UDF Executives Ordered to Pay $8.3 Million to Settle SEC Charges

The Securities and Exchange Commission has charged two real estate investment funds and four executives for allegedly misleading investors by failing to disclose that it could not pay its distributions and was using money from a newer fund to pay distributions to investors in the older fund. The SEC also charged a fifth executive for allegedly signing false SEC filings.

United Development Funding is a family of private and publicly-traded investment funds that deploys investor capital as loans to homebuilders and land developers. The SEC said that UDF allegedly solicited investors by advertising annualized returns of up to 9.75 percent as well as regular distributions.

The SEC's complaint named UDF III, UDF IV, and various UDF executives including co-founder and CEO Hollis Greenlaw, president Benjamin Wissink, chairman and co-founder Theodore Etter, chief financial officer Cara Obert, and David Hanson, the chief accounting officer of UDF IV.

The regulators claim that for nearly five years, UDF did not tell investors that it lacked the monthly cashflow at times to cover investor distributions in one of its older funds, UDF III, a publicly registered non-traded limited partnership.

Instead, to pay these distributions, the company's newer public REIT, UDF IV, allegedly loaned money to developers who had also borrowed money from UDF III. Rather than using those funds for development projects that were underwritten by UDF IV, UDF directed the developers to use the loaned money to pay down their older loans from UDF III.

The SEC claims that in most of these cases, the developer never received the borrowed funds, and UDF transferred the money between funds so that UDF III could make the distributions to its investors.

The complaint also alleges that UDF III failed to appropriately impair loans in violation of GAAP, and that UDF IV did not adequately disclose the status of real property within its portfolio.

Finally, the complaint accuses David Hanson of signing false and misleading SEC filings and management representation letters without taking sufficient actions to ensure their accuracy.

Without admitting or denying the allegations, Greenlaw, Wissink, Etter, and Obert agreed to pay $7.2 million in disgorgement and prejudgment interest, as well as a $1.1 million fine, while Hanson agreed to pay a $75,000 fine. The defendants also agreed to orders enjoining them from violating certain federal securities law provisions in the future.

In a statement, Greenlaw said "We believe that it was time to put this matter behind us and that this settlement is in the best interests of UDF and its investors. UDF IV had already undergone an independent investigation conducted by the law firm Thompson & Knight LLP with the assistance of independent forensic accountants from a global accounting firm."

The company's commissioned investigation concluded in May 2016 and found no evidence of fraud or misconduct.

"The settlement will allow the companies to avoid the time, expense and distraction of a potential dispute with the SEC, which will enable UDF to focus on returning value to its investors," added Greenlaw. "Furthermore, UDF believes their business was injured by Kyle Bass and Hayman Capital, and it intends to pursue that litigation with all the more vigor now that this SEC matter is resolved."

In early 2016, hedge fund manager Kyle Bass publicly accused UDF IV of operating a "Ponzi-like real estate scheme," by using new investor money to pay existing investors. It was later revealed that Bass held a short position in the company's common stock.

UDF filed a lawsuit against Bass and his Hayman Capital hedge funds late last year, claiming that their funds were financially damaged by their accusations. UDF believes that Bass and his funds raked in profits of an estimated $60 million or more as a result of their short position. A Dallas court recently denied a motion by Bass to dismiss the lawsuit, allowing it to proceed to trial.

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