Ariel A. Neuman - State Bar No. 241594
aneuman@birdmarella.com
David H. Chao - State Bar No. 273953
dchao@birdmarella.com
Ashley D. Bowman – State Bar No. 286009
abowman@birdmarella.com
BIRD, MARELLA, BOXER, WOLPERT, NESSIM, DROOKS, LINCENBERG & RHOW, P.C.
1875 Century Park East, 23rd Floor
Los Angeles, California 90067-2561
Telephone: (310) 201-2100
Facsimile: (310) 201-2110

Attorneys for Defendants Hui Feng and Law Offices of Feng & Associates P.C.

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA, WESTERN DIVISION

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

vs.

HUI FENG; LAW OFFICES OF FENG & ASSOCIATES P.C.,

Defendants.

CASE NO. 2:15-CV-09420-CBM-SS

DEFENDANTS HUI FENG AND LAW OFFICES OF FENG & ASSOCIATES P.C.'S REPLY BRIEF IN SUPPORT OF MOTION FOR JUDGMENT ON THE PLEADINGS

Date: July 26, 2016
Time: 10:00 a.m.
Crtrm.: 2

Assigned to Hon. Consuelo B. Marshall

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I

INTRODUCTION

There is no dispute that the SEC has never issued a rule, order, adjudication, or any other guidance even suggesting that immigration lawyers assisting EB-5 clients to navigate the complex USCIS program requirements must register as brokers. Indeed, there is no dispute that for the first 23 years of the EB-5 program's existence, the SEC did not see fit to even try to regulate EB-5 investments and then, in its only comment on the matter – in 2013 – the SEC equivocated that *some* EB-5 contributions *may* be "securities" under federal law, but failed to take a clear position. There is also no dispute that this action against Defendants Hui Feng and Law Offices of Feng & Associates, P.C. ("Feng Parties") (and concurrently filed cases against other lawyers) is the SEC's first attempt to ever seek to apply the securities laws to an immigration attorney and his law firm in connection with his provision of legal services to EB-5 clients. Nor is there any debate that the Feng Parties provided highly valuable legal services to their clients to ensure their visa applications would be granted by USCIS, but did not give advice on investment returns. To assert, as the SEC does, that the Feng Parties were thus on notice that EB-5 contributions were securities and they had become brokers offends both common sense and basic principles of fairness.

The Feng Parties had no reason to believe they were acting as brokers by providing competent legal counsel to their EB-5 clients. While the SEC exhorts that the vagueness inquiry must be confined to the facts of this case, it repeatedly distorts those facts to serve its needs rather than face the actual circumstances in which the Feng Parties found themselves. For instance, the offering documents referenced in the Complaint clearly establish that *none* of the Feng Parties' clients had a reasonable expectation of profit, gutting any argument that the EB-5 investments were securities in the first place. Nor did the Feng Parties conduct traditional "broker" tasks; instead, they provided immigration counsel and occasionally helped

their EB-5 clients with administrative tasks such as obtaining signatures or emailing documents. Never once did they negotiate EB-5 project terms or analyze the financial needs of the regional centers. Further, the SEC's assertion that regional centers expressed concerns about the broker registration statute to Feng is simply false and cannot be found in the pleadings. And contrary to the SEC's casual reference to Feng as an "EB-5 securities salesman," it is undisputed that he never sold a single security to any client.

A person of ordinary intelligence under the foregoing circumstances would have no reasonable basis to know that his or her provision of legal services would amount to prohibited broker activity. This is particularly true given that until seven months ago, the SEC had never even hinted that someone in the Feng Parties' position would be considered a broker. Section 15(a) of the Exchange Act is therefore void for vagueness as applied to the conduct in this case.

The SEC's response to the Feng Parties' Rule 9(b) argument is similarly disconnected from reality. Although not a single client has come forward and claimed to be defrauded, and the SEC does not claim that *every* client was defrauded, the SEC maintains that it need not identify with particularity which of the Feng Parties' numerous clients the *SEC believes* were defrauded so that the Feng Parties might be able to prepare their defense for trial. And although the SEC suggests at several points in its Complaint and motion papers that only *some* of the regional centers at issue in this case were victims of the alleged fraud, it again asserts that it need not identify them by name (though again, none have come forward to demand money back). The SEC has no excuse for this deficiency; it has long possessed a list of the Feng Parties' clients and the relevant regional centers thanks to its year-long investigation prior to filing this case. It also clearly had particular victims in mind when it undertook this significant enforcement action. It just does not want to tell the Feng Parties who they are. Any private plaintiff alleging similar claims would be expected to file an amended complaint that

complies with Rule 9(b), and the SEC should not receive special treatment in this regard.

The Complaint must be dismissed in its entirety and judgment should be entered on the unregistered broker claim in favor of the Feng Parties.

II

FACTUAL BACKGROUND

To distract from the deficiencies in the Complaint and to bolster its claims, the SEC's Opposition repeatedly mischaracterizes the Feng Parties' Answer. Finding the actual facts established by pleadings insufficient to support its claims, the SEC attempts to fabricate new ones.

For instance, the SEC repeatedly asserts that the Feng Parties "admit" or "agree" that EB-5 clients were motivated to enter the EB-5 program at least in part to obtain a return on their investment. *See* Opp. at 7. In fact, in their Answer, the Feng Parties repeatedly deny such claims and admit only that the program is designed to attract immigrants willing to put their capital at risk with the expectation of receiving a green card. Answer ¶ 14. They further state that their clients' main purpose for entering the EB-5 program was to be eligible for visa status "because any return [the EB-5 program investment] generates cannot cover the cost and justify the risk of entering the EB-5 program" unless the client is simply aiming to obtain a green card. Answer ¶ 40.

In paragraph 51 of the Answer, the Feng Parties deny that they "facilitated" their clients' investments, and admit only that they provided clients occasional "administrative assistance" with paperwork and the same "administrative and legal service duties" that any attorney would typically give clients. But again, the SEC ignores this denial and claims that Defendants "admit they facilitated their clients' investments." Opp. at 8:5-7.

In paragraph 52 of the Answer, the Feng Parties clarified that Feng interfaced with regional centers to make sure their clients were eligible to file immigrant visa

applications. The SEC completely ignores this clarification and misquotes the Answer as an admission that the Feng Parties "'interfaced directly' with the regional centers regarding their clients' investments." Opp. at 8:5-7.

Finally, the SEC even mischaracterizes its own Complaint. Nowhere does the Complaint allege that the regional centers "expressed concerns" to the Feng Parties that payment to the Feng Parties' U.S.-based bank accounts may trigger the broker registration requirements. *Compare* Opp. at 8:19-20 to Compl. ¶ 76. Such editorializing by the SEC is an effort to contrive some form of notice to the Feng Parties where none existed.

As discussed herein, such twisting of facts permeates the SEC's Opposition and undermines its arguments at every turn. Other examples are discussed where relevant below. But perhaps most relevant, the SEC does not contest the primary fact underlying the Feng Parties' Motion: that until this case was filed, the SEC had never so much as hinted that an immigration lawyer assisting EB-5 clients to navigate a complex *immigration* program might be required to register as a broker in order to carry out his legal work.

III

ARGUMENT

A. The Unregistered Broker Statute Is Void for Vagueness

The SEC's section 15(a) claim violates Due Process because the term "broker" is void for vagueness as applied to the alleged conduct in this case. The SEC does not dispute that the term "broker" lacks a coherent definition, and concedes that the agency has done nothing over the past 25 years to clarify its meaning as applied to immigration attorneys in the EB-5 industry. Because an ordinary person in the Feng Parties' position would not have reason to know he qualified as a broker, the unregistered broker claim must be dismissed.

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1. The Definition Of "Broker" Is So Vague That People Of Ordinary Intelligence Must Guess At Its Meaning

The SEC's Opposition confirms that the unregistered broker statute is vague on its face. The SEC readily admits that the Exchange Act fails to define the crux of the broker definition – i.e., "being engaged in the business of effecting transactions." Faced with these loose terms, the SEC does not dispute that the average person must guess at the meaning of "broker" and that even federal judges differ on its application. In other words, the SEC concedes by omission that "men of common intelligence must necessarily guess at its meaning and differ as to its application." *United States v. Hockings*, 129 F.3d 1069, 1072 (9th Cir. 1997). Indeed, the SEC's selective citation to one strain of case law, and complete disregard for contrary authority cited in the Motion, merely serves to amplify that the statute is vulnerable to uneven and arbitrary enforcement.

While the SEC wants to focus on cherry-picked cases that define "broker" in terms serving the SEC's interests in this case – i.e., non-binding decisions that prioritize the receipt of transaction-based compensation – it conspicuously ignores the analysis in contrasting cases cited in the Motion. Those cases uniformly teach that mere compensation is *not* dispositive of the broker inquiry, but rather that fact-finders must evaluate whether the defendant *performed tasks* indicative of what brokers do. For example, in *S.E.C. v. M&A West, Inc.*, No. C-01-3376 VRW, 2005 WL 1514101 (N.D. Cal. June 20, 2005), *aff'd*, 538 F.3d 1043 (9th Cir. 2008), the district court concluded the defendant was not a broker because, even though he received compensation, he did not perform the core tasks of a broker. *Id.* at *9. Instead, the court observed the tasks performed by the defendant were akin to those of paralegals, lawyers, and businessmen who "facilitate" transactions, while noting the defendant lacked authority to actually enter transactions "for the account of others." *Id. See also S.E.C. v. Kramer*, 778 F. Supp. 2d 1320 (M.D. Fla. 2011) (finder who earned compensation did not perform tasks amounting to broker

activity).[1] That other federal courts have rejected the SEC's preferred focus on transaction-based compensation demonstrates the meaning of "broker" is hard to capture, not only to laymen but also to government agencies and federal judges alike who have expertise in statutory interpretation.

Moreover, even the authority cited by the SEC recognizes that most courts do not accord special weight to transaction-based compensation but rather look to a mix of *tasks* that might amount to broker activity. *See S.E.C. v. Collyard*, No. 11-CV-3656, 2015 WL 8483258, at *3-4 (D. Minn. Dec. 9, 2015). Some courts ask whether the person (1) is an employee of the issuer; (2) received commissions; (3) sold securities of the issuer; (4) was involved in negotiations between the issuer and investor; (5) made valuations as to the merits of the investment; and (6) was an active finder of investors. *Id.* at *3 (citing *S.E.C. v. Hansen*, No. 83-CV-3692, 1984 WL 2413, at *10 (S.D.N.Y. Apr. 6, 2014)). Others consider different factors, including "handling customer funds and securities, participating in the order-taking or order-routing process, and extending or arranging for the extension of credit in connection with a securities transaction." *Id.* at *4 (citation omitted). Still other courts ask whether the tasks performed include "analyzing the financial needs of an issuer, recommending or designing financing methods, involvement in negotiations, discussion of details of securities transactions, making investment recommendations, and prior involvement in the sale of securities." *Cornhusker Energy Lexington, LLC v. Prospect St. Ventures*, No. 8:04CV586, 2006 WL 2620985, at *6 (D. Neb. Sept. 12, 2006). In sum, far from presenting a clear definition of what it means to be a broker, the SEC's Opposition reveals the exact

[1] Instead of focusing on the analysis in these cases, the SEC attempts to dismiss them because the analysis was done at a different stage of the proceedings. Opp. at 18-19. That is irrelevant. What matters is the factors courts have used to analyze whether someone is a broker, and whether those analyses would fairly put the Feng Parties on notice that they were acting as such.

opposite: that federal courts have come to varying constructions of the term. If even jurists differ on this point, there is no question that persons of common intelligence must necessarily guess at the meaning of broker without specific and unambiguous guidance. *Hockings*, 129 F.3d at 1072. And, it is precisely because there are so many diverse factors for the SEC to pick and choose from that the statute is particularly susceptible to inconsistent enforcement.

2. Section 15(a) Is Unconstitutionally Vague As Applied To The Feng Parties

Not only is the broker definition vague on its face, but this uncertainty is compounded in this case, where after 25 years of silence the SEC now seeks to apply the unregistered broker statute in a field of *immigration* law that it does not administer, and against a class of persons that have never been subject to the securities laws for their services in this industry. An ordinary person in the Feng Parties' position would have no reason to know that the EB-5 investments involved securities in the first place, and thus by definition would not have known he was acting as a broker. And even if he knew they were securities, he still would have no reason to believe that providing legal services to EB-5 clients would amount to broker conduct.

a. Feng Parties Lacked Fair Notice That Their Clients' EB-5 Investments Were Securities

The Feng Parties lacked fair notice that their clients' participation in EB-5 projects involved securities in the eyes of the SEC. On this point, the SEC's Opposition is far more telling by what it does not say, than what it says. The SEC does not dispute that for more than 23 years, it did not even attempt to regulate the EB-5 program at all – i.e., no formal or informal rulemaking, adjudication, enforcement, or otherwise.[2] This is not surprising, since it is also undisputed that

[2] The SEC attempts to excuse its absenteeism by arguing that the EB-5 program

the EB-5 program was intended by Congress and the President to attract foreign capital to stimulate job creation, not to create a market for securities. Nor does the SEC dispute that before 2013, the SEC failed to articulate any position whatsoever about whether it deemed EB-5 projects to involve securities. And it does not dispute that when it first spoke on the issue in 2013, it still failed to take a position: the October 2013 "Investor Alert" merely stated that EB-5 program "may" involve securities, which necessarily implies that some EB-5 investments *may not* constitute securities. Apparently unsure of its position, the SEC offered zero guidance on how to tell the difference. Without this guidance, and keeping this historical context in mind, to believe that anyone in the Feng Parties' position would understand that EB-5 projects involved securities in the eyes of the SEC cannot be squared with common sense, much less with the traditional notions of fairness that undergird the Due Process Clause.

Unable to rebut these realities, the SEC instead attempts to divert the Court's attention to a self-serving sampling of evidence, which the SEC contends placed the Feng Parties on notice that their clients' EB-5 projects involved securities. However, the few documents cited by the SEC come nowhere close to establishing fair notice to the Feng Parties.

(i) Fine Print Buried In Two "Offering" Documents Does Not Establish Fair Notice

Although the SEC vaguely asserts the Feng Parties have represented over 100 EB-5 clients, it has cherry-picked offering documents from just two EB-5 projects in 2012, claiming they placed the Feng Parties on notice that EB-5 investments are securities in the eyes of the SEC. The documents themselves, however, suggest no

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was unpopular during the first two decades of its existence. But this misses the point. Regardless of the SEC's subjective reasons for failing to regulate, the fact remains the SEC's protracted silence undercuts any objective fair notice to the EB-5 industry that its transactions involved securities.

such thing.

As a threshold matter, the SEC has laid no foundation for the authenticity of these documents, or that the Feng Parties even reviewed them. Notably, the Complaint only alleges that Feng obtained offering documents from regional centers, circulated them to his clients, and transmitted the signed pages to regional centers. Compl. ¶¶ 40, 51. Nothing in the Complaint suggests that the Feng Parties reviewed the fine print themselves, or had reason to do so. In fact, in their Answer, the Feng Parties make clear that their clients were responsible for choosing EB-5 projects on their own. Answer ¶ 40. Accordingly, it is implausible to accept that these two documents put the Feng Parties on notice.

But even if the Court accepts the SEC's naked assumption that the Feng Parties reviewed the fine print of such offering documents, the language in the documents is nowhere as clear cut as the SEC portrays. Tellingly, both offering documents cited by the SEC expressly define the investments as "units," rather than shares or securities.[3] Further, both documents explain that the units have not been registered under securities laws because they are exempt. Dkt. 44-1 ("SEC RJN"), Ex. 2 at p. 5 ("The units have not been and will not be registered under the Securities Act or 1933 . . . or any state securities laws or the law of any foreign jurisdiction."); *id.*, Ex. 11 at p. 4 ("These Units have not been registered under the Securities Act or under applicable state securities laws."). Both documents also expressly state that the units were not in any way subject to the review of the SEC. *Id.*, Ex. 2 at p. 5 ("The units offered hereby have not been approved or disapproved by any securities regulatory authority of any state or by the United States Securities

[3] The SEC's reference to the usage of the term "restricted securities" is isolated to a single instance in the document from the American Dream Fund LLC, and is buried in a boilerplate section in the middle of a 110-page document. SEC RJN, Ex. 11 at p. 290. However, the rest of the document consistently refers to the investments as "units."

and Exchange Commission or by an securities regulatory authority in any other jurisdiction . . . ."); *id.*, Ex. 11 at p. 4-5 ("Neither the Securities and Exchange Commission nor any state securities regulatory authority has approved or disapproved the offer and sale of these Units . . . .").

No matter what an SEC lawyer may claim should be the take-away from such text, the documents hardly contain a clear statement that these "units" are securities subject to regulation by the SEC. In fact, an ordinary reader could reasonably conclude exactly the opposite given that they were named "units" rather than "securities," and since the documents emphasized they were *not* subject to the oversight of the SEC. Such a conclusion would have been readily validated by the fact that, for more than two decades up to that point (and for years going forward from then), EB-5 investments were in fact *not* subject to the oversight of the SEC.

(ii) Case Law Confirmed EB-5 Projects Did Not Involve Securities

Furthermore, regardless of whether these statements were cause for doubt (if the Feng Parties ever saw them), settled case law and the actual nature of the transactions gave the Feng Parties ample reason to believe their clients' EB-5 investments were *not* in fact securities. In its Opposition, the SEC attempts to minimize *Forman* by arguing that the Feng Parties' EB-5 clients had "dual motivations" of both obtaining a green card and an expectation of profit. But the SEC's argument both misstates the holding of *Forman* and ultimately assumes facts not supported by the pleadings (or reality).

First, the *Forman* Court did not hold that a security exists as long as the investor has "dual motivations" to both use and profit from the item purchased. Instead, the Court wrote that the test for a "security" is whether the "investor 'is attracted *solely* by the prospects of a return' on his investment." *Id.* at 852 (emphasis added) (quoting *S.E.C. v. W.J. Howey Co.*, 328 U.S. 293, 300 (1946)). "By contrast, when a purchaser is motivated by a desire to use or consume the item

purchased . . . the securities laws do not apply." *Id.* By drawing this contrast, the Court explained that if an investor has another motivation to use the item purchased, then he is not "attracted solely" by the prospect of profit, and the investment is not a security. Therefore, even if it were true that the Feng Parties' clients had dual motivations, this clearly fails the test articulated in *Forman* because the investors are not "solely attracted by the prospects of a return," but rather have a different motivation to obtain a visa. Therefore, the SEC's "dual motivations" concept does not alter the conclusion that, under *Forman*, EB-5 investments are not securities.

Second, and bolstering the first point, the pleadings establish that the Feng Parties' EB-5 clients lacked any reasonable expectation of profit. In fact, as the SEC well knows, the evidence shows that the vast majority if not all of the Feng Parties' EB-5 clients knew from the outset that they were going to *lose money*. The fact is, they did not care so long as they got their visa.

For instance, in support of its Opposition to the Feng Parties' transfer motion, the SEC submitted an exhibit reflecting a comprehensive listing of the Feng Parties' EB-5 clients.[4] Dkt. 15-3, Ex. 2. The listing makes clear that each and every client's expected return ("Total Interest to Clients") was so negligible that it was entirely offset, and in the vast majority of cases, completely ***outweighed by*** the management fee paid to the regional center leading the project ("Management Fee"). *See also* Compl. ¶¶ 32-33 (alleging the separate payment of management fees, which was not pooled for purposes of making loans). This was no surprise to the clients, because the offering literature for all these EB-5 projects explicitly disclosed the amount of the administrative or management fees and the anticipated return (or lack thereof).[5]

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[4] The SEC's Opposition repeatedly cites prior filings in this case and documents referenced generally in the Complaint. The Feng Parties thus proceed likewise.

[5] *See* SEC RJN Ex. 2 at pp. 4, 31, 35 (no interest mentioned); Ex. 11 at 2, 30; Feng Parties' Supplemental RJN ("Supp. RJN"), Ex. A at pp. 4-5, 45; Ex. B at pp. ii, 53; Ex. C at pp. ii, 39; Ex. D at pp. ii, 45; Ex. E at pp. ii, 42; Ex. F at pp. ii, 43; Ex.

Because the offering documents disclosed to the EB-5 clients that their expected return would be eclipsed by mandatory fees, the pleadings establish that the EB-5 clients had no reasonable expectation of profits. *See Warfield v. Alaniz*, 569 F.3d 1015, 1021 (9th Cir. 2009) ("[W]e must focus our inquiry on what the purchasers were offered or promised.").[6]

The Ninth Circuit's decision in *S.E.C. v. Goldfield Deep Mines Co. of Nevada*, 758 F.2d 459 (9th Cir. 1985), is therefore distinguishable. There, the court held that an ore purchase program involved securities because the promotional literature "evinced a clear expectation of eventual profit," despite the expectation of initial losses. *Id.* at 463-464. By contrast, the EB-5 offering materials provided to the Feng Parties' clients uniformly disclosed that their expected return, if any, would be dwarfed by management fees, not to mention legal fees and the devaluing effect of inflation over the 5-6 year investment period. Unlike the investors in *Goldfield*, the Feng Parties' clients had no reasonable expectation of profit.[7]

Taking this into account, and given the SEC's historical absence from this field, a person in the Feng Parties' position would not assume that he was working in connection with securities, and therefore lacked fair notice that his legal services

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G at pp. 2, 4; Ex. H at pp. 2-3, 24; Ex. I at pp. 4, 11-12.

[6] The SEC alleges that the Feng Parties' clients "received Schedule K-1s that reflected the interest (i.e. profits) they had earned on their capital contributions." Opp. at 4:21-23. But these K-1s confirm that the Feng Parties' clients earned minimal interest on their investments, and in reality saw a negative return. (*See, e.g.*, Supp. RJN Exs. J-K.) As explained above, after accounting for administrative and legal fees related to the EB-5 projects, the amounts paid by the Feng Parties' clients virtually always exceeded any expected return (i.e., they lost money).

[7] Even if the EB-5 clients had expected some profit, several courts have noted in the case of dual motivation, the case law insists that the fact finder must look to the purchaser's "primary motive." See *Rice v. Braniger Organization, Inc.*, 922 F. 2d 788 (11th Cir. 1991); *Grenader v. Spitz*, 537 F. 2d 612 (2d Cir. 1976). Here, even the SEC does not contend the primary motive for the Feng Parties' clients was anything other than getting a green card.

could possibly constitute broker conduct.[8]

3. The Feng Parties' Lacked Fair Notice That Their Legal Services Constituted Broker Activity

Section 15(a) is vague as applied to this case for the independent reason that it failed to give fair notice to the Feng Parties that their legal services and ministerial tasks constituted prohibited broker activity.

a. Case Law Did Not Give The Feng Parties Fair Notice They Were Acting As Brokers

None of the cases cited by the SEC, taken individually or together, gave fair notice that the Feng Parties were acting as brokers. Although the SEC references a "rich" body of case law articulating the elements of broker activity, it fails to unpack those elements. If it had, it would have found that the Feng Parties did not engage in any of the substantive tasks that brokers typically perform.[9] The Feng Parties

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[8] Stretching to support its arguments, and despite its observation that "the Court may not properly take judicial notice of the our-of-court statements of another immigration attorney for the truth of the matter asserted," Opp. at 14-15 n.2, two pages later the SEC asks the Court to do precisely this by taking notice of a blog post purportedly authored by Feng's prior counsel, John Roth. Concurrently with this reply brief, the Feng Parties' have filed formal objections to the SEC's request for judicial notice of this blog post. As explained therein, the Court should deny the SEC's request, both because the SEC admits that it cannot be subject to judicial notice, and because it is plainly irrelevant. Even assuming the blog's author was truly Feng's prior counsel – a distinct assumption that is not subject to judicial notice and lacks foundation – his opinion is irrelevant because the Due Process inquiry is what an ordinary person in the Feng Parties' historical context would know, not what a random immigration attorney and registered broker chosen by the SEC would opine.

[9] The SEC concedes that the purpose of the unregistered broker statute is "to ensure that 'securities are [only] sold by a salesman who understands and appreciates both the nature of the securities he sells and his responsibilities to the investor to whom he sells.'" *Roth v. S.E.C.*, 22 F.3d 1108, 1109 (D.C. Cir. 1994) (quoting "Persons Deemed Not to Be Brokers," Exchange Act Release No. 20,943 (May 9, 1984), 49 Fed. Reg. 20,512, 20,515 (1984)). It is undisputed that the Feng

were not employed by any issuers, did not sell securities for any issuers, did not engage in negotiations between issuers and investors, and did not make valuations. *See Hansen*, 1984 WL 2413, at *10. They did not take or route purchase orders, or arrange for the extension of credit. *See Collyard*, 2015 WL 8483258, at *4. Nor did they analyze the financial needs of any issuers, recommend or design financing methods, or make financial investment recommendations." *See Cornhusker Energy*, 2006 WL 2620985, at *6.

By contrast, the pleadings establish at most that Feng occasionally accommodated his EB-5 clients' requests for ministerial assistance, and at all times performed legal tasks that any EB-5 immigration lawyer would do:

- While the Complaint alleges that the Feng Parties had a website containing a list of "recommended EB-5 offerings," the Answer explains that Feng's recommendations were "based on a conscientious study of various USCIS Policy Memorandums and the business plan requirements according to Matter of Ho, a precedent decision by the Administrative Appeals Office ("AAO") in 1998." Answer ¶ 50.[10] Which means, Feng's work was designed to ensure that his clients participated in EB-5 programs that complied with USCIS requirements and thus were most likely to get them a green card, not to help them get a return on his investment.
- While the Complaint alleges that Feng "facilitated" his clients' EB-5 investments, the Answer clarifies that on some occasions he

Parties did not sell securities to their EB-5 clients.

[10] As demonstrated in this instance and below, the SEC relies on vague and broadly worded allegations in the Complaint. The Feng Parties' Answer, however, clarified those allegations and brought meaning to the words used by the SEC. In ruling on a 12(c) motion, the court accepts as true all allegations in the Complaint and treats as false only those allegations in the Answer that contradict the allegations in the Complaint. *MacDonald v. Grace Church Seattle*, 457 F.3d 1079, 1081 (9th Cir. 2006). None of the allegations in the Answer cited here contradict the allegations by the SEC, and so should be accepted as true.

accommodated his clients' request for administrative help, whereby he might explain or translate certain terms of documents, print out signature pages, explain how to sign properly, and transmit documents to the regional centers. *Id.* ¶ 51.

- While the Complaint alleges that Feng "interfaced directly" with regional centers, the Answer clarifies that Feng sometimes asked regional centers questions to assess their likelihood of EB-5 compliance, consistent with his function as immigration counsel. *Id.* ¶ 52.
- While the Complaint alleges that Feng "channeled" communications between his clients and regional centers, the Answer clarifies that Feng served occasionally as a language translator to help his clients understand the EB-5 projects, but did not negotiate with the regional centers concerning the projects or analyze their financing needs. *Id.* ¶ 53.
- While the SEC alleges that the Feng Parties received EB-5 investment funds from clients that they transmitted to regional centers, the Answer clarifies that in only two isolated instances, due to foreign currency exchange control issues in China, the Feng Parties used their bank account to help clients transmit funds to regional centers. The Feng Parties did not charge for this courtesy and it was not a regular practice. *Id.* ¶ 54.

In sum, the Feng Parties engaged in none of the substantive tasks commonly associated with brokers, but rather provided ordinary legal services in the same way that any EB-5 immigration lawyer would. Accordingly, they had no cause to believe their services would trigger the broker statute.[11]

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[11] Indeed, even Congress's deliberations regarding potential reforms to the EB-5 program since 2015 demonstrate the ambiguity surrounding whether these investments are securities, and how to define the role of third parties who interact with regional centers Tellingly, draft Senate legislation proposes adding language to 8 U.S.C. § 1153(b) to delineate, for the first time, the concept of "compliance with

Nor would the decision in *S.E.C. v. Benger*, 697 F. Supp. 2d 932 (N.D. Ill. 2010), have put the Feng Parties on notice that the broker statute may apply to attorneys such as them. That case concerns an attorney who, unlike Feng, was not providing legal services to an investor but was instead regularly engaged in the substantive tasks that brokers are known to perform: serving as escrow agent for the transactions at issue, tasked with receiving money from investors and distributing them to issuers, communicating with issuers regarding receipt of funds and documents, and receiving and processing documents for the sale of securities. *Id.* at 936, 945. Since it is undisputed that the Feng Parties were not escrow agents or otherwise regularly engaged in such tasks, it is unfair to presume this case put them on notice.[12]

The SEC also attempts to rely upon one of its own no-action letters from 2010 to suggest that anyone who has received transaction-based compensation as a "finder" was on notice they are a broker. This argument fails, however, because of

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securities laws," including whether subject matter jurisdiction even lies in the United States, implying the prior uncertainty and need for clarification on this issue. *See* S. 1501, 114th Cong. § 2(b)(I)(i) (2015), available online at https://www.congress.gov/bill/114th-congress/senate-bill/1501/text. Furthermore, the proposed bill indicates that even if an attorney acts as a "third-party promoter" of a regional center, he or she is only required to register with USCIS, not the SEC. *See id.*§ 2(b)(K)(i)(I). Finally, the proposed legislation places the burden on regional centers, and not immigration attorneys, to be responsible for the broker-like functions of "monitor[ing] and supervis[ing] all offers, purchases, and sales of securities made by the parties associated with the regional center to ensure compliance with U.S. securities laws." *Id.* § 2(b)(I)(iii).

[12] The SEC cites two enforcement actions in 2013 that it claims put the Feng Parties on notice that they were acting as brokers. However, neither case involves an immigration lawyer at all, much less whether the provision of legal services can amount to broker conduct. Both cases were brought against regional centers who either lied to clients about the nature of their investments, or misappropriated their money (i.e., spent it or embezzled it). *See S.E.C. v. Chicago Convention Center, LLC*, No. 13CV982 (N.D. Ill.); *S.E.C. v. Ramirez*, No. 7:13-cv-00531 (S.D. Tex.).

the chorus of federal courts in the same period that recognized a "finder's exception," permitting a person to be paid for bringing together parties to a transaction without requiring broker registration. *See Kramer*, 778 F. Supp. 2d. at 1336 (collecting cases); *M&A West*, 2005 WL 1514101, at *9; *Salamon v. Teleplus Enterprises, Inc.*, 2008 WL 2277094, *8 (D.N.J. 2008). In fact, the *Kramer* court noted that the SEC has issued a series of no-action letters indicating there was no need for broker registration even though the "finder" received a percentage fee. *Id.* (citing David A. Lipton, 15 Broker–Dealer Regulation § 1:18); *see also Cornhusker*, 2006 WL 2620985, at *6 (noting series of no-action letters recognizing finder's exception). Given the weight of authority that merely acting as a finder does not constitute broker activity, the Feng Parties had no reason to suspect any wrongdoing.

b. The SEC Mischaracterizes The Feng Parties' Interactions With Regional Centers

The SEC goes on to mischaracterize its own Complaint and argue that the Feng Parties were on notice of their broker status because "several promoters refused to send his commissions to U.S.-based bank accounts for fear of violating Section 15(a)(1)." Opp. at 17:10. In fact, the Complaint alleges that "[i]n or about May 2013, some of the [regional centers] informed Feng that they would not wire commissions to United States-based bank accounts as part of an *apparent* effort to avoid running afoul of the broker-dealer registration requirements contained in the federal securities laws." Compl. ¶ 76 (emphasis added). While the SEC attempts to add its gloss to the regional centers' motivations, nowhere in the pleadings does it say that these unidentified regional centers *discussed* with the Feng Parties their purported reasons for sending the money elsewhere. Moreover, as clarified in the Answer, and not disputed in the Complaint, "another regional center that the Feng Parties worked with continued to pay contingency fees based on clients' immigration success to Mr. Feng and Law Office's US based bank accounts."

Answer ¶ 76. Accordingly, there was nothing about the Feng Parties' interactions with the regional centers that would have added any clarity to the existing vagueness of the broker definition in Section 15(a)(1).[13]

Furthermore, while the SEC cites to referral fee agreements between the Feng Parties and regional centers as proof of their broker status, upon closer examination, the content of these agreements suggests the opposite:

> The Partnership [i.e., the investment fund], together with WRCI [the regional center], will provide information ***directly*** to the potential investors. The Finder agrees ***not*** to provide any information other than the information specifically provided by the Partnership to potential investors and that ***only the Partnership and WRCI are authorized to provide information to potential investors***.

SEC RJN Ex. 3, ¶ 3 (emphasis added).

The plain language of the agreement expressly prohibits the Feng Parties from performing broker-like functions. A person in the Feng Parties' position reading

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[13] In a bald attempt to skirt the rules of procedure, the SEC requests judicial notice of portions of Feng's investigative testimony. Opp. at 17 n.6 (citing SEC RJN ¶ S). Once again, the Feng Parties' have concurrently filed objections to the SEC's request for judicial notice of this transcript. As explained more fully therein, the Court should reject the SEC's request outright, since the purported evidence is completely beyond the scope of the pleadings and improper in this Rule 12(c) proceeding. However, in the unlikely event this Court were to consider such evidence (and thereby convert this motion into one for summary judgment), nothing about Feng's testimony is remarkable or relevant. In his testimony, Feng candidly observes the widespread uncertainty in the EB-5 field about whether it was subject to SEC regulation, which is completely consistent with the vagueness of the statute as applied here. At any rate, Feng's subjective thoughts are not relevant to the Court's inquiry because the test for an as-applied challenge is objective. The Court must decide whether a "person of ordinary intelligence" would have a reasonable opportunity to know what is prohibited under the circumstances of the case. *See Rojas-Garcia v. Ashcroft*, 339 F.3d 814, 822 (9th Cir. 2003); c*f. Bouie v. City of Columbia*, 378 U.S. 347, 355 (1964) ("The determination whether a criminal statute provides fair warning of its prohibitions must be made on the basis of the statute itself and the other pertinent law, rather than on the basis of an ad hoc appraisal of the subjective expectations of particular defendants.").

this language would not suspect he was becoming a broker, given that he is promising not to engage in broker-type activity.

c. The SEC's History Of Inaction Perpetuated The Lack Of Fair Notice

Finally, it remains undisputed that until seven months ago, when it filed charges against the Feng Parties (and settlements with other immigration attorneys), the SEC had never – in the history of the EB-5 program – suggested in formal or informal publication, guidance, or rule that immigration attorneys assisting EB-5 clients were acting as brokers. This fact alone serves to validate why the Feng Parties had no reason to suspect they were acting as brokers.

And while the SEC is correct that it may properly proceed to announce a new policy by adjudication rather than by rulemaking, it misleadingly implies that that is what it has done here. But there has been no "adjudication" of the relevant issue. "Adjudication" in the administrative context refers to agency proceedings to formulate a final order, not a judicial proceeding in an Article III court. *See, e.g.*, 5 USC § 1551(7); *Armstead v. U.S. Dept. of Housing and Urban Development*, 825 F. 2d 278, 281 (3d Cir. 1987) ("The Administrative Procedure Act defines 'adjudication' as an 'agency process for the formulation of an order,' 5 U.S.C. § 551(7), and defines 'order' as a 'final disposition ... of any agency in a matter other than rule making.' 5 U.S.C. § 551(6)."). It is undisputed that the SEC did not engage in any prior "adjudication" concerning the application of the broker statute to someone in the position of the Feng Parties.

Nor does the statutory authority to engage in adjudication or rulemaking relieve the SEC of the strictures of Due Process when promulgating new interpretations of statutes. The Fifth Amendment demands that every statute must be applied in a way that gives fair notice of what conduct it proscribes. If the SEC's argument were accepted by the Court, then every vagueness challenge would be defeated with the agency's response that it can devise new rules with impunity

merely by filing a complaint in federal court.[14]

4. The SEC Does Not Dispute The Danger Of Arbitrary Enforcement

The SEC's Opposition completely fails to address the second prong of the void for vagueness standard: whether the vagueness "authorizes or even encourages arbitrary and discriminatory enforcement." *S.E.C. v. Gemstar-TV Guide Int'l, Inc.*, 401 F.3d 1031, 1048 (9th Cir. 2005). The SEC does not dispute that the malleability of the broker definition invites the risk of arbitrary enforcement of the securities laws and does not attempt to explain why the agency has only decided to apply its expansive broker definition to pursue immigration attorneys working in small firms. Accordingly, the Court should construe the SEC's failure to oppose this argument as a concession that it is a valid ground to dismiss the Section 15 claim. *See Hakakha v. CitiMortgage, Inc.*, No. EDCV151320JGBSPX, 2015 WL 4873561, at *8 (C.D. Cal. Aug. 13, 2015) (construing plaintiff's failure to address specific arguments in motion to dismiss as plaintiff's concession that they are valid reasons to dismiss those claims).

B. The Complaint Fails to Satisfy Rule 9(b)

The Ninth Circuit has long interpreted Rule 9(b) to require that allegations of fraud must be "specific enough to give defendants notice of the particular misconduct . . . so that they can defend against the charge and not just deny that they have done anything wrong." *Vess v. Ciba-Geigy Corp. USA*, 317 F.3d 1097, 1106 (9th Cir. 2003). Thus, Rule 9(b) requires a plaintiff to "identify the 'who, what, when, where and how of the misconduct charged,' as well as 'what is false or

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[14] By contrast, where the SEC faced a similar dilemma when it deemed interests in resort and golf condominiums and cooperatives to constitute securities, it issued a guidelines release that set forth clearly demarcated standards as to what developers and real estate brokers could do or promise without being deemed to have sold a security. *See* Securities Act Release No. 5347 (January 4, 1973) ("Guidelines As to the Applicability of the Federal Securities Laws to Offers and Sales of Condominiums or Units In a Real Estate Development").

misleading about [the purportedly fraudulent conduct], and why it is false." *Cafasso, ex rel. United States v. Gen. Dynamics C4 Sys., Inc.*, 637 F.3d 1047, 1055 (9th Cir. 2011). It is uncontroversial that failure to comply with Rule 9(b) can be challenged after an Answer has been filed. *Id.* at 1054-55.

1. The Complaint Fails To Specify Time, Place, and Parties With Particularity

The SEC's Complaint wholly ignores its obligation under Rule 9(b) to articulate who the Feng Parties allegedly defrauded. To be clear, the SEC does not claim that *every* client or regional center was defrauded. *See* Compl. ¶¶ 6-7, 72, 81 (vaguely referring to "dozens of clients," "at least 5 Promoters," "certain Promoters," the "vast majority" of clients, etc.). And it is undisputed that *not a single client or regional center* has asked the Feng Parties to return any fees or other monies ever, even after the public filing of this lawsuit. Thus, it cannot be the case that every client or regional center to whom no disclosure was made is a purported victim of fraud, since at least some (if not all) did not consider the information material. So who were the victims? How can the Feng Parties be prepared to defend this case? Surely the SEC – a government agency with enough resources to investigate for over a year– would not have filed this action unless it had identified some clients and some regional centers who told them that the allegedly undisclosed information was material. Surely the SEC knows to whom it was referring when it alleged in the vaguest possible terms that omissions were made "[i]n communications with *some* of the [regional centers]." Compl. ¶¶ 78-81 (emphasis added). The Court should not allow the SEC to gain unfair advantage over the Feng Parties by failing to disclose that information in the Complaint as required.

Rather than acknowledge its failure to satisfy Rule 9(b), the SEC raises a number of distractions, each of which essentially boils down to "you know what you did and you know who you did it to." That is not how the rules of civil procedure function, especially in a case where fraud is alleged.

Yes, the Feng Parties know who their clients were. And yes, they know with which regional centers those clients dealt. And yes, they can answer broad discovery inquiries which do not require any knowledge of who the *SEC* contends was the victim of fraud. And they can even answer a Complaint which very generally avers fraud by stating that they committed no fraud.[15]

But they have no ability to identify – based on the Complaint – which clients and regional centers will be the subject of the SEC's case-in-chief. This is exactly the kind of uncertainty Rule 9(b) pleading standards seek to avoid when requiring parties to defend against securities fraud allegations. *See Parnes v. Gateway 2000*, 122 F.3d 539, 549 (8th Cir. 1997) (Rule 9(b) particularity requirement serves to, *inter alia*, "ensure[] that a defendant is given sufficient notice of the allegations against him to permit the preparation of an effective defense"); *see also Vess*, 317 F.3d at 1102 (same). Because the SEC's Complaint falls far short of this pleading standard, it must be dismissed.

2. The SEC Fails to Differentiate Allegations Against Feng And His Law Firm

"Rule 9(b) does not allow a complaint to merely lump multiple defendants together but requires plaintiffs to differentiate their allegations when suing more than one defendant ... and inform each defendant separately of the allegations surrounding his alleged participation in the fraud." *Swartz v. KPMG LLP*, 476 F.3d 756, 764-65 (9th Cir. 2007). Thus, in "a fraud suit involving multiple defendants, a plaintiff must, at a minimum, identify the role of each defendant in the alleged fraudulent scheme." *Moore*, 885 F.2d at 541.

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[15] That the Feng Parties could file an Answer is hardly dispositive. *See Cafasso*, 637 F.3d at 1054-55. The ability to deny that the Feng Parties committed securities fraud while acting as immigration counsel to EB-5 clients does not indicate the Feng Parties know which clients or regional centers *the SEC believes* were defrauded, especially given the Complaint's vague language cited above.

Here, the SEC does not dispute that its Complaint fails to distinguish between the conduct of Feng and his Law Office with regard to several allegations. *E.g.*, Compl. ¶¶ 6, 7, 25, 65-66, 72, 78-80. Instead, the SEC attempts to excuse these shortcomings by arguing that (1) Feng and his Law Office are one in the same, and (2) the normal pleading requirements for fraud under Rule 9(b) are "relaxed" when alleging a fraudulent omission rather than a fraudulent act. But both arguments are unavailing.

First, the SEC attempts to use its motion briefing to supplement the deficiencies in its Complaint. Despite its failure to include an alter-ego allegation in the Complaint, the SEC now claims in its Opposition that it "need not differentiate between Feng and his small personal corporation" because "for all intents and purposes, they are one and the same." Opp. at 25. But the law does not permit such amendment by briefing. *See, e.g.*, *Broam v. Bogan*, 320 F.3d 1023, 1026 n. 2 (9th Cir. 2003) (declining to consider opposition papers in ruling on sufficiency of pleadings); *Clayton v. Pepsi Cola Bottling Grp*., No. CV85-5957-WMB, 1987 WL 46230, at *5 (C.D. Cal. Mar. 3, 1987) (same); *Janoe v. Stone*, No. 06CV1511JM, 2008 WL 3931310, at *2 (S.D. Cal. Aug. 19, 2008) ("Plaintiff cannot use his opposition to cure deficiencies in his pleading."). .[16] The SEC's belated "alter ego" assertions in its Opposition do not relieve it of the obligation under Rule 9(b) to "inform each defendant separately of the allegations surrounding [its] alleged participation in the fraud." *Swartz*, 476 F.3d at 764-65.

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[16] The SEC's citation to *Smith v. Jenkins*, 626 F. Supp. 2d 155, 165 (D. Mass. 2009) is inapposite on this point. There, the court stated that plaintiffs had "asserted fraud claims against [a lawyer] and [his] Law Offices based on [an employee's] conduct and the doctrine of *respondeat superior*." The case is not relevant to the issue here, which is that the Complaint fails to identify the alleged speaker with particularity. While in *Smith* it was apparently clear who the alleged speaker was and the legal theory under which the plaintiffs sought to hold the law firm responsible, there is no such clarity here.

Second, that the Complaint rests on a theory of omission does not relieve the SEC of the duty to identify the parties to the alleged omissions with particularity. While the standard may be slightly relaxed as to time and place, "a plaintiff alleging a fraudulent omission or concealment must plead the claim with particularity." *Gomez v. Carmax Auto Superstores California, LLC*, No. 2:14-CV-09019-CAS PL, 2015 WL 350219, at *6 (C.D. Cal. Jan. 22, 2015); *Kearns v. Ford Motor Co.*, 567 F.3d 1120, 1127 (9th Cir. 2009) (contention that nondisclosure claims need not be pleaded with particularity is unavailing). The SEC's reliance on *Republic Property Trust v. Republic Properties Corp.*, 540 F. Supp. 2d 144, 153 (D.D.C. 2008), is misplaced, both because it was subsequently reversed, *Liberty Property Trust v. Republic Properties Corp.*, 577 F.3d 335 (D.C. Cir. 2009), and in any event, it expressly states that "Rule 9(b) requires that the pleader provide the 'who, what, when, where, and how' with respect to the circumstances of the fraud." *Republic Property*, 540 F. Supp. 2d at 153.

Contrary to the SEC's view, *Corral v. Carter's Inc.*, 2014 WL 197782 (E.D. Cal. Jan. 16, 2014), actually reaffirmed that "[t]o satisfy Rule 9(b), a pleading must identify the who, what, when, where, and how of the misconduct charged." *Id.* at *5. The only difference there was that instead of requiring the plaintiff to allege "what is false or misleading about [the purportedly fraudulent] statement, and why it is false," a plaintiff alleging fraudulent omission must "adequately allege why the omitted fact is true, as well as being material to [the victims'] decision-making." *Id.* But regardless of whether the Complaint alleges the Feng Parties committed fraud by act or omission, it must identify the defendant it accuses of acting or failing to act.

Because the SEC fails to allege with particularity who it claims was defrauded, the Feng Parties cannot meaningfully prepare for its defense. The two fraud claims should therefore be dismissed.

IV

CONCLUSION

The Feng Parties respectfully request that the Court dismiss the Complaint in its entirety, and enter judgment as to the section 15(a) claim in favor of the Feng Parties and against the SEC.

DATED: July 12, 2016

Ariel A. Neuman
David H. Chao
Ashley D. Bowman
Bird, Marella, Boxer, Wolpert, Nessim, Drooks, Lincenberg & Rhow, P.C.

By: /s/ Ariel A. Neuman
Ariel A. Neuman
Attorneys for Defendants Hui Feng and Law Offices of Feng & Associates P.C.

Responses, Replies and Other Motion Related Documents

2:15-cv-09420-CBM-SS
Securities and Exchange
Commission v. Hui Feng et al

ACCO,(SSx),DISCOVERY

UNITED STATES DISTRICT COURT for the CENTRAL DISTRICT OF CALIFORNIA

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Ariel A Neuman aan@birdmarella.com, aneuman@birdmarella.com, brl@birdmarella.com, rec@birdmarella.com

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Donald W Searles searlesd@sec.gov, berryj@sec.gov, irwinma@sec.gov, LAROFiling@sec.gov

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