

## **EB-5 Program Status – Observations on China’s Project Activity**

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Posted by **Arnstein & Lehr LLP**



### **Ronald R. Fieldstone**

#### ***Summary of Conference and Business to Beijing, China***

As a follow-up to my recent March 2015 trip to China, I have several observations concerning the status of the EB-5 program and, in particular, the reaction in China with respect to same.

The good news is that the market in China still seems very robust, even with retrogression estimated to take place in May or June. There seems to be a tremendous demand for the EB-5 green card program, notwithstanding the fact that the Chinese nationals are also migrating to other countries around the world that have a much easier entry policy than the United States.

After meeting with many agents, it is apparent that there are too many projects on the market. The projects that have a major developer track record are at a significant advantage in garnering EB-5 funding as compared to smaller projects with less known developers.

#### **Types of Investor Agents and Their Methodology**

It was very interesting to discuss with the agents their methodologies of obtaining investors and how they work internally. There are various classes of agents which could be summarized as follows:

1. The major agents that do everything internally although they sometimes cooperate with other agents.
2. Wholesalers that do not necessarily sell to investors but deal with sub-agents to raise capital and, in return, split the administrative fee and the back-end fees that may be earned.
3. Some agents do both. They work as a wholesaler and bring in other agents and at the same time directly deal with investors in order to cover both ends of the market.
4. Various small agents that work directly with investors and will only handle transactions of typically 20-25 investors or less, since they have limited capacity.

It is noteworthy that the Chinese regulation of the migration agents and their registration and banking requirements may be terminating. Therefore, marketing agents may no longer have to be registered.

With respect to pricing, it seems consistent that the investors typically receive 0.5% interest per year and pay administrative fees of around \$50,000. Agents seem to be receiving most of the administrative fee and only allotting a small percentage to regional centers. Likewise, agents charge on the back-end interest somewhere around 2% to 4.5% per year on the amount of capital funded. If the project is very large or riskier, that rate may go up. Furthermore, with respect to direct programs, the rate should even be much higher given the perceived risk, especially if a non-real estate project is involved.

### **Most Important Project Characteristics**

From a diligence standpoint, the agents consistently look to projects that have the following characteristics.

- (1) It is preferable that the project be located in “bigger cities” such as New York, Los Angeles and San Francisco. Other major cities are also desirable, such as Las Vegas, large cities in Florida, Houston, Dallas, the Washington D.C. area and, to some extent, Chicago. It is noteworthy that some agents will not do business in Chicago, given the taint of the Chicago Convention Center project.
- (2) There is a preference for well established developers who have a very significant track record in order to provide assurances that the project will be finished and operated successfully.
- (3) There is a preference given to projects that are under construction or just beginning construction to take away the risk that construction will not be commenced.
- (4) For certain agents, the percentage of EB-5 money should not be too large as compared to the entire total capital stack.
- (5) There is a preference for at least a 30% job cushion.
- (6) Much more preferable to have a prior exemplar approval, either from a 526 petition approval or a 924 exemplar approval. Otherwise, agents like to see a sufficient amount of funds in escrow and a developer guarantee of refund that is supportable by appropriate financial verification.
- (7) Agents are still not as positive on direct programs, although a few agents are actively marketing direct programs as a specialized practice.
- (8) Agents prefer a brand name with respect to real estate projects and, in particular, with respect to hotels, the names of the operators and even the names of the other members of the project team (G.C., architect, engineer), the names of the companies doing the approvals and/or feasibility reports, as well as the professionals involved with the project.

It is noteworthy that both the agents and the investors constantly Google and do other web searches on all parties involved in a transaction, and in particular, the developer and its principals. One should never underestimate the degree of due diligence taken by these parties.

### **EB-5 Beijing Summit – Conference Highlights**

At the Summit Conference in Beijing on March 21, 2015, there was a lot of good information provided at the sessions I attended that can be summarized as follows:

- (1) Retrogression is still a major issue and apparently the old 21 years old rule is now 18? Children are now becoming the applicant so that they will not age out and have better protection due to retrogression.
- (2) How to deal with the early payback of a loan prior to 829 approval. Given the fact that retrogression is inevitable and it will become more significant over time, which in turn will delay the ability to obtain the EB-5 visa approval and 829 petition approval, approval within a five-year timeframe is probably unrealistic. Accordingly, the industry needs to deal with the reality that developers will not want to be in a position to have funds available and not be able to pay back the loan at scheduled maturity, and then have to continue to pay interest on the loan. Accordingly, there were discussions involving whether the loan could be paid back to the new commercial enterprise (“NCE”) who in turn would reinvest the money or even hold it in escrow until the 829 petition is approved as to each applicable investor. Another option is to have the funds relent to the developer for another project that does not necessarily have to create jobs. It is my understanding that USCIS has not provided any guidance on this issue and, therefore, this is one of the open areas that will ultimately be addressed in the near future.
- (3) Concern over the quality of translations, which could be an issue with respect to the 526 petition and supporting documentation, as well as the offering and related documents themselves.
- (4) It became apparent that USCIS is no longer requiring proof of funding verification for the administration fee, which is logical since it would seem that USCIS really has no reason to address same.
- (5) Some of the immigration attorneys noted that certain projects either had exemplar approval or had 526 approval and, thereafter, USCIS is then asking for additional information on future applications due to some degree of time delay that may have occurred.
- (6) There were detailed discussions about SEC enforcement with respect to broker-dealer registration issues and registered investor advisor issues. Offshore agents seem to have little concern about broker-dealer issues since virtually all of them only conduct operations offshore and are, therefore, not really concerned about the SEC regulation with respect to their selling activities. However, it was made very clear to everyone in attendance the fact that the sales activities may be exempt from registration, but this does not exempt compliance with the 1933 Act and all disclosure obligations related thereto since the EB-5 program still involves the issuance of a U.S. security.
- (7) Discussion of F-1 student to applicant which is becoming more common, and the utilization of a power of attorney to potentially avoid broker-dealer registration issues where the child is in the United States and provides the parent the power-of-attorney to sign certain documents on behalf of the child when the parent is gifting the money to the child and making the investment decision independent of the child.
- (8) General discussion about “Izumi” and guarantees of repayment. There was consensus that virtually any form of loan guarantee should be acceptable, including governmental agency guarantees. However, it was made clear that there would never be a direct guarantee to the investor of a return of capital.

(9) Escrowing. It is apparent that the escrowing of EB-5 funds has become far more complicated given the numerous variations involved in dealing with the escrow arrangement and the financial institution and their administrator, who is generally NES Financial Services. It is also noteworthy that some very significant financial institutions have left the EB-5 escrow market due to the concern over adverse publicity if a deal defaults, rather than concern over actual liability for serving as an escrow agent. There was a detailed discussion of all the escrow arrangement variations, taking into account the discussion points set forth above.

(10) A general discussion of the extension of the EB-5 Program and whether the EB-5 Program will be extended under its current format. There was a general consensus that the EB-5 Program will be extended, and the majority of the participants believe that the extension will be without change although there were discussions about increasing the visa count as well as increasing the investment threshold to qualify for TEA designation.

(11) Retrogression Backlog. As time goes on, the retrogression issue will become more and more pronounced for Chinese nationals as the building increases.

(12) There was a discussion as to the inconsistency of the time period to obtain 526 approvals. It was noted that some regional centers/applicants were receiving approval in as early as 6 or 7 months, and others were taking longer than the average time of 14 months.

(13) United States Income and State Tax Concern. It has become apparent that the Chinese nationals and the agents are now much more concerned about United States tax exposure. Pre-immigration tax planning should commence after I-526 petition approval has been received and prior to migrating to the United States. It is noteworthy that there is a very favorable United States/China treaty, allowing a Chinese national to spend up to 6 months per calendar year in the United States, without having to become a U.S. taxpayer. There were also discussions as to pre-immigration tax planning and the various strategies that should be utilized. I think agents are becoming far more sensitized that they should be advising their clients on a more active basis. However, some applicants are not that wealthy, and the tax planning may not be that significant to them.

