



Real Estate Projects – Still the Darling of EB-5

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As of December 2013, 439 EB-5 regional centers are registered with US Citizenship and Immigration Services (USCIS). EB-5 is a job creation program and yet to many EB-5 investors, it is hardly surprising that the majority of the EB-5 projects on the market focus on real estate development. Why do the real estate development projects remain among the most popular EB-5 projects? This article examines the reasons of its popularity, noticeable legal nuances and the recent trends in EB-5 real estate projects.

Why Choose Real Estate as an EB-5 Investment?

Real estate in general is a tangible investment. Compared to other tangible investment such as manufacturing or intangible investments such as stocks and bonds, with real estate projects there is less likelihood of fraudulent activities. Investors can physically inspect real estate property; obtain background checks of the developers, sellers and brokers; obtain an appraisal of the property, etc. Using leverage or debt in real estate can be structured more safely than using debt to buy stocks by trading. Real estate investments have traditionally been a good inflation hedge to protect against a loss in the purchasing power of the dollar. From the investors' point of view, real estate EB-5 projects have tangible collaterals – the land and the property.

How EB-5 Financing Become Popular in the Real Estate Industry?

Few would dispute that 2008 and 2009 were historically catastrophic years for real estate development in general, for hotel development in particular. According to the statistics



from HVS Global¹, the hotel performing metrics such as the demand, occupancy, Average Daily Rate (ADR) and Revenue Per Available Room (Rev PAR) not only ceased growing, the growth rate of 2009 in the said performing metrics became negative. It became extremely difficult to obtain financing from conventional means, construction loans notably being the first victims.

At the same time around 2008 and 2009, the EB-5 rules regarding real estate construction jobs changed to facilitate the infusion of EB-5 funding into the real estate industry. On December 10, 2008 Senator John Cornyn (R-TX) voiced this reasonable concern in his letter to USCIS. In his letter, the Senator requested USCIS to publish its “views on the job creation requirement as it applies to Regional Centers generally and the construction industry specifically”². On January 16, 2009, under pressure from stakeholders such as regional centers and EB-5 Practitioners USCIS released a policy memo directed at construction jobs: “Indirect and induced jobs created as a result of construction jobs whether counted or not may be included in the job count. Even when the construction jobs may not be counted towards the [direct] job creation requirement, they do have indirect and induced impacts that are eligible to be included in the final job count because they are ‘continuous, permanent employment’.”³

The letter and subsequent USCIS memorandums cleared the legal obstacles regarding construction jobs for large scale real estate projects to access EB-5 financing. The authors witnessed how regional centers not only in New York but all across the country have substantially benefited from the EB-5 financing since the construction job rules has changed.

¹ HVS and STR Hotel Valuation Index:
<http://www.hvs.com/staticcontent/file/TrendsInTheInternationalHospitalityIndustry.pdf>

² Letter to Senator John Cornyn from USCIS offices File No. CO703.2342, Re: Job Creation Requirement for Immigrant Investor (January 16, 2009), P.1, Para. 1.

³ Id. P.1, Para. 4.



Why Use EB-5 in Real Estate Financing?

EB-5 program serves as a fantastic alternative financing mechanism for real estate developers. It can be structured as a short-term low-interest non-secured loan, which is non-delusive to the property owner's equity. The May 30, 2013 Policy Memorandum has allowed the timing of EB-5 funding to be flexible. It allows a project to receive credit for the job creation, even after the construction has commenced and the EB-5 capital is received to replace the interim or bridge financing. The policy memorandum now allows the EB-5 financing to be used even if the EB-5 financing is not contemplated prior to the acquiring the temporary bridge financing.

Even with the recovery of the market, a real estate developer can save millions of dollars using EB-5 funds as opposed to conventional financing. EB-5 investors have shown a preference for real estate projects, mainly because of the collateral value and the ease of the return on investment in contrast to manufacturing projects, which do not have the same asset value and may not have the ability to repay the investor in five (5) years.

In the 439 regional centers currently approved, at least 20% have been approved within the past four months. Most recently approved regional centers are real estate related and some covers multiple states in geographic areas. The authors believe the radical increase in the number of approved regional centers is due to the new rule implemented by the May 30, 2013 Policy Memorandum allowing for the "hypothetical" project. If a proposed regional center applies for designation with "hypothetical" projects, general proposals and general predictions may be sufficient to determine that the proposed regional center will more likely than not promote economic growth, improved regional productivity, job creation, and increased domestic capital investment.

Recent Trends in EB-5 Real Estate Projects

While real estate projects span the whole country, certain areas such as New York City have taken the lead in successful real estate projects. Applicable marketing plays an enormous role, however developers and practitioners must take heed from past disasters. A Chicago Convention Center (ACCC) project significantly slowed down the market in China and other



countries for some time. Investors have become more cautious about projects that associate themselves with government officials and politicians. The EB-5 market has evolved after the ACCC fiasco, investors and marketing agents have become savvier about conducting due diligence before making their investment decisions, unfortunately similar type of misrepresentations are still prevalent in the industry.

Despite the securities fraud charges against the ACCC by the Securities and Exchange Commission (SEC), the authors noticed that further to several large scale marketing promotion events recently held in China, marketing material contained misleading information, misrepresenting facts to the investors. For example, the governor and Department of Commerce in the State of Washington made presentations to promote a Seattle based project in front of hundreds of EB-5 investors in major cities in China. Predictably the marketing materials in Chinese have misrepresented the project as “government verified and guaranteed”.

Another New York hotel project invited a former governor to attend the marketing promotions in China. Sources confirmed misrepresentations on the Chinese marketing material, including confusing “Long Island”, the affluent New York City suburb with “Long Island City”, a newly developed neighborhood in Queens, New York.

According to the Securities Act of 1934 Section 10(b)(5) the anti-fraud provision and the Supreme Court interpretation of the “misrepresentation” in connection with the purchase or sale of a security has three layers of seriousness: intentional false statement, reckless material misrepresentation and omission of material information. Developers and practitioners are cautioned to verify that foreign marketing material is not misleading.

The overseas investors’ logic for government associated EB-5 projects is that if a government official agrees to openly promote an “at risk” investment, there must be some merit in the project. At least it should not be fraudulent. The ACCC case proved this logic to be wrong. Politicians are not held responsible for making such an association with a fraudulent project. The Chicago Tribune revealed that Illinois Governor Pat Quinn openly stated at an EB-5 promotional event in Beijing, China that: “We know how to make



convention centers”⁴. Despite the lofty promises made by Quinn, the project collapsed, the investors lost time and money⁵.

For New York City based developers, it is noted that the Mayor-elect de Blasio who will take office in January 2014 has taken a drastically different view on real estate development than Mayor Bloomberg. Bloomberg is known for changing the New York City landscape with high-density and high-quality designed projects serving wealthy owners and investors and granting tax exemption and government funding. 40% of the city has been rezoned during Bloomberg’s 12 years in office. De Blasio’s view is that the administration should review every NYC project “with an eye towards maximizing affordable housing, good jobs and value for the taxpayers.” According to the New York Times⁶, the new mayor, an advocate for affordable housing could make it difficult for developers of luxury retail malls or high-end residential apartments “by slowing approvals of construction permits or delaying the use of government funds”.

Using EB-5 Funds to Purchase Real Estate

Can EB-5 funds be used to purchase real estate? Yes and No. USCIS has clarified⁷ that it is not prohibited to use EB-5 funds to acquire real estate; however, it is not generally reasonable to treat EB-5 funds spent on real estate acquisition as inputs to an employment econometric impact model.

⁴ Hotel proposal illustrates promise and peril of investment program, Chicago Tribune, July 15, 2012 http://articles.chicagotribune.com/2012-07-15/news/ct-met-china-investment-visas-sethi-sidebar-20120715_1_eb-5-hotel-proposal-foreign-investors

⁵ U.S. Securities and Exchange Commission, Litigation Release No. 22615, February 8, 2013: \$145 million was raised in securities and \$11 million in administrative fee. As of December 2013, the \$145 million held in escrow account are returned to the investors; the \$11 million is misappropriated.

⁶ Going out with Building Boom, Major pushes Billions in Projects, New York Times, December 15, 2013, http://www.nytimes.com/2013/12/16/nyregion/going-out-with-building-boom-mayor-pushes-billions-in-projects.html?partner=rss&emc=rss&utm_medium=referral&utm_source=pulsenews&r=0

⁷ USCIS Stakeholder Meeting held on the July 03, 2012. <http://www.uscis.gov/news/questions-and-answers/questions-and-answers-eb-5-economic-methodologies>



The requirement of Matter of Izummi, 22 I & N Dec. 169 (Comm'r 1998), that the “full amount of money must be made available to the business(es) most closely responsible for creating the employment upon which the petition is based.” For example, a job-creating enterprise may propose to allocate some EB-5 funds to purchasing land and allocate other EB-5 funds to developing and operating a business on the purchased land, and the jobs created by the enterprise can be apportioned among all the EB-5 investors. Where some EB-5 funds will be used for real estate acquisition, though not prohibited, such apportionment should be detailed in the business plan.

From an investor’s point of view, the investors cannot obtain permanent residence through making a passive investment in the real estate market in the US because the investment capital must be placed “at risk” and the capital must be used to create jobs.

Tenant Occupancy

Real Estate projects have grown in complexity in terms of job creation and capital stack. Issues such as “tenant occupancy” have constantly occurred for mix-used, renovation and newly built real estate projects. In a recently issued RFE, the USCIS requires the project to prove that “the construction project will be attracting a tenant from within the region who was not able to operate prior to the commercial construction project or attracting new tenants from another geographical region.” The following evidence should be provided to overcome the obstacles that the tenant jobs are “new” jobs rather than “merely relocated” jobs.

- A description of the projects and services to be provided;
- A detailed market analysis and a marketing plan which provides support of new tenant occupancy in the region
- The current size of the market
- Historic trends and developing trends and projected growth rate
- The target market and number of purchase
- Low vacancy rates of commercial space within the region
- A lack of suitable commercial space that the new tenants are expected to lease



- A detailed letter from state or local government official to evidence the availability of suitable space or the lack thereof

This is not an exhaustive list. The EB-5 job creation has become more complicated to prove in real estate industry. USCIS does give the projects the option to remove the tenant jobs all together.

Debt, Equity and Preferred Equity

The two common financing model used by EB-5 real estate projects are loan models and equity loans. The former structures the EB-5 financing as a short-term loan, which will be returned to the investors upon the adjudication of their permanent residence. The latter structures the EB-5 funding as equity investment. The investors hold long-term common shares in the project and receive dividends payment based on their equity ownership in the new commercial enterprise.

Some projects have structured the EB-5 financing as “preferred equity”. It is a class of ownership in a corporation that has a higher claim on the assets and earnings than common stock. Preferred stock generally has a dividend that must be paid out before dividends to common stockholders and the preferred equity holders usually do not have voting rights. It is as a financial instrument that has characteristics of both debt (fixed dividends) and equity (potential appreciation). The preferred equity model needs to be carefully structured by experienced EB-5 attorneys or else it may appear to be a redemption agreement, which is explicitly prohibited under the EB-5 rules. Authors have seen several Requests of Evidence (RFE) and Notices of Intent to Deny (NOID) relating to the preferred equity model.

In Conclusion:

In the past five years, the number of EB-5 real estate projects has tripled. It is not surprising that the most successful and the biggest failure of the EB-5 projects are all in the real estate industry. It provides the attractive opportunities to developers for inexpensive financing and creates additional legal nuances in the EB-5 adjudication. It only takes a fraudulent project to ruin it for all the other fair players. Ironically the market has short



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memories. The industry calls for the good conscious of the practitioners to maintain the order and integrity.

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Mona Shah, Esq. is the principal of Mona Shah & Associates in New York City. The firm has assisted many Regional Centers and Investors in navigating this complex, nuanced and constantly changing area of immigration law. Mona has more than 18 years of legal experience in immigration law and extensive knowledge in EB-5 law. Mona's substantial litigation background includes her representation of clients in both state and federal courts. She has handled complex immigration law appeals before the US Circuit Courts of Appeal nationwide. Before coming to the US, Mona was a crown prosecutor in the UK. Mona has authored and published numerous articles and has spoken extensively both in the US and overseas.

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