

Financing Construction Projects Using the EB-5 Program

Stephen Sewalk, PhD/JD, Assistant Professor
Yulin Wang, MS ACCT, Graduate Research Associate
Katelin Knox, JD/LLM, Graduate Research Associate
Yu Fang, MS FNCE, Graduate Research Assistant
Burns School of Real Estate and Construction Management
Daniels College of Business
University of Denver
Denver, Colorado

Starting with the 2008 recession, many construction projects have stalled or been cancelled due to a lack of financing. Banks have become risk adverse and equity investors, wanting to ensure that their investments pay-off, have demanded high rates of return on construction projects. Even as the economy recovers slowly, funding for projects remains difficult to find. Due to the lack of construction financing since the financial crisis in 2008 funding available through EB-5 visas caught the attention of construction projects and in particular small hotel developers and demand for this type of funding has been increasing.

The US government under present rules sets aside up to 10,000 EB-5 immigrant green cards each year. Of these 3,000 are reserved for foreign nationals who invest through a pre-approved Regional Center designated by USCIS based on proposals for promoting economic growth. Congress created the Immigrant Investor Program (EB-5) in 1990 to stimulate the U.S. economy through job creation and capital investment by foreign investors.

This source of funding is important to construction developers and can make the difference between projects getting funding and succeeding or remaining on the sidelines. In this paper we present EB-5 funding, discuss how to structure a project and show the value to constructors of using this type of funding.

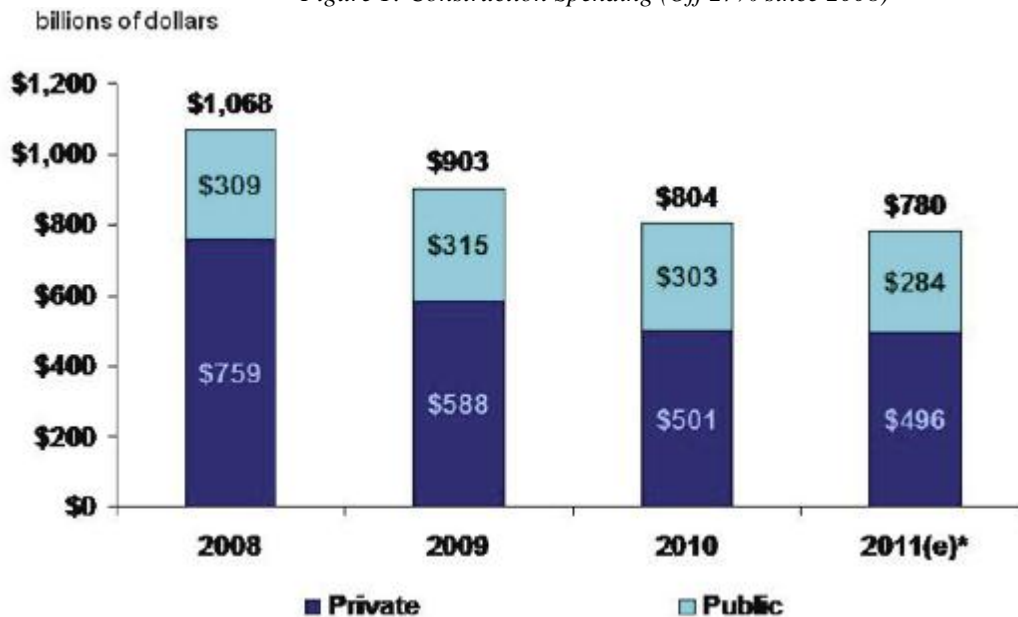
More importantly by understanding the types of projects that can attract EB-5 investors and structuring those to ensure both project and investor success, a development project can more rapidly garner funds once the decision has been made to move forward.

Key Words: Finance, Construction, EB-5 Green Cards, Immigration, Construction Financing

Introduction

The construction industry is a very volatile sector of the US economy, very dependent on valuations and capital. Since 2008, spending on construction has declined by approximately 27% or \$300 billion. However, private sector spending declined by almost one-third compared to a decline in the public sector of 10 percent (AIA, 2011).

Figure 1: Construction Spending (Off 27% since 2008)



Sources: US Dept of Commerce Construction Spending Put-in-Place and AIA

For construction projects of all types (apartments, hotels, restaurants, shopping centers, malls, and infrastructure among others), need funding. Funding for a project comes in the form of debt and equity. Most developers and owners seek an optimal mix of debt and equity financing that minimizes their costs while providing solid and viable returns. It is common within the industry that banks and lenders will require 10-25% equity in order to provide the debt financing. This allows a developer to seek a long to value (LTV) commercial construction loan between 75-90% of the value of the development.

Interest rates on debt start around 6 percent per year, with some riskier forms of financing reaching 10 percent or higher (Butler, 2012). This can be quite expensive and therefore risky to the developer and to those putting equity into the project. This risk factor means that developers would prefer cheaper financing increase the odds that their project succeeds.

Project Financing and the EB-5 Program

The US Congress created The Immigrant Investor Program (EB-5) in 1990 to stimulate the U.S. economy by encouraging foreign investors to invest capital (green card incentive) creating jobs in the process. The U.S. Citizenship and Immigration Services or USCIS administer the EB-5 program (Ivener & Fullmer, 2009).

Although 10,000 EB-5 visas are available every year, so far the available allocation has never been entirely used (Kalmykov, 2012). The popularity of the program has increased, in 2006 502 green cards were issued; however, by 2011 this had increased to 3,463 green cards, a compound annual growth rate of 47%. Assuming this rate of growth continues, it is possible that within 3-4 years there will be more immigrants seeking the EB-5 immigration route than green cards available (Kalmykov, 2012).

Because of the increasing demand for EB-5's now is a perfect time for construction firms, developers and investors to seek this type of funding. In this paper, we examine the structure of the EB-5 program, how the EB-5 program can assist the construction industry and how it is used, and discuss a real project as an example of the EB-5 program structure. Furthermore, it should be noted that hotel developers can raise money through the EB-5 program by offering returns of less than 4 percent, the EB-5 program has proved to be a relatively cheap source of financing (Wing, 2011). Investors who take an equity stake in a hotel project aim for returns of up to 20 percent (Morrissey, 2012).

EB-5 Program Structure

The EB-5 program requires that a principal (investor) invest a minimum of \$500,000 in a new or \$1 million in an existing commercial business respectively within the USA. Further, this investment needs to create or maintain a minimum of 10 jobs (direct and/or indirect) for a minimum of two years for each investor seeking to qualify for permanent residency (green card) (OECD, 2010).

The amount of capital invested depends on the economic status of the location of the business. If the investment is in a Targeted Economic Area (TEA) defined by law as “a rural area or an area that has experienced high unemployment of at least 150 percent of the national average”, investors may elect to invest as little as \$500,000. However, these special areas can be designed so by the mayor of any U.S. city (OECD, 2010).

The Basic Program and the Regional Center Pilot Program are two methods available for a foreign investor to utilize the EB-5 to gain a green card for permanent residency for himself and his immediate family.

The regional center can be public or private and acts as an economic unit to accelerate the EB-5 program aiming to help foreign investors obtain EB-5 visas. A Regional Center acts like a loan origination shop (USCIS, 2012). Developers are able to submit their projects to the Regional Center to indicate that they are seeking EB-5 Capital for their project. Regional Centers will review the projects and issue non-binding letters of intent that outline the terms on which a construction loan can be made utilizing the EB-5 program. The waiting time for EB-5 funding may take approximately 7 to 9 months. The EB-5 financing is available to any project, even ones that banks will not consider lending to, as long as the project can properly verify that jobs (direct and indirect) are created with the investments (McNeill, 2012).

EB-5 regional centers play an especially important role in raising EB-5 financing for new hotel development, and there has been some concern among investors and project developers that the federal regulations authorizing EB-5 regional centers were set to expire on September 30, 2012. However, on September 17, the U.S. House of Representatives passed S. 3245 (412-3) including a three-year re-authorization of the EB-5 Regional Center Program through September 2015 (Rubocki & Purcell, 2012).

Profile of EB-5 Investors

While anyone from around the world is eligible to apply to come to the US with an EB-5 the overwhelming recent majority of new investors, come from China. South Korea provided the highest number of EB-5 investors in FY 2008 (48%) as shown in Figure 2; however, since then Chinese investors have been held the first position 46% of the total in 2009, 41% in 2010, 70% in 2011 and 80% in 2012.

Figure 2: Nationality (Country) and Numbers of EB-5 Investors FY 2008 - 2012

Nationality / Country of Origin	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012					
					C5	T5	I5	R5	Total	
China	360	1,979	772	2,408	90	108	5,923	3	6,124	80%
South Korea	693	873	295	254	9	13	425	-	447	6%
Taiwan (Chinese)	-	-	-	117	3	4	141	-	148	2%
Venezuela	47	170	94	122	-	7	102	-	109	1%
Iran	24	85	62	-	2	2	77	-	81	1%
Top 5 Countries	1,124	3,107	1,223	2,901	104	134	6,668	3	6,909	
% of Total	78%	74%	65%	84%	65%	82%	91%	50%	90%	
Total For All Countries	1,443	4,218	1,885	3,463	159	164	7,312	6	7,641	

Source: US Department of State (January 2013)

Of importance to these investors is that their project results in real jobs that allow them to stay in the US. While the limit of 10,000 investors per year has yet to be reached, it is presently anticipated to be reached in 2014 or 2015.

Calculating Jobs using the EB-5 Program

In addition to the investment, the new commercial enterprise must create or preserve 10 full-time jobs within two years of the immigrant investor's admission to the United States as a Conditional Permanent Resident. These jobs may be direct or indirect. Ensuring that sufficient jobs created is crucial to determining the result of the investment concerning the success of the project as well as the success of the immigrant seeking a green card.

There are two job classifications, direct and indirect. United States Citizenship and Immigration Service (USCIS) identifies a "direct" to mean a job at the commercial enterprise level, one that is an identifiable job verified by payroll records and subject to Section 8 CFR requirements and establishes an employer-employee relationship between the commercial enterprise and the people employed (USCIS, 2012). USCIS identifies an "indirect" to indicate a job at the project

level; these are multiplier-effect type jobs, and are calculated using the regional centers RIMS II or IMPLAN economic models. These calculations determine the estimated number of indirect jobs created through investments in the regional center's investment projects (USCIS, 2012). The RIMS plan is the Regional/Output Modeling System provided by the Bureau of Economic Analysis to calculate multiplier effects at the county level. Moreover, IMPLAN or Impact Analysis for Planning provides multiplier effects to the zip code level (Alward, MIG, 2011).

Accountability and the EB-5 Program

Unlike traditional funding, there is more at risk for EB-5 investors. Traditional equity investment requires a high rate of return. An investor using the EB-5 program is less interested in a high return, but rather seeks to ideally get their money returned, possibly with a small amount of interest, but more importantly wants the project to succeed to ensure that they receive their green card and can immigrate to the USA to start a new life.

The foreign investor faces substantial risk, as they must trust an investment company to invest a large sum of money (life savings) in order to be able to obtain legal permanent residency after the 2-year probationary period. The investment needs to fund a project (or new enterprise) that must either create a minimum of 10 new jobs or maintain 10 jobs (troubled industry) for each equity investor. Furthermore, a foreign investor may not be familiar with US laws and therefore faces additional costs associated with their investment. These include the \$1,500 application fee for the I-526 (not including attorneys or other fees). A regional center may charge upwards of \$30,000 to \$50,000 to match an investor to a project. Assuming the project is a success it will then be necessary to remove the conditional status on the residency by filing form I-829 at a cost of \$3,835 per applicant. Because of these additional costs, the total cost to the applicant can easily exceed \$50,000 in excess of the investment made. Concerning the investment, this assumes that the project does not experience cost overruns or schedule delays that may influence job creation and/or calculations requiring additional funds or potentially limiting the number of green cards.

Most of the EB-5 investors invest through regional centers, and there is no two-year job creation rule in the regulations. The regulations only require evidence that the direct or indirect employment will be created by the investment (8CFR§204.6(j)(4)(ii)), with no specific time frame provided.¹ Further, regulation 8CFR§204.6(m) only states that the regional center describe how the investment will promote economic growth through job creation and how indicate how jobs will be created, again with no specific time period. The only time period within the regulations that applies to investors through regional center investors is 8CFR§216.6(c)(1)(iv)23 that jobs be created "within a reasonable time" following the approval of the condition removal.²

¹ The requirement of "qualifying employees," which appears in 8CFR§204.6(j)(4)(i) relating to direct EB-5s does not appear in 8CFR§204.6(j)(4)(iii) relating to regional centers because it is completely inapplicable to indirect and induced jobs.

² Supra note 20.

Projects and EB-5 Funding

It is important to understand how to analyze a project for EB-5 funding because although EB-5 funding could in theory be used on any project, the key factor is the creation of jobs, many of which are indirect and induced. A construction project that lasted more than 24 months and had consistent employment in the construction sector, with employees working long-term at least 35 hours per week would allow construction jobs to be included.

There are several different types of construction projects, here we examine four broad sectors: 1) Residential, 2) Commercial, 3) Industrial, and 4) Infrastructure.

Residential

A single residence would not constitute a suitable investment for EB-5. A very large residential development that is built over multiple years and involves the construction of the equivalent of several homes per month could potentially qualify if it creates full time jobs. However, for this to qualify for EB-5 funding each investor into the development would need to create 10 jobs. While potentially challenging, it would be possible to develop a plan that would build out sufficient homes continuously to qualify. However, the development would have to be sufficiently large to support continued development over several years (as well as demand for the homes).

Commercial (Non-Hotel, Non-Shopping Center)

Commercial buildings could include apartment, office, and high rise mixed-use buildings. Unless the development is quite large, the majority of commercial buildings are constructed in a period of 14-22 months. Very few permanent jobs are created in an apartment building in comparison to the cost of the building. With regards to office and mixed-use high rise buildings the jobs created are few compared to the cost of the building, limiting the number of potential investors and therefore the interest for EB-5 purposes.

Commercial (Hotel, Shopping Center/Mall, Resorts, Cruise Ships)

Commercial buildings that include hotels, shopping centers/malls, resorts, and even cruise ships have a tendency to create a significant number of long-term jobs. An increasing number of hotels are finding EB-5 financing. A large multi-use shopping center complex would also fit well with EB-5 financing. Buildings and structures that fit into the tourism and travel industries would seem to be a natural for EB-5 funding given the large number of jobs created.

Industrial

Industrial projects would also prove challenging with EB-5 funding, especially high-tech that employ few people. However, a project that funds a start-up, i.e. e-commerce that requires hiring significant numbers of sales people could qualify. While typically funded by venture capitalists (VCs), it is technically possible for EB-5 investors to fund a VC that invests in these types of opportunities. However, the objective of EB-5 investors is to invest in a safe secure project guaranteed to create jobs resulting in them acquiring their permanent residency. This is why construction projects are preferred.

Infrastructure (Highways, Roads, Bridges, Toll Roads)

Roads, while costly, produce few long-term jobs. Even toll roads produce few jobs relative to the significant investment required to build them.

Infrastructure (Pipelines, Energy Projects)

Very large infrastructure projects could potentially qualify based on the number of jobs created and the length of employment. As an example, a long-term commitment to build large pipelines or multiple power plants that hire 1000s over multiple years would qualify if the funding commitment from EB-5 investors were in the \$500k to \$1 million investment for every 10 jobs created directly, indirectly and induced. Projects requiring more funding per investor would eliminate many potential investors.

To examine this issue in more detail, we examine the Atlantic Yards Project, as this project combines a basketball arena, 16 high-rise buildings and retail space built over multiple years.

Case Study: The Atlantic Yards Project

The Atlantic Yards Project consists of the Barclays Center basketball arena and 16 high-rise buildings in Brooklyn. According to Joe DePlasco, a spokesman for Forest City Ratner Cos., developer of Atlantic Yards, the project is using \$228 million of EB-5 money for the \$1.4 billion project. This includes the arena, infrastructure and high-rise buildings. The arena will have a new subway entrance, parking facilities, municipal water and sewer line upgrades as well as 6,430 housing units and 247,000 square feet of retail space (Oder, 2012).

The EB-5 funding is coming from 456 foreigners through the New York City Regional Center. Because there are 456 individual applications, this implies that there needs to be a minimum of 10 jobs created per investor, or a minimum of 4,560 jobs generated for a two-year period.

To win green cards, the foreigners' \$228 million has to generate 4,560 jobs within two years of their investments. Forest City likely will pay 4% to 5% interest rate, as with other New York City Regional Center projects promoted by the city, while the majority of the investors, from China, will get no interest, and the 40 or so Korean investors will get 0.25% (Order, 2011).

Figure 3: The Atlantic Yard Project

Total project cost: \$ 1.448 billion		Number of EB-5 investors: 456
EB-5 financing: \$ 249 million		Number of jobs required to be created: 4560
% of EB-5 investment in total project cost: 17%		Total estimated number of jobs created: 7696
Government involvement:	New York state appropriation: \$100 million	Government funds: \$ 742 million
	New York city appropriation: \$131 million	
	New York state bonds: \$511 million	

An Example: Calculating 'Jobs Created'

The construction of the entire project creates jobs in two ways aside from the construction jobs. Note that the construction jobs typically do not count because these are viewed as part-time jobs as they typically do not last more than 2 years. For a very large project built over a long-time frame it is possible to count construction jobs as long as workers work more than 35 hours per week. Therefore, EB-5 focuses on two types of jobs that are created. The first are the support jobs created due to the construction, such as providing services and materials to the construction site and to all of the construction workers. The second being full-time jobs created by the business or project itself.

The retail shopping center of 247,000 square feet creates jobs in two ways. While construction costs for a building vary by type and location, we will make some simplifying assumptions. For this example, assume that actual "hard" costs of construction are \$100 per square foot, and \$200 per square foot includes all of the soft costs, profits, and land purchases. This distinction is important because only the hard costs can be used to calculate indirect jobs. The total hard construction cost estimate would be \$24.7 million, and the RIMS II final demand multiplier for construction is then used to calculate jobs. This multiplier varies widely by region and can range from 5 to 20. Assuming 20, this would imply 500 total jobs created from the construction activity. This does not count construction jobs, but rather the indirect jobs created by the construction activity.

Once the retail shopping center is open, the actual sales per square foot is calculated based on the mix of stores and the location, but assume that the average is \$58 per square foot per month or approximately \$700 per square foot per year. This implies \$172.9 million in sales. Here again, the RIMS II multiplier varies widely by region, assuming 20 this would imply approximately 3,500 permanent new jobs created from the operations of the retail space.

This methodology is then followed through with the remainder of the project. As noted above the project cost is estimated at \$1.448 billion. As the store example, approximately half is hard construction costs, the other half is all other costs. Using the above multiplier this would imply \$724 million to be applied to the multiplier (jobs per \$1 million), of between 5 and 20. Assuming 20, this would imply 14,480 jobs; however, this expenditure is over several years, for example, if over 5 years this implies an average employment of 2,896.

The other operations, including the arena, infrastructure (parking, municipal water, sewer line, roads, new subway entrance) as well as the high-rise buildings (cleaning, operations, maintenance) further create more jobs as the residential area will also need maintenance, etc.

In the case of this project the projected total number of jobs created would be over 7,500. However, to be conservative the project used lower estimates to assist in ensuring that permanent residency is not denied to some of the investors. To justify the 4,560 jobs created would require that the minimum multiplier for this region be a 12 rather than a 20.

Updated Job Information

At a recent Atlantic Yards District Service Cabinet meeting Forest City Ratner officials indicated that there were 666 workers at the site, including the arena, transit connection, and rail yard. Actual full-time construction jobs are probably 25% lower, or closer to 500 (Oder, 2012). Figure 4 shows how construction activity varies in terms of workers per quarter. Because of the duration of this project, these jobs can be counted.

Figure 4: Summary of Construction Workers for the Atlantic Yards Project

Table 13

Summary of Construction Workers and Delivery Trucks

	Year	2006				2007				2008				2009				2010			
		Quarter	1st	2nd	3rd	4th	1st	2nd	3rd	4th	1st	2nd	3rd	4th	1st	2nd	3rd	4th	1st	2nd	3rd
FEIS	Workers				565	635	460	588	1,140	1,575	2,220	2,920	3,540	3,710	3,505	2,325	1,250	745	665	620	340
	Deliveries				155	270	240	410	305	265	375	355	430	470	405	360	280	140	150	160	165
Cur.	Workers					26	56	75	151	175	184	184	184	180	171	337	459	563	742	1,055	1,476
	Deliveries					75	90	110	106	106	106	126	126	96	96	166	231	191	374	266	231
	Year	2011				2012				2013				2014				2015			
		Quarter	1st	2nd	3rd	4th	1st	2nd	3rd	4th	1st	2nd	3rd	4th	1st	2nd	3rd	4th	1st	2nd	3rd
FEIS	Workers	490	1,035	1,760	2,105	2,215	2,090	1,450	810	595	570	820	845	440	420	705	870	870	855	855	805
	Deliveries	255	255	335	360	320	235	195	115	90	120	40	40	85	70	130	100	65	155	150	155
Cur.	Workers	1,681	1,728	1,620	1,597	1,615	1,904	1,949	1,954	1,880	1,706	1,352	873	721	833	1,089	1,369	1,465	1,440	1,246	1,234
	Deliveries	265	314	310	409	447	404	283	367	341	358	298	240	299	278	325	310	280	255	225	210
	Year	2016				2017				2018				2019							
		Quarter	1st	2nd	3rd	4th	1st	2nd	3rd	4th	1st	2nd	3rd	4th	1st	2nd	3rd	4th			
FEIS	Workers	1,225	1,420	1,070	655																
	Deliveries	155	55	80	50																
Cur.	Workers	1,323	1,509	1,494	1,197	783	601	756	968	936	819	757	1,019	1,380	1,389	1,145	649				
	Deliveries	200	75	70	65	110	95	130	80	45	155	150	170	155	65	90	50				

Sources: Atlantic Yards Arena and Redevelopment Project FEIS (2006)
Revised schedule (April 2009)

Conclusion

Given the current economic climate and risk averse lenders, this makes construction finance more difficult to find and to qualify. The EB-5 program is an opportunity to find funding that may be not be available from traditional sources of funding. Furthermore because of the nature of the program, which provides green cards and permanent residency to foreigners, the EB-5 program provides low cost funding helping to ensure that projects are more viable financially (Wing, 2011). To ignore this source of funding could be expensive and subject a project to higher interest costs, which can be significant, especially on larger projects.

To minimize the risk to the investors seeking residency, a project needs to be thoroughly developed and viable even with higher interest rates. The lower cost financing available from the EB-5 program will then make the project more successful.

For further research we intend to show the types of projects that would benefit most from the EB-5 program, describing in greater detail the methodology used to count jobs and how some projects can be more successful for both developers and those seeking permanent residency.

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