UDF Responds to Ponzi Charges, Discloses SEC Investigation

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United Development Funding IV (NASDAQ:UDF), a publicly traded real estate investment trust, saw its shares plummet late last week following two anonymous online reports posted on Harvest Exchange, an investor networking website.

The first report, a 3-page missive titled, "A Texas-Sized Scheme: Exposing the Darkest Corner of the REIT Business, United Development Funding (UDF)", accuses "the UDF umbrella, [which includes both traded and non-traded REIT products], of exhibiting characteristics emblematic of a Ponzi scheme."

UDF III, a non-traded limited partnership, and UDF IV quickly responded to the rumors by issuing a joint press release stating that "a hedge fund has created a significant short position in United Development Funding IV shares [and the company believes the hedge fund is] trying to unlawfully profit by manipulating and depressing the [share] price."

The UDF press release also revealed that the companies have been the subject of a nonpublic fact-finding investigation being conducted by the Securities and Exchange Commission since April 2014.

According to the release, "the SEC has informed the companies that this investigation is not an indication that any violations of law have occurred or that the SEC has any negative opinion of any person, entity, or security."

On a brief conference call with financial advisors on Friday afternoon, UDF chairman and chief executive officer, Hollis M. Greenlaw, vigorously denied the Ponzi-scheme charges.

On Monday morning, UDF issued a detailed press release disputing the statements posted to the Harvest website while addressing additional questions from investors.

The company said, "The statements clearly demonstrate a lack of understanding of the residential development project life cycle, which typically involves multi-phase master planned communities and the related financing structures. Investors who wish to understand our business should review our registration statements and periodic SEC filings, which describe the business model for each fund."

Regarding the alleged "short and distort" scheme, the company explained that "UDF IV short activity reported by Nasdaq.com at November 30, 2015 was in excess of 4.1 million shares, up from approximately 59,000 shares on December 31, 2014." The company indicated that they have communicated the knowledge of the facts and circumstances to the Securities and Exchange Commission. The company further defended its position stating that their "underlying business model is sound" and "the fundamentals of [their] business have not changed from the end of the September quarter to the date of the anonymous release of misleading information on December 10th."

While the two anonymous reports' claims remain unsubstantiated, investors quickly reacted and the price of UDF shares have plunged dramatically. Shares lost more than 52 percent and closed at $8.55 on Friday, down from $17.85 on Thursday. UDF originally listed on the New York Stock Exchange in June 2014 and sold its shares for $20 apiece. The company's share price has remained relatively stable since that time.

Following the original statement by UDF, a second anonymous report was posted on the Harvest website titled, "United Development Funding (UDF) – One Example of Many: How The Scheme Works, from One UDF Fund to the Next." The detailed 20-page report noted that "UDF did not refute the allegations and instead disclosed the SEC investigation."

As previously reported by The DI Wire, Whitley Penn LLP declined to stand for reappointment as the independent registered public accounting firm of the various UDF companies. No explanation for the resignation was offered by either UDF or Whitley Penn, beyond the standard publicly filed disclosure.