



Self-Directed IRAs as Funding Options for EB-5 Investors and Issuers



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Once upon a time, structuring an EB-5 investor's source of funds was simple. Throughout most of the program's history, the majority of source of funds were based on secured loans, a sale of property, or income.

Unfortunately, it is no longer that simple. We are at a crossroads in the EB-5 program where there's a juxtaposition of an increased minimum investment amount, tied up assets, staggered liquidity, and tax issues. Not to mention, we still have to make sure the EB-5 program achieves the investor's desired immigration goals.

Recently, a new option has emerged - Self-Directed IRA accounts ("SDIRAs"). SDIRAs are a powerful funding option for many investors, both as a pool of lawful funds and for certain tax advantages. For investors and issuers alike, it's important for them to understand the nuances of pursuing and accepting SDIRAs because it may be the difference between an investor electing to subscribe or not.

Below we explore why SDIRAs have become an increasingly popular and viable option, the mechanics behind using them, and some issues to consider when implementing a plan to accept them.



WHAT IS AN SDIRA?

SDIRAs are similar to other retirement accounts such as a traditional IRAs, Roth IRAs, or a 401K plan. They are funded with the investor's income and the funds can grow with certain tax advantage. The biggest difference, however, is the amount of freedom and control over the menu of investment options in each account.

In a traditional retirement account, a custodian or broker typically decides what menu of investment options are accessible to an investor. That menu may be limited to a few mutual funds or target-date funds (such as your typical 401K provider), or it may be much wider and include publicly-traded stocks, bonds, and ETFs (such as an IRA account through Charles Schwab).

However, an investor generally cannot use these accounts to invest into an EB-5 offering since they are private placements and are not public securities. The reason why funds in an SDIRA can be used to invest into an EB-5 offering is because now the investor decides the menu of investment options available to them (rather than the broker, for example). This allows investors to invest within a larger universe of options, including precious coins, artwork, collectibles, and yes, EB-5 private placement offerings. Thus, by rolling over eligible funds into an SDIRA, an investor is in complete control and able to use SDIRA funds to invest into an EB-5 offering.

Of course, while an SDIRA is now a viable option, it may not be appropriate for every investor. There are costs and fees to set up and manage SDIRAs and investors can incur penalties if funds are not properly invested or managed. Investors are advised to consult with an appropriate financial or tax advisor if they are interested in this option.

SDIRAS AS APPROVABLE CUSTODIAL ACCOUNTS

At a high level, using an SDIRA as the source of an EB-5 transaction isn't complicated. SDIRAs are funded with lawfully-earned money and are owned by the investor in a custodial account. The investor owns and controls the account and directs all investment decisions in the custodial account, whether that be publicly traded stocks or private placements. For EB-5 investments, the custodial account would simply subscribe, on the investor's behalf, by signing subscription documents in the name of the SDIRA. Finally, it is important to understand that custodial accounts are not a new concept in EB-5 and in fact have been widely used by law firms and issuers for years for certain transactions.

We originally explored SDIRAs as a possible piece of the source of funds puzzle because investors often had trouble completing the entire \$800,000 puzzle. It boils down to liquidity and tax-efficiency. Like most of us, it's not unusual for EB-5 investors to have a large amount of their money saved in a retirement account, whether that's a Traditional IRA, Roth IRA, 401K plan, etc. Until recently, using these types of retirement accounts for EB-5 this wasn't possible (largely because SDIRAs simply weren't a widely known option). However, by rolling other eligible retirement funds into a SDIRA, an investor can now use that entire amount as part of their source of funds for an EB-5 subscription. Thus, SDIRAs are ultimately part of a powerful set of tools advisors need to become familiar with in order to help their clients not only source their funds, but to help save them money and provide flexibility.

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PROCEDURAL ISSUES & PITFALLS TO CONSIDER

While we are advocates of using SDIRAs as a funding option, we'd caution investors and issuers to not blindly jump headfirst into setting up SDIRAs. Not all SDIRA providers and custodians are created equal. For investors, there are multiple issues to consider to ensure that it's structured properly, including, but not exclusive to, the following:

- **Ensure it's a Qualifying Rollover:** Investors should note that it is important to structure this as a qualifying rollover and not a withdrawal or distribution from their retirement accounts. Failure to do so would result in funds being taxed as ordinary income and possibly subject to additional early withdrawal penalties.
- **401K Plans and Conversions to SDIRA:** Investors should check with their 401K custodian to see whether it's possible to allow an in-plan conversion to an SDIRA. Some give maximum flexibility and have SDIRA options built into their plans, though many won't allow that conversion unless one leaves the company.
- **SDIRA and Subscribers:** Although funds earned by a couple through marriage are generally considered jointly owned, it's not necessarily the case when it comes to claiming the same treatment for subscriptions. Talk closely with your attorney and issuer to ensure that the right SDIRA and subscriber is used if it's a married couple.
- **SDIRA Doesn't Impact 401K Loans:** Keep in mind that while SDIRAs may only be used for the subscriber, both spouses can still draw on 401K loans, assuming they qualify.
- **Whether SDIRA Custodian is Familiar with EB-5 Private Placements:** Beware that not all SDIRAs are created equally, nor do they allow the same level of flexibility. If your SDIRA custodian doesn't allow you to invest in private placements (such as EB-5), then this effectively eliminates this option. For example, some of the more popular brokerage firms that supposedly provide SDIRA options limit investors from investing into EB-5 offerings (e.g., Fidelity). Please make sure that your custodian is familiar with EB-5 offerings.
- **Whether the Regional Center, Issuer, or Law Firm is Familiar with SDIRAs:** Not all regional centers, issuers, or law firms are experienced or comfortable with using SDIRAs as a funding mechanism. Those who are new should familiarize themselves with these options before advising clients. Otherwise, there is a risk that the investment could be improperly structured. Specific side letters and subscription documents are needed for SDIRA investments to be properly attributed to the investor (and, as such, it is critical to seek proper advice to ensure they are structured correctly on both the SDIRA and issuer side).

CLOSING THOUGHTS

Incorporating SDIRAs into an investor's funding strategy is part of the ongoing evolution of creatively structuring investments to help investors reach the minimum investment amount of \$800,000. It demands both attorneys and regional centers evolve and work closely with investors to help them structure tax advantaged and efficient funding plans. As one of our investors happily remarked just this week, "SDIRA, RC loans, 401k loans, and other loans are all approved at this point. This is big!! This makes it much easier for folks to reach the 800k mark. Many thanks to the RCs and Attorneys pushing the boundaries and making this possible."

Indeed, we couldn't agree more. In reality, SDIRAs have become part of our toolbox to construct an investor's sensible funding strategy that bridges immigration, investment, and tax goals. For example, instead of advising an investor to sell a house, we may advise them to file based on a partial investment; then six months later, bridge that minimum investment gap by taking out a 401K loan, exploring whether it makes sense to take out a margin loan on (or possibly sell) their restricted stock units (RSUs), and then creating an SDIRA to fill out the remainder of their investment. This allows investors to lock in their priority date, get the clock ticking on the processing of their Employment Authorization Document and Advance Parole document, and decide later whether to stagger the tax hit of liquidating any RSUs by spreading them out over two years.

It's important that, as an industry, we eventually move to normalize these concepts and educate ourselves, and clearly lay out these strategies and why they're acceptable to USCIS. EB-5 is difficult enough already – there's no need to remain burdened by traditional and perhaps dated source of funds avenues. We certainly advocate for evolution, education and working together with industry stakeholders and USCIS to ultimately accomplish investor goals. ■