



Redeployment Raises Questions and Increases Litigation Risks to EB-5 Sponsors

by Catherine D. Holmes

USCIS adopted Policy Manual changes on June 14, 2017, specifically addressing requirements for redeployment of capital contributions of EB-5 investors until the end of their two-year period of conditional permanent residency. Two years later, USCIS has not provided any further guidance on these issues, leaving EB-5 sponsors to navigate this uncertain terrain using their own best judgement. These efforts have produced varied results, as each EB-5 sponsor and its advisors seek to establish a method for redeployment of EB-5 capital that will satisfy USCIS guidelines, U.S. securities laws, EB-5 investors, and all of the other parties who collectively have an impact on the investment of EB-5 capital. In some cases, EB-5 investors have threatened or actually filed actions against new commercial enterprises (NCEs) as a result of the approval process and/or selection of the reinvestment. This article briefly describes some of the questions that arise in connection with redeployment decisions, and offers some thoughts on how to address the inherent risks of the redeployment process.

Should EB-5 investors be asked to approve a redeployment?

If the partnership or operating agreement of the NCE does not authorize the general partner or manager to select a reinvestment at all, or only allows reinvestment with the consent of the EB-5 investors, then it will be required that consent be obtained. However, rather than asking for approval of a specific reinvestment option, it may be preferable to request approval of an amendment to the partnership or operating agreement to allow the general partner or manager to select all reinvestments for the NCE, subject to defined standards that apply to selection of the reinvestment. The benefit of this approach is that it covers not only the first reinvestment, but all future reinvestments that may be necessary for as long as the NCE has EB-5 investors who are not eligible for repayment. To use this approach, it is important that the standards that will apply to reinvestments demonstrate that the process used to select reinvestments protects the EB-5 investors.

Why not have EB-5 investors approve every redeployment decision?

Even though it might potentially reduce litigation risks if a majority of EB-5 investors voted to approve each redeployment investment, obtaining approval from EB-5 investors (many of whom may still be abroad due to retrogression delays) may be difficult, and could result in EB-5 investors objecting to the reinvestment recommended by the general partner or manager of the NCE. This could lead to one or more rounds of voting with inconclusive results. In the worst-case scenario, if approval could not be obtained without significant delays, the NCE may run the risk of not meeting USCIS requirements for reinvesting capital within a commercially reasonable period of time. In practice, therefore, it may be advisable to have the manager or general partner of the NCE make the reinvestment decision. The manager or general partner should issue a notice to the EB-5 investors regarding the reinvestment, and should include details of the process used to underwrite the reinvestment. Some EB-5 investors may still object, but if the NCE's operating agreement or partnership agreement grants the manager or general partner the authority to make the reinvestment decision without consent of the EB-5 investors, and the process used to make the redeployment selection provided third-party protections, it should reduce the litigation risks to the NCE.

What process should be used to make a reinvestment decision that demonstrates protection of the interests of the EB-5 investors?

The best practices for selection of reinvestments should include the following elements: (i) written advice from the NCE's immigration legal counsel that the reinvestment meets the USCIS standards for reinvestment, based upon current understanding of those standards, (ii) written advice from a third party regarding the value of the asset in which the reinvestment will be made, which may be in the form of a registered investment adviser's analysis of the reinvestment, third-party due diligence report, or other third-party analysis (especially if there are conflicts of interest between the general partner or manager and the owners of the property in which the reinvestment will be made), (iii) terms of the reinvestment that are no less favorable to the EB-5 investors than their original investment, especially with respect to anticipated exit date, priority of payment, and subordination to other creditors.

Should EB-5 investors be permitted to receive repayment rather than have their funds reinvested?

Because of the extreme delay now projected for investors from China in particular, some EB-5 investors may decide they would rather receive a return of their investment than continue to pursue a visa under the EB-5 Program. One of the best ways for an NCE and its management to reduce risks is to repay EB-5 investors who ask for a return of their funds at such times as the funds become available for repayment. However, the NCE must be cautious in offering this option to EB-5 investors, to avoid the impression that all EB-5 investors in the NCE have the right to a return of their investment at any time. If, however, an EB-5 investor provides evidence to the NCE that he or she has withdrawn their I-526 petition, it may be acceptable to repay that EB-5 investor without putting the other EB-5 investors in the NCE at risk. This should be discussed with the NCE's lead immigration counsel to determine how this may be accomplished and documented.

This article does not address securities law issues in connection with reinvestment decisions, a topic discussed in a previous article entitled: "The Essential Role of a Registered Investment Adviser in the Redeployment of EB-5 Capital."

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