THE IMPACT OF CHINESE QUOTA RETROGRESSION ON EB-5 INVESTORS AND EB-5 INVESTMENTS

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The EB-5 quota for China is expected to retrogress in 2013. This quota retrogression will impact not only EB-5 filings for Chinese nationals, but also EB-5 investments for applicants from other countries. This article will explore the ramifications of Chinese EB-5 quota retrogression for Chinese nationals and for the EB-5 program.

BACKGROUND

Although the EB-5 program's quota has remained unchanged since EB-5 became law in 1990, the approximate 10,000 quota for investors and derivative family members has been more than enough to satisfy demand.[1] In fact, in no previous fiscal year has demand exceeded 50% of the allocated quota.

However, with the increasing popularity of regional center investments, EB-5 visa usage reached its highest level in the fiscal year ending September 30, 2012.[2] The December 2012 Department of State Visa Bulletin predicted that the quota usage could be so high in the fiscal year ending September 30, 2013, that the per country limit may have to be imposed in the second half of the fiscal year.[3] Once that happens, the only country that would be affected is China since approximately 80% of

[1] There are about 9,940 EB-5 visas available in a year, unless there are unused family based visas, which would be reallocated to the employment-based categories according to their percentage of total employment-based numbers (the baseline is 140,000 and EB-5 is given 7.1% of that number). See 8 U.S.C. §§1151, 1152 and 1153.
[2] According to the Department of State, EB-5 visa usage totaled 7,641—more than double the usage in the prior fiscal year.
[3] www.travel.state.gov/visa/bulletin. The INA sets a per country limit of 7% of worldwide total numbers for any one country.

the world's EB-5 investors are from China.[4]

At this time, the U.S. Department of State has no idea how long of a "backlog" there may be should there be a need to impose a China cut-off date. That could only be determined if a cut-off is established, and would be dependent on several variables. Even though a cut-off date is not certain for FY2013, the increased demand makes the establishment of a cut-off date in the coming years almost inevitable.

DIRECT EB-5 FILINGS

Though most Chinese nationals choose to invest in a regional center, EB-5 visa quota retrogression for Chinese natives will all but eliminate the possibility of direct EB-5 filings. In order to obtain approval of an EB-5 petition, the investor must demonstrate that he or she has invested or is actively in the process of investing the required amount of capital. [5] The petitioner must demonstrate that the required amount of capital is at risk.[6] Evidence of mere intent to invest will not suffice. As a practical matter, USCIS has required the petitioner to demonstrate that the entire investment of $1,000,000 or $500,000 (if in a targeted employment area) has been made at the time of filing the form I-526, Immigrant Petition by Alien Entrepreneur.

With quota retrogression, it may be several years between the filing of the form I-526 and the time the investor can lawfully immigrate to the United States and manage his investment. For nationals of countries with investment treaties with the U.S., this problem is solved by the availability of the E-2 visa,

[4] U.S. Department of State EB-5 visa statistics (October 2012). The China EB-5 limit for fiscal year ending September 30, 2013 has already been reached. The only reason there are/will be numbers available in future months is that there are "otherwise unused" EB-5 numbers on a worldwide basis. A China cut-off date would only be imposed when/if it became apparent that the combination of China demand, and demand from all other countries (AOC), would not allow the AOC EB-5 status to remain "Current" throughout the fiscal year without the worldwide limit being reached.
[5] 8CFR§204.6(j)(2).
[6] Id.

which allows the investor to come to the U.S. to oversee the investment. However, no such treaty exists for Chinese nationals.

An investor who will have no way to directly manage his investment for many years due to quota retrogression will be unlikely to invest. Even if he did, an EB-5 petitioner must demonstrate that he will be engaged in the management of the new commercial enterprise.[7] A petitioner who cannot immigrate to the United States for many years because of quota retrogression may not be able to demonstrate that he will be able to manage a direct EB-5 investment.

In addition, for direct EB-5 investments, the I-526 petition must be accompanied by evidence that the new commercial enterprise will employ not fewer than ten qualifying employees within the next two years.[8] A comprehensive business plan must to be submitted showing the jobs that will be created and the approximate dates of hire.[9] The plan must demonstrate that the ten qualifying employees will be employed within the next two years. [10] The business plan should contain a detailed market analysis, including competing businesses, their strengths and weaknesses.[11] It defies logic that a petitioner could submit a credible business plan when he or she has no idea of the prospective timeline for immigrating to the United States. A petitioner who will have no ability to manage his investment will have no ability to employ and oversee the requisite employees.

Similarly, the ability of a Chinese investor to invest in a "troubled business" to obtain residence under the EB-5 program will be all but eliminated because of Chinese quota retrogression as the petitioner must demonstrate maintenance of the number of existing employees at no less than the pre-investment level for

[7] 8CFR§204.6(j)(5).
[8] 8CFR§204.6(j)(4)(i)(B). See infra, regarding the applicability of this rule to regional center investments.
[9] Id. See Matter of Ho, 22 I&N 201 (Assoc. Comm'r Examinations 1998).
[10] Id. See infra, regarding a USCIS Memorandum creating a "2½ year rule," which requires the investor to prove that the requisite jobs will be created within 2½ years of the approval of the I-526 petition.
[11] Id.

a period of two years.[12] When the petitioner may not immigrate for two (2) years, this may be impossible.

CHINESE QUOTA RETROGRESSION AND THE CHILD STATUS PROTECTION ACT

Chinese EB-5 quota retrogression will create a conflict between project developers, the agents and the Chinese investors. The project developers and the agents are anxious to obtain approval of form I-526. Many projects hold a petitioner's funds in escrow until the form I-526 is approved. Thus, approval of the form I-526 is often crucial to freeing up the investor's capital for use in the investment.

So how is this prompt-as-possible approval of the I-526 petition inconsistent with the investor's interest? It may be if the investor has a child reaching age 21. Here's why.

The Child Status Protection Act ("CSPA") freezes the age of children who are derivative beneficiaries of an I-526 petition while the petition is pending, but not once the petition is approved and awaiting the quota to become available.[13] A Chinese petitioner with children age eighteen or older will want to freeze a child's age for as long as possible if Chinese EB-5 priority dates retrogress. The longer the time the I-526 is pending, the longer the time the child's age is frozen. Thus, it will be beneficial for certain Chinese nationals who have children close to "aging out" to draw out the I-526 petition process. It might be advantageous for a Chinese national to receive a Request for Evidence as such a request makes the petitioning process longer. It might also be advantageous for the Chinese national to delay responding to the Request for Evidence until the latest possible date, again drawing out the petitioning process.[14] For example, form I-526 was filed for Mr. Wang on October 1, 2012. At the time the I-526 was filed,

[12] 8CFR§204.6(j)(4)(ii).
[13] Section 3, Public Law 107-208 116 Stat. 927.
[14] Legacy INS considers for CSPA purposes a visa petition to be "pending" as long as no final agency determination has been made on the petition. INS memorandum dated February 14, 2003 (HQADN70/1.1.1).

Mr. Wang's son's age was 20 and the priority date was current. While the I-526 was pending, Chinese EB-5 priority dates retrogressed to October 1, 2011. If Mr. Wang's 526 is approved on October 1, 2013, Mr. Wang can deduct the entire period of time the I-526 was pending (twelve months) from his son's actual age, likely saving him from "aging out."

Chinese EB-5 priority date retrogression will make it imperative for counsel to carefully track the ages of a petitioner's children and to strategize how to prolong the I-526 petitioning process, if a child is close to "aging out." It will also be imperative for counsel to make certain that the immigrant visa is applied for within one (1) year of the priority date becoming current, in order to be able to take advantage of the period of time the child's age is frozen during the petitioning process.[15]

Counsel representing the project and the investor may have to resolve ethical issues with the developers of the project and the investor pertaining to protracting the I-526 processing time.

IMPACT ON LENGTH OF INVESTMENT AND INVESTOR EXIT STRATEGY

Pursuant to 8 CFR§216.6(c)(1)(iii), the investor's investment in the new commercial enterprise must be "sustained" during the two years of conditional residence. Although the regulation is unclear as to whether the investment must be sustained until the filing of the condition removal petition or until the approval of the condition removal petition, USCIS appears to have required the sustaining of the investment through the approval of the I-829 petition. So how long is this period in which the investment must be sustained? If the average processing time of an I-526 petition is 8 months, and if it takes approximately one year to complete the adjustment of status process, or the conditional immigrant visa and U.S. entry process, and another two years is added for the filing of the I-829 petition and another

[15] 8 U.S.C. § 1153(h)(1)(A).

approximately 4 to 8 months is added for the approval of the petition to remove conditions on residence, one sees that, from the time of the investment and filing of the I-526 petition until the time conditions are removed and the investment no longer must be sustained, in most cases, between 4 and 5 years have elapsed.

So what happens in the event of quota retrogression? The time period before which the investor cannot have his investment capital returned is extended by the length of the quota retrogression. From the investor's point of view, this means that the investment money will be tied up for a longer period of time and any "exit strategy" will become more protracted.

There are particular issues for regional center investors. A significant majority of regional centers utilize the so-called "loan model". Under this model, the investor is an equity investor in the new commercial enterprise. The new commercial enterprise is, in turn, a lending company that lends the EB-5 investors' investment money to the project developer (the so-called "job creating enterprise"). Traditionally, the loan from the new commercial enterprise to a job-creating enterprise is five years (for the reasons indicated above), sometimes with provision for one or two year extensions (to cover any outliers), creating a five year exit strategy for investors.

Quota retrogression will require lengthening of the loan time period, which will delay the investor's return of investment proceeds. From the point of view of the job-creating enterprise, this could be good news or bad news. It means that the generally low interest EB-5 money will be available for a longer period of time. However, many project developers seek to refinance or sell the business, which could have significant negative consequences for the condition removal process for the investors if it occurs before the approval of the I-829.

Quota retrogression highlights the importance of USCIS addressing an unanswered question. What if a five year loan is, in fact, paid back to the new commercial enterprise at the end of the five years? However, with quota retrogression, the new commercial enterprise cannot pay the loan proceeds with interest back to the investors until the conditions are removed, which perhaps may be multiple years later. Is the investment in that event "sustained"? The authors believe that the answer is in the affirmative, but USCIS has yet to opine. The reason that the authors believe that the investment has been sustained is because the regulatory requirement is that the investment be sustained in the new commercial enterprise and not in the job-creating enterprise. If the investor's money has been used to create the jobs in the job-creating enterprise, and if the loan proceeds have been returned to the new commercial enterprise, and if the new commercial enterprise has not redeemed the investors' investment, the investment has clearly been "sustained" in the new commercial enterprise. Since the new commercial enterprise is "formed for the ongoing conduct of lawful business"[16] presumably the new commercial enterprise could lend the money elsewhere once the job creation requirement is met, although there is no specific requirement that it do so.

One issue that could be raised is that an investment that sits in a company bank account may not be considered to be "at risk" or being used for job creation. However, in the example cited, the necessary job creation has already occurred and the investment money was placed at risk in creating the jobs. Furthermore, the "capital at risk" requirement is a requirement of the I-526[17] and not a requirement of the I-829. The only requirements of the I-829 are that the investment in the new commercial enterprise has been sustained and the jobs created (or will be created within a reasonable time).[18] These requirements are satisfied in the case of a five year term loan even if quota retrogression results in a delay in the return of the investment money from the new commercial enterprise to the investor.

[16] 8CFR§204.6(e).
[17] 8CFR§204.6(j)(2).
[18] 8CFR§216.6(c)(1).

TWO AND ONE HALF YEAR RULE

USCIS presently applies an adjudicative standard, articulated in the controversial Neufeld Memorandum of December of 2009[19], requiring proof that the requisite ten jobs will be created within 2½ years of the approval of the investor's I-526 petition. This does not appear in the statute, regulation or any precedent decision. Rather, it is a creature of a non-binding memorandum.

The premise of the rule is faulty to begin with but loses any foundational justification once there is quota retrogression. The rule is premised on a six month period to complete adjustment of status or consular conditional immigrant visa processing. The two year conditional residence is then added to arrive at the 2½ year requirement.

The "rule" is faulty for at least four reasons even without quota retrogression:

- Neither the adjustment of status process nor the consular conditional immigrant visa process is usually completed within six months;
- With the conditional immigrant visa process, the investor and his family have an additional six months after issuance of the conditional immigrant visa to actually immigrate to the U.S. and commence the two year period of conditional residence;
- The regulations clearly state that the jobs do not all have to be created by the time of filing of the condition removal petition. The jobs do not even have to be created by the time of the adjudication of the condition removal petition, which is traditionally many months after the two

[19] USCIS Memorandum from Donald Neufeld to Field Leadership (HQ70/6.2, AD 09-38) (December 11, 2009).

years. Rather, the regulatory requirement is that the jobs must be created within a "reasonable time" after the adjudication of the I-829 condition removal petition;[20] and

– The two year job creation rule is arguably inapplicable to regional center investments.

With quota retrogression, the foundation of the rule is not only faulty but completely destroyed. As a practical matter, when the quota retrogresses, there will be no reliable indicator of when any particular investor's priority date will be reached. Until the priority date is reached, no adjustment of status application can be filed and no conditional immigrant visa interview can be scheduled. As arbitrary as the 2½ year rule is presently, it would be completely unjustifiable with quota retrogression which could result in the investor having to prove the requisite job creation before he ever even becomes a conditional permanent resident.

An examination of the regulations reveals that quota retrogression, while creating a major stumbling block for direct EB-5 investors, is actually helpful to investors in a regional center. The job creation regulation, 8CFR§204.6(j)(4), is divided into three parts – "general", which applies to direct EB-5; "troubled business"; and "immigrant investor pilot program". The "general" requirement (arguably not applicable to troubled businesses and regional center pilot program investors)[21] is that the comprehensive business plan shows the need for at least ten qualifying employees within the next two years. The troubled business regulation requires that the I-526 petition include evidence that the number of existing employees will be maintained at no less than the pre-investment level for at least two years. The qualification of a business as a troubled business is premised on the business' net loss during the 12 or 24 month period prior to the I-526 priority date.

[20] 8CFR§216.6(a)(4)(iii) and 8CFR§216.6(c)(1)(iv).
[21] Note that USCIS does, without apparent regulatory authority, apply the "general" job creation regulatory section to regional center investors.

However, for the large majority of investors who invest in regional centers, there is no two year job creation rule to be found anywhere in the regulations. Rather, 8CFR§204.6(j)(4)(ii) only requires evidence that the direct or indirect employment will be created from the investment but with no time period specified whatsoever.[22] 8CFR§204.6(m), which is the added regulatory section relating to regional centers, lists the requirement that the regional center describe how it will promote economic growth through job creation and how jobs will be created; but there is likewise no mention whatsoever of a time period. In the absence of such a two year time period for regional center investors, the only time period that exists is the requirement in 8CFR§216.6(c)(1)(iv)[23] that the jobs be created "within a reasonable time" following the approval of the condition removal.

Therefore, it would be a reasonable expectation that USCIS will withdraw its arbitrary 2½ year rule once quota retrogression is a reality. Presumably, unless some completely arbitrary standard is applied, the requirement would revert to the regulatory requirement that the regional center investor must prove that the indirect and induced employment will occur within a reasonable time after the conditions on residence are removed, which could be 4, 5, 6 or even more years from the time of filing the I-526 petition, depending on how backlogged the Chinese quota becomes.

IMPACT ON JOB CREATION

The 2½ year rule has significantly restricted indirect and induced job creation projections, and therefore the number of investors who can provide EB-5 capital to a given project. The reason is that in many projects, such as hotels, office buildings and shopping centers, stabilized occupancy may not occur for two or more years after construction is completed. If the construction period is, say, 18 months, and

[22] 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.
[23] Supra note 20.

stabilized occupancy (and the job creation that goes with it) does not occur for another 24 months, the job creation resulting from stabilized occupancy may occur after the 30 month period. The result has been that in many projects indirect and induced jobs from construction are the only jobs that can be counted. With the expected elimination of the 2½ year rule, the often significant operations jobs numbers can be added to the mix, increasing the number of jobs and therefore the number of investors per project.

Also, if the 2½ year rule is eliminated, a project including a mix of Chinese and non-Chinese EB-5 investors could have the benefit of allocating job creation over an extended period of time. For example, the non-Chinese EB-5 investors, who will be able to file their I-829 petitions much sooner, could be allocated the construction jobs whereas the Chinese investors could be allocated the operations jobs. Furthermore, with the protracted filing date of I-829 petitions for Chinese investors, developers will have longer periods of time to meet the required inputs in the economist's job projection report, such as longer periods of time to expend the money, produce the necessary revenues, employ the necessary direct employees, achieve the necessary occupancy rate, complete construction, etc. Meeting these projected inputs is critical for the investors to meet the job creation requirement to be able to remove conditions on their residence.

CONCLUSION

We can speculate on whether EB-5 quota retrogression for Chinese nationals will have an impact on the number of Chinese investors who choose to invest under the EB-5 program. However, no speculation is necessary regarding the impacts of quota retrogression on investors who have already invested or will invest in the future. The impacts, as this article has revealed, will be profound – for the investors, for the investment entities and for the policies of the government agency that regulates the program.