators could help fund managers comply with legal requirements by acting as an authorized signatory. Some administrators already act as co-signers on a fund's bank account to help ensure that money transfers are limited to their intended and authorized purpose. Although acting as an authorized signatory as proposed in Section (P) may be outside of the suite of services that today's fund administrators typically provide, fund administrators may already have the personnel and expertise that will be needed to provide this type of independent oversight for the benefit of investors while at the same time reducing some of the administrative burden that currently falls on EB-5 fund managers.

Fraud has occurred in only a small number of EB-5 projects; however, in most instances of fraud the NCE maintained complete, unfettered control of the investment funds. In 2013, The U.S. Securities and Exchange Commission's (SEC) Office of Investor Education and Advocacy and U.S. Citizenship and Immigration Services (USCIS) issued a joint Investor Alert, reminding potential EB-5 investors to thoroughly research EB-5 offerings and to take steps to help protect themselves from fraud. Among the "hallmarks of fraud" listed in the Investor Alert is "Layers of companies run by the same individuals" – in essence, conflicts of interest is the common denominator of the EB-5 fraud cases to-date. As a result, it seems that EB-5 investors are asking more questions about procedure after funds are deposited into escrow than in prior years and Section (P) may be a way to help guide the industry toward a procedure that provides more comfort to savvy investors than has previously been offered by most EB-5 issuers. In retrospect, some of the proposals in Section (P) may have effectively curbed most of the known EB-5 fraud. Whether or not Section (P) or a similar iteration of regulation is enacted, EB-5 investors may soon demand more transparency and insight into how their funds flow through the investment process.

The regulatory landscape for the Regional Center Program remains rather vast and full of possibilities for industry pioneers. Bridges – from EB-5 investor, to NCE, to JCE posted by independent third-party sentries, like fund administrators, may help light the way through the EB-5 investment cycle increasing the likelihood that EB-5 investors reach their destination. ■