



Foreign Investment in U.S. Commercial Real Estate A Guide to Legal Issues



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A NOTE FROM THE WRITER

Foreign investment in U.S. commercial real estate has increased dramatically and is expected to continue to increase, with many billions of dollars in foreign capital invested in the U.S. from 2005 through the current year 2015. Although there are many reasons for this dramatic increase including the best opportunity for capital appreciation, the following guidelines will examine and analyze solely the legal issues that most commonly arise and must be considered by foreign investors when contemplating such investments.



1 FIRPTA

The Foreign Investment in Real Property Tax Act (“FIRPTA”) was enacted in 1980 to correct perceived unfair tax advantages for foreign investors in U.S. real estate. (Note: in this paper, unless otherwise noted, the word “foreign” refers solely to individuals who are not citizens of the United States or entities that are not qualified or registered as domestic entities in the United States). Under § 897 of the Internal Revenue Code (“IRC”) (which, together with IRC §§ 1445 and 6039(c) and some uncodified provisions make up FIRPTA), gains on dispositions of U.S. property interests by a nonresident alien or a foreign corporation are treated as “effectively connected income” (“ECI” -- rental income and/or gains on U.S. real estate), which is taxed at the same rates that apply to U.S. taxpayers. Foreign investors that receive ECI are required to file US federal and state income tax returns. Although in most cases rental income will constitute ECI, FIRPTA only applies to gain on the disposition of U.S. real estate, U.S. trade or business rules apply to rental income. The form of entity utilized by a foreign investor to invest in U.S. real estate is strongly influenced by the tax treatment of such entity (e.g., corporation, partnership, trust, joint venture, limited liability company (“LLC”), or Real Estate Investment Trust (“REIT”)) and the nationality of the entity.

IRC § 1445 provides that, subject to certain enumerated exemptions (including the furnishing of a nonforeign affidavit by the transferor), “in the case of any disposition of a United States real property interest (as defined in IRC § 897) by a foreign person, the transferee shall be required to deduct and withhold a tax equal to 10 percent of the amount on the disposition.”

A “foreign person” is defined in Treas. Reg. § 1.897-9T as a nonresident alien individual, foreign corporation that has not made an election under section 897(i) of the Internal Revenue Code to be treated as a domestic corporation, foreign partnership, foreign trust, or foreign estate. It does not include a resident alien individual.

A U.S. real property interest is defined as an interest in real property in the United States or the Virgin Islands, and also includes a direct or indirect (e.g., through a corporate subsidiary) ownership of U.S. real estate as well as investments in certain U.S. entities that own U.S. real estate. The sale of an interest in a partnership or trust will be treated as ECI to the extent it is attributable to U.S. real property interests held by such entity.

A foreign corporation is taxed on ECI (including FIRPTA income) at a maximum rate of 35%. Foreign corporations are also required to pay a “branch profits” tax equal to 30% of after-tax income that is not reinvested in the United States (although this is often reduced under tax treaties). If a foreign investor makes a mortgage loan secured by U.S. real estate, it is not subject to FIRPTA. This is true even for a participating mortgage loan, but only so long as the mortgage is structured so that it is treated as debt for U.S. income tax purposes (i.e. the participation feature is reasonably capped).

2 The Patriot Act

As an immediate result of the terrorist attacks on American soil on September 11, 2001, the USA Patriot Act, 115 Stat. 272, was signed into law in 2001; see also USA Patriot Improvement and Reauthorization Act of 2005, 120 Stat. 192 (2006). These laws (collectively the “Patriot Act”) enable the U.S. government to investigate suspected terrorists and prevent such persons from gaining access to financial resources needed to carry out their activities by means such as money laundering. Executive Order 13224, 66 Fed. Reg. 49,079 (Sept. 23, 2001) (“Executive Order”) focuses on persons who are deemed to be security risks to the United States and prohibits Americans from entering into any transactions with such persons. The Patriot Act does not impose anti-money-laundering requirements on parties involved in real-estate transactions (as such transactions were not considered a prime source of money-laundering activities), unless a party (1) is a “financial institution,” which includes “persons involved in real estate closings and settlements” (which refers to settlement agents and not the contracting parties), or (2) is involved in cash payments (not checks, wire transfers, or credit cards) over \$10,000. One transaction or several transactions can trigger the \$10,000 limit.

However, the Executive Order applies to any kind of business transaction and all persons and entities, not only “financial institutions,” must comply with the Executive Order. The Executive Order “blocks property and prohibits transactions with persons who commit, threaten to commit, or support terrorism.” The names of such persons are compiled by the U.S. government and the list is widely known as the “Specially Designated Nationals and Blocked Persons (“SDN”) list. To avoid violating the Executive Order, parties must check the SDN list before entering into a transaction with another party. [Note: The “Customer Identification Program” regulations of the Patriot Act require, under many circumstances, that a financial institution notify its borrower that it is obtaining and verifying such information. 31 C.F.R. 1020.220(a)(5)(i).]

The Executive Order imposes a “strict liability” standard. The normal response of parties dealing with foreign investors in real estate would be to not accept payments of more than \$10,000 in cash without reporting such action to the U.S. Treasury Department and to check the SDN list before entering into transactions with third parties.

Another popular response to the Patriot Act and the Executive Order has been the insertion of contractual “anti-terrorism” clauses in real-estate contracts. See **Exhibit A** attached hereto for suggested sample Patriot Act and anti-terrorism clauses in mortgages and leases. These types of clauses are still commonly inserted in current mortgage-loan and lease documents. *But see* Steven A. Teitelbaum, Stephanie M. Holmes, and Brian Morganstern, *Anti-Terrorism Clauses in Commercial Real Estate Transactions*, 25 No. 2 PRAC. REAL EST. LAW. 29 (March, 2009). The authors conclude that these clauses are mostly legally unnecessary and may even be counter-productive, i.e., that in commercial real-estate transactions such clauses generally needlessly delay negotiations; contain vague language; may actually increase contractual liability (because a breach may easily occur and there is no private cause of action under the Patriot Act); and create a lack of reciprocity. But the authors also acknowledge that “it is possible that well-crafted, narrowly tailored anti-terrorism clauses may be used as evidence of



due diligence to avoid criminal liability, to decrease civil penalties for noncompliance, and to escape contractual entanglements with prohibited parties.” *Id.* at 39. The authors then set forth a “Practice Checklist” for anti-terrorism clauses in commercial real-estate transactions, which suggests that such clauses address the following issues: 1) reciprocity; 2) certification of identity; 3) option to terminate; 4) overly broad terminology; and 5) scope of penalty.

3 Federal and State Ownership, Reporting, and Disclosure Laws

Most of the federal and state regulation of foreign investment in U.S. real estate is concerned with identifying the source and level of the investment by means of various reporting and disclosure statutes. The purpose of these statutes generally is the compilation of statistical analysis and information, and not the ability to use such information for other reasons such as taxation.

A. Federal Statutory Reporting and Restrictions

There are few federal statutory restrictions on foreign investment in real estate, which often deal with specialized land or functions such as agriculture, grazing on public lands, or public lands improved at the expense of a reclamation project, and which generally require only periodic reporting and/or disclosure.

See, e.g., the Agricultural Foreign Investment Disclosure Act (“AFIDA”), 92 Stat 1263 (1978). The regulations promulgated under the law require foreign entities to report interests in U.S. agricultural land to the U.S. Department of Agriculture. As stated in 1 FED. REG. REAL ESTATE & MORTGAGE LENDING § 7:19 (4th ed.) (Database updated June 2015):

As originally enacted, AFIDA required the Secretary of Agriculture to analyze the information contained in the disclosures, to “determine the effects of foreign persons acquiring, transferring, and holding agricultural land, particularly the effects of such acquisitions, transfers, and holdings on family farms and rural communities.” Once this analysis was made, a report was to be submitted to Congress and the President. This analysis and report has been eliminated. The Secretary still must submit, every six months, to the various State departments of agriculture, copies of the Form FSA-153 applicable to land in that state. All reports submitted by the Secretary of Agriculture are available for public inspection.

The International Investment and Trade in Services Survey Act of 1976, 22 U.S.C.A. §§ 3101- 3108 (with accompanying regulations at 15 C.F.R. pt. 806 (1998)), as amended (“IITSA”), was enacted with the following purpose, as set forth in § 3101(b):

It is . . . the purpose of this chapter to provide clear and unambiguous authority for the President to collect information on international investment and United States foreign trade in services, whether directly or by affiliates, including related information necessary for assessing the impact of such investment and trade, to authorize the collection and use of information on direct investments owned or controlled directly or indirectly by foreign governments or persons, and to provide analyses of such information to the Congress, the executive agencies, and the general public. It is the intent of the Congress that information which is collected from the public under this chapter be obtained with a minimum burden on business and other respondents and with no unnecessary duplication of effort, consistent with the national interest in obtaining comprehensive and reliable information on international investment and trade in services.

The IITSA, pursuant to § 3102(3), defines “person” as “any individual, branch, partnership, associated group, association, estate, trust, corporation, or other organization (whether or not organized under the laws of any State), and any government (including a foreign government, the United States Government, a State or local government, and any agency, corporation, financial institution, or other entity or instrumentality thereof, including a government-sponsored agency); and further, pursuant to § 3102(3), as “any person resident outside the United States or subject to the jurisdiction of a country other than the United States.”

See Michael T. Madison, Jeffrey R. Dwyer, and Steven W. Bender, *IITSA*, 1 LAW OF REAL ESTATE FINANCING § 2:8 (Database Updated July 2015), which states as follows with respect to compliance with the IITSA:

Administered by the Department of Commerce, IITSA requires the filing of reports concerning direct or indirect acquisition by a foreign person of a voting interest of 10% or more in a U.S. enterprise, including real estate. IITSA contemplates large investment-grade acquisitions and therefore exempts from its reporting requirements real estate purchases of less than \$1 million and under 200 acres, residential properties held strictly for personal use, and investments as a limited partner.

Owing to IITSA's statistical nature and function, information received through its reporting requirements is subject to strict confidentiality standards and is limited to use for statistical purposes.

The Hart-Scott-Rodino Antitrust Improvement Act of 1976, 15 U.S.C.A. § 1311 et seq., as amended ("Hart-Scott-Rodino Act"), which applies strict reporting and disclosure requirements to determine if certain transactions involve any antitrust violations, exempts many smaller real-estate transactions but may affect large corporations involving significant real-estate portfolios. Although it contains exemptions for acquisitions of realty transferred in the ordinary course of business and non-income-producing raw land, it may not exempt income-producing farmland acquired in the ordinary course of business. The Federal Trade Commission has determined that acquisition of commercial property of less than \$15 million in any one metropolitan area should be exempt.

See generally Michael V. Seitzinger, *Foreign Investment in the United States: Major Federal Statutory Restrictions*, CONGRESSIONAL RESEARCH SERVICE (June 17, 2013), which states as follows at page 10:

There appear to be few federal restrictions on the ownership of land [in the United States] by foreign individuals or by foreign corporations. However, such past acts as the Homestead Act [citation omitted] required American citizenship in order to make claims on these lands. Today, the Desert Land Act requires citizenship or a declared intention of citizenship in order to make claims [citation omitted]. Also, the Secretary of the Interior continues to require American citizenship or a declared intention of citizenship for authorizing permits for grazing on public lands [citation omitted], and . . . the Agricultural Foreign Investment Disclosure Act requires the disclosure to the Secretary of Agriculture by foreigners of agricultural land purchases in the United States. Further, public lands improved at the expense of funds from a reclamation project can be sold only to United States citizens [citation omitted].

B. State Statutory and Regulatory Reporting and Restrictions

Many (but not all) states have statutes that deal with ownership, reporting, disclosure, and/or divestment of foreign investments in U.S. real estate. For example, in Alaska, Articles of Incorporation of domestic corporations and applications of certification of authority for foreign corporations and biannual reports of all corporations must disclose (among other items) the name and address of each alien affiliate, the percentage of outstanding shares controlled by each alien affiliate, and a specific description of the nature of the relationship between the foreign corporation and its alien affiliate; or, a statement that there are no alien affiliates. To be qualified in Alaska to acquire and hold exploration and mining rights in state-owned lands, a corporation must be organized under the laws of a state or territory of the U.S. and no more than 50% of its stock may be owned or controlled by aliens who could not own directly.

In California, there are no restrictions on land ownership except with respect to leases and prospecting permits on public land. An Illinois statute, 815 ILCS 125/1, requires that foreign corporations must sell title to the land acquired under any judgment or power in a mortgage or deed within five years of acquiring title. (Most real estate attorneys in Illinois, when giving legal opinions on mortgage loans in Illinois by foreign corporations, will raise this statutory language as a qualification or exception). In Kansas, with certain exceptions, no corporation, trust, limited partnership, or corporate partnership shall own or lease any agricultural land. In addition, foreign insurance companies may not engage in agriculture, horticulture, or dairy business. In Minnesota, all corporations are prohibited from owning real estate capable of being used for farming, subject to certain exceptions. In addition, no corporation, partnership, limited partnership, trustee or other business entity shall acquire, directly or indirectly,

any legal or beneficial interest in agricultural land unless 80% of each class of stock issued or if the ultimate beneficial interest is held directly or indirectly by U.S. citizens. In Missouri, persons not citizens of the United States and not residents of the United States or of some territory, trusteeship, or protectorate of the United States, and corporations not created by or under the laws of the United States or of some state, territory, trusteeship, or protectorate of the United States shall be capable of acquiring, by grant, purchase, devise or descent, real estate except agricultural land. Oklahoma and Wisconsin have restrictions on foreign ownership of real estate, and other states (including Wyoming and New Hampshire) restrict foreign ownership as well. Over half of the states have some restrictions on the ownership of land by foreigners.

Many of the state laws and regulations apply to agricultural land and have varying degrees of restrictions. *See, e.g., Allegheny Corp. v Richardson, Inc.*, 463 NW2d 678, 679-80 (S.D. 1990) (holding that South Dakota statute prohibiting foreign corporations from being licensed to own agricultural land to be used in farming business in state was plain and unambiguous; thus, issuance by secretary of state of certificate of authority purporting to permit corporation to purchase state farm land was ineffectual for that purpose, and corporation could not successfully maintain action for specific performance of alleged contracts to purchase farm land).

Additional state restrictions and licensing requirements may apply in the case of hotels, resorts, and other types of commercial properties that involve the sale of beer and wine or liquor. Although these requirements vary widely among the states, many require full disclosure of the beneficial owners of the property. A foreign investor interested in acquiring such properties should become familiar with and understand the liquor-license requirements of the state where the property is located.

See generally, Alien Land Ownership Guide (State Laws Relating to Ownership of U.S. Land by Aliens and Business Entities), National Association of Realtors, available at [http://www.realtor.org/NCommSrc.nsf/files/Alien%20Land%20Ownership%20Guide%20\(November%202006\).pdf/\\$FILE/Alien%20Land%20Ownership%20Guide%20\(November%202006\).pdf](http://www.realtor.org/NCommSrc.nsf/files/Alien%20Land%20Ownership%20Guide%20(November%202006).pdf/$FILE/Alien%20Land%20Ownership%20Guide%20(November%202006).pdf). [Note: This summary was prepared in 2006 and may not be current, complete, or accurate with respect to all of the laws summarized in the Guide.]

4 Ownership Structures

A. Tax Considerations

Because of the tax implications of foreign investment in U.S. real estate, it is crucial for a foreign investor to focus on tax structuring when forming an entity to own U.S. real estate. *See generally* Michael T. Madison, Jeffrey R. Dwyer, and Steven W. Bender, *Relevant tax goals – Summary of U.S. Tax Consideration in Selecting an Entity*, 1 LAW OF REAL ESTATE FINANCING § 2:49 (Database Updated July 2015). The authors state, at § 2:21, that:

The relevant tax goals of a foreign person selecting an entity structure to hold U.S. real estate are not identical with the goals of a U.S. person. The goals with respect to a foreign person are as follows:

- (1) to qualify for nonrecognition treatment of gains when transferring appreciated U.S. real property interest to the entity;
- (2) to avoid nonrecognition treatment when transferring assets other than U.S. real property interest to the entity;
- (3) to avoid exposing the operating income from the real estate enterprise to U.S. taxation at both the entity and owner level (the only pass-through entity available for foreign persons to use in conducting a U.S. enterprise is a partnership);
- (4) to reduce, where possible, the U.S. income tax base of operating income by making payments to entity owners that are deductible at the entity level but are not includable in the U.S. tax base of the recipient owner;

(5) to avoid or reduce U.S. income tax on termination of the enterprise by restricting U.S. taxation to tax at the entity level; and

(6) to avoid U.S. estate, gift, and generation-skipping tax on the direct or indirect gratuitous transfer of U.S. real property interests.

A comprehensive analysis of the tax effects of the investment structure selected by a foreign investor for investment in United States commercial property is beyond the scope of this paper. For an excellent summary of the tax issues with respect to foreign investment in U.S. real estate, including suggested structures to minimize adverse tax effects, see Deloitte, *Introduction to the taxation of foreign investment in U.S. real estate* (2014), available at <http://www2.deloitte.com/us/en/pages/tax/articles/introduction-to-the-taxation-of-foreign-investment-in-us-real-estate.html>.

B. REITs

Foreign investors often choose to invest in a REIT as a buffer between themselves and U.S. real estate, in order to avoid or minimize the tax impact of the structure. See John L. Sullivan and Robert J. Le Duc, *Non U.S. Investors in U.S Real Estate: Tax Challenges and Solutions*, DLA Piper, available at: <https://www.dlapiper.com/en/us/insights/publications/2014/07/non-us-investors-in-us-real-estate/>. The authors discuss and analyze the various forms of ownership structures that may be considered with respect to foreign investment in U.S. real estate in general, and in particular the utilization of REITs as investment vehicles. The authors note that a properly organized and structured REIT will escape corporate taxation, despite being viewed as a corporation for most US federal income tax purposes. The authors also note that:

[W]ith few exceptions, gains that a REIT derives from dispositions of US real property interests will be taxable under FIRPTA in the hands of a non-US investor just as if such investor disposed of the US real property interest itself. Importantly, all ordinary REIT dividends should be viewed as dividends under US tax treaties and other provisions, such as [IRC] Code Section 892, and generally should not be viewed as ECI. This means such ordinary dividends are potentially subject to favorable US withholding rules under tax treaties and/or Code Section 892. Note, however, that ordinary REIT dividends are usually subject to less-favorable rates of withholding than corporate dividends under tax treaties.



The authors also compare the advantages and disadvantages of public REITs and private REITs with respect to foreign investors who choose participation in a REIT to invest in U.S. real estate. The use of public and private REITs has significantly increased as the applicable restrictions have been lessened.

Foreign persons are subject to a 30% federal withholding tax on ordinary dividends paid by a REIT (unless reduced by treaty) and capital gain dividends are treated as ECI unless the REIT invests in mortgages or (in some cases) the REIT is publicly traded.

In a relatively standard structure non-U.S. investors would collectively hold less than one-half of the REIT's shares, the REIT would be domestically controlled and the non-U.S. investors could sell such shares free of U.S. tax; however, ordinary dividends would not be free of U.S. withholding tax (although depending on the availability of tax treaties and/or I.R.C. § 892, any operating income passed through such a REIT as ordinary dividends may qualify for favorable withholding rates).

C. LLCs

With respect to the use of an LLC as an ownership vehicle, *see* David C. Djaha and John M. Creedon, *A Primer on Real Estate Investing Through Limited Liability Companies* 14 No. 2 IBA REAL EST. 41, 43 (Sept. 2010). The authors state that:

LLC agreements must be tailored to address the specific tax needs or concerns of the members and structured in a manner that minimizes adverse tax consequences, especially for investors that are not ordinarily subject to US tax. LLCs are often the preferred investment vehicle because they allow flexibility in structuring investments in a manner that maximizes the after-tax income of otherwise tax-exempt investors, often by minimizing unrelated business taxable income (UBTI) for US tax-exempt institutions and effectively connected income (ECI) for foreign investors.

The income tax rates and rules applicable to individuals (including the FIRPTA rules) will in most cases apply to a foreign individual holding ownership through a U.S. LLC. Absent an election to be taxed as a corporation, if a U.S. LLC has just one owner it is disregarded for U.S. tax purposes, and if it has multiple owners it is taxed as a partnership. The compliance burden and expense can become burdensome because a U.S. LLC may have a tax withholding and filing obligation on top of the filing obligation of a foreign owner of the LLC.

D. Other Structures

Typical non-REIT and non-LLC investment structures in U.S. real estate include direct investment, partnership, joint venture, corporation, trust, "standard" and participating or contingent mortgage loans, and a standard real-estate fund with a subsidiary REIT structure. The tax implications of these various structures are beyond the scope of this paper. If a corporation or partnership is selected, the appropriate method of capitalization (ratio of debt to equity) must be established. Trusts are seldom used by foreign investors with respect to commercial real estate in the United States. *See* Michael T. Madison, Jeffrey R. Dwyer, and Steven W. Bender, *Relevant Tax Goals – Summary of U.S. Tax Treatment of Trusts*, 1 LAW OF REAL ESTATE FINANCING § 2:25 (Database Updated July 2015), where the authors state that "Holding income-producing U.S. real property through a trust is not advisable unless it is a grantor trust or is used as a vehicle to make gifts of U.S. real property interests to persons who need some type of custodial arrangement."

5 EB-5 Investments

A. Definition and Scope

The EB-5 program was established in 1990 by the Immigration and Nationality Act, 8 U.S.C. § 1153(b)(5). The program was created as a mechanism to boost foreign investment in job creation and economic development in areas that were suffering from high unemployment, or were considered blighted or rural. The program also offers permanent U.S. residence to immigrants seeking to enter the United States, who invest specified amounts in a new or established U.S. commercial enterprise that creates or preserves at least ten full-time jobs for U.S. workers (excluding the investor and his or her immediate family) per investor. The United States Citizenship and Immigration Services (“USCIS”) administers the program. The program is known as EB-5 for the name of the employment-based fifth preference visa that foreign investors receive. The minimum investment amount required to qualify for the program and obtain the desired visa is \$500,000 in a Targeted Employment Area (“TEA”) and \$1 million for projects in a non-TEA area.

See S.H. Spencer Compton and Diane Schottenstein, *The Intersection of Real Estate and Immigration*, 30 No. 4 PRAC. REAL EST. LAW. 5 (July 214), at *6, which states that, “The United States Citizenship & Immigration Services (“USCIS”) “in essence defines a TEA as either: (1) a rural area; or (2) an area experiencing unemployment of at least 150% of the national average rate [citing 8 CFR section 204.6(e)].”

EB-5 projects have experienced rapid growth in the past several years. See 48 No. 12 MORTGAGE AND REAL ESTATE EXECUTIVES REPORT NL-4, 48 No. 12 (2015), which states that, “From 2010 to 2014, there has been a 504% increase in the use of EB-5 financing, with nearly \$9 billion in capital invested in the U.S. from 2005 to 2014.” Also, according to this Report:

In early June [2015], bipartisan legislation was introduced in the U.S. Senate. The bill would both reauthorize and reform the 20-year old Immigrant Investor Program known as “EB-5” that is set to expire on September 30, 2015.

One of the key changes on the table under the newly proposed Senate Bill is to redefine the criteria to qualify as a Targeted Employment Area (TEA), which would have significant impact on a project’s ability to access EB-5 money.

The minimum investment amount to qualify for the program and obtain the desired visa is \$500,000 in a TEA area and \$1 million for projects in a non-TEA area. “The overwhelming majority of deals that are getting done are TEA deals,” says Jonathan Bloch, a partner and head of the EB-5 developer financing team at Jeffer Mangels Butler Mitchell LLP in Los Angeles.

In some states, the definition of TEA has been interpreted very loosely or expansively, resulting in EB-5 projects being granted in areas that are not blighted or struggling with high unemployment. That use has drawn criticism from program administrators and legislators. [There have also been incidents involving fraud in connection with certain EB-5 projects.] The Senate bill calls for defining TEAs more narrowly based on a single census tract where a project is located, and that census tract must have an unemployment rate that is 150% above the national unemployment rate or about 8.25% based on current unemployment levels.

Under current law, there is no national standard for calculating TEA. It is done at the state, county or even city level, depending on the region. For example, California EB-5 projects use 10 to 12 census tracts surrounding the physical location of a project to establish a combined unemployment rate for a broader area to help define whether it does or does not qualify as a TEA.

Another notable change is that the new legislation would raise the minimum investment amount, which has not changed in the past 15 years. The figure would increase to \$800,000 for TEA projects and \$1.2 million for non-TEA projects. However, the general view in the industry is that raising the minimum amount is not going

to impact the enormous demand from people overseas to be investors in this program, says Bloch. There are a number of other proposed changes within the 80-page bill that are aimed at bringing more oversight and efficiency to the program. Legislators and government agencies want to make sure that the money is targeted and goes to the right areas and are creating jobs, they also want to make sure there is no fraud and abuse.

Bipartisan legislation was introduced in the U.S. Senate in June, 2015 that reauthorizes and reforms the 20-year-old EB-5 program, which was set to expire on September 30, 2015. This new legislation would mean changes (and some challenges) for EB-5 investors (still a small but steadily increasing segment of the commercial real estate market), including: 1) more clarity and transparency; 2) reduction in the instances of fraud and wrongdoing; and 3) the direction of EB-5 funds to U.S. geographical areas where development and job creation are most crucial. Also, the SEC likely will be more inclined to prosecute “middlemen” and intermediaries, such as unlicensed investment brokers and those individuals seeking a “finder’s fee” for directing a foreign investor to a Regional Center program (see below for a discussion of Regional Centers). There are, unfortunately, some individuals and entities that use the EB-5 program in violation of securities laws and regulations.

On September 22, 2015, Invest in the USA (“IIUSA”), a national not-for-profit industry trade association for the EB-5 program, delivered a “Working” letter to Congress signed by more than 875 organizations supporting reauthorization of the EB-5 program. See *IIUSA Sends Congress Letter of Support for EB-5 Reauthorization*, available at <https://iiusa.org/blog/press-room/press-releases/press-release-iiusa-sends-congress-letter-support-eb5-reauthorization/#sthash.2rRM5ThU.dpuf>. According to IIUSA’s economic impact report, investments made through the EB-5 Program in fiscal year 2013 contributed \$3.58 billion to U.S. Gross Domestic Product and supported over 41,000 U.S. jobs, at no cost to the taxpayer. In addition, almost \$3.25 billion in EB-5 investments was raised in the first three quarters of fiscal year 2015, with more than \$6.5 billion in additional EB-5 investment funding awaiting government approval.

On September 30, 2015, the EB-5 program received a temporary reprieve via the passage of a Continuing Resolution (“CR”) by Congress, which will fund the federal government for an additional 10 weeks through December 11, 2015. The CR contains a short-term extension of the EB-5 program in its present form, and will allow Congress more time to enact reforms to the program and reconcile the House and Senate legislative proposals. Section 131 of the CR contains the language expanding the EB-5 program. While the CR has prevented a government shutdown, if lawmakers are unable to pass an Omnibus appropriations bill containing long-term or permanent reauthorization of the EB-5 program with reform measures or agree to a further extension (or perhaps a stand-alone EB-5 reauthorization bill) by December 11, 2015 the program will expire, or else Congress will have to find another legislative remedy to keep the program alive.

B. EB-5 Regional Centers

EB-5 investments may be made in a designated regional center (“Regional Center”), which allows indirect job creation to be taken into account to meet the required employment numbers. The Regional Centers are able to pool investments, so that the individual investor need not be responsible for directly overseeing the specific investments. A number of developers have used this vehicle to finance the acquisition of existing hotels and the construction of new hotels, as it can provide inexpensive financing with favorable terms. It has also become an attractive source of mezzanine financing now that capital for construction projects is more readily available from traditional first-mortgage financing sources. According to S.H. Spencer Compton and Diane Schottenstein, *The Intersection of Real Estate and Immigration*, 30 No. 4 PRAC. REAL EST. LAW., supra, at *6:

A “Regional Center” is defined by the USCIS as “any economic entity, public or private, which is involved with the promotion of economic growth, improved regional productivity, job creation and increased domestic capital investment.” Investments within a Regional Center allow foreign nationals to count jobs created both directly and indirectly for purposes of meeting the ten-job-creation requirement. For example, if a project is to build a hotel, those hotel jobs subsequently created can be counted as jobs created by the EB-5 construction project. This use of Regional Centers was first introduced as a pilot program in 1993, and in 2003 President Obama [sic] made it a permanent feature.

How does the process work? First, the Regional Center obtains preapproval for its selected EB-5 projects, and then foreigners invest in that Regional Center. Regional Center certification arguably lends legitimacy that helps in marketing to foreign nationals. These passive investments have been likened to those in a closed end mutual fund: the Regional Center is a third-party investment vehicle which pools capital from multiple EB-5 investors, then invests in various multimillion-dollar projects and charges an administrative fee for its management services. As of February 2012, there were 218 Regional Centers, predominately in California, Florida and Washington. According to the USCIS website (uscis.gov); as of June 2, 2014, USCIS had approved approximately 532 Regional Centers. A Regional Center being listed on the website does not indicate an endorsement by the USCIS.

USCIS has stated, in its *General EB-5 Program Overview*, available at <http://www.uscis.gov/sites/default/files/USCIS/Resources/Resources%20for%20Congress/Congressional%20Reports/EB-5%20Investor%20Pilot%20Program.pdf>, that:

A Regional Center is not merely a defined geographic area but rather is a business entity that coordinates foreign investment within that area in compliance with the EB-5 statutory, regulatory and precedent decision framework. (Emphasis in text.)

As of August 3, 2015, USCIS had approved approximately 697 regional centers. Regional centers can operate in multiple states; thus a regional center may be listed more than once in the USCIS database of the current regional centers.

6 Title and Related Issues

A. Title Insurance

In the United States, it is customary for the transferee of legal title to real estate (or the mortgage lender under a U.S. mortgage) to obtain title insurance. Title and related issues are, generally, not significant in connection with investments in U.S. real estate by foreign investors, i.e., the same considerations would apply with respect to investments in U.S. real estate by U.S. investors. The purchaser's title (or lender's mortgagee's lien) is perfected against third parties by recordation of the deed (or the mortgage) in the public records in the state where the property is located. The cost of title insurance is not dependent on the type of deed delivered by the seller (whether the conveyance is by warranty deed, "special" or "limited" warranty deed, or quit-claim deed) or the form of the mortgage or deed of trust prepared by the lender. Because § 1445 of the Internal Revenue Code requires that a transferee of a U.S. real property interest withhold tax if the transferor is a foreign person, the title company customarily will require that the transferor execute a Certification of Nonforeign Status to certify to the transferee (and the title company) that (if such is the case) withholding of tax is not required upon the disposition of a U.S. real property interest by the transferor. The transferor certifies the following: the transferor's address; the transferor's taxpayer identification number; and that the person or entity is not a nonresident alien for purposes of U.S. income taxation. If the transferor is a foreign person (which may include an entity such as an LLC in which foreign persons are investors), then the transferee is required to withhold tax from the sale proceeds in accordance with IRC § 1445.

If the title insurer is relying on an indemnity or guaranty from a foreign individual or entity with respect to a covered matter under the title policy or a special endorsement, or "gap" coverage (for the length of time between closing a transaction and recordation of documents), or in connection with other title-related issues, it should take the necessary precautionary steps set forth in C. below.

See generally, Mayer Brown, *A Brief Legal Guide to Investing in Real Estate in the U.S.*, available at: https://www.mayerbrown.com/files/Publication/c81e9e4a-437e-4b69-9e98-833cacedcc5f/Presentation/PublicationAttachment/191e1235-e696-48be-9168-8616aa32c9ab/A_Brief_Legal_Guide_to_Investing_in_Real_Estate_in_the_US.pdf.

B. Transfer Taxes

Although transfer taxes are imposed on the transfer of real property in the United States by many states, as well as by many counties and municipalities, this does not normally present any special issues with respect to transfers by foreign persons or entities, as the tax is imposed on the stated consideration in the deed or on the value of the property. While the payment of such obligations may be dictated by state and local law with respect to which party is liable for payment, in many locations the parties are jointly and severally liable, and the parties can follow the custom and practice in the location or negotiate payment of the transfer-tax obligation.

For income-tax purposes, the nexus for U.S. transfer taxes is the site of the property (obviously in the United States). The stock of a foreign corporation has a foreign situs, even if the foreign corporation owns only U.S. real estate and the shareholder is not treated as owning any part of the real estate assets. Under the aggregate theory of partnerships, U.S. assets held by a partnership will be treated as owned by the partners under the “look through rule,” regardless of the nationality of the partnership. Thus a foreign partnership conducting a U.S. trade or business would be deemed to have a U.S. situs. The same reasoning may apply under the “look-through rule” to a trust interest.

C. Indemnification

If, in connection with a real-estate transaction involving foreign investment in U.S. real estate, a party seeks an indemnity or guaranty covering certain defined risks or obligations from a foreign person(s) or entity, certain additional steps should (to the extent possible subject to negotiating strength and the size of the transaction) be taken to ensure that the indemnitor or guarantor will be able to enforce, and collect under, the indemnity or guaranty if the need to do so arises. The legal identity and financial strength of the indemnitor or guarantor must be carefully evaluated and analyzed, and if possible the indemnitor or guarantor should be required to provide detailed current audited financial statements (that comply with or are similar to U.S. GAAP accounting standards), preferably on at least a quarterly basis. Also, the indemnitor or guarantor should consent to jurisdiction in the United States in the state where the real property is located, and the indemnity or guaranty agreement should provide that applicable U.S. and state law apply to the validity and enforceability of the indemnity or guaranty agreement, which should be stated in U.S. dollars. Furthermore, any judgment that is obtained against the indemnitor or guarantor (including collection costs and attorney’s fees) should be enforceable and collectible in the country where the indemnitor or guarantor is located, or else an enforceable international arbitration clause should be included in the indemnity or guaranty agreement. The indemnity or guaranty agreement should also provide for notice and service of process on a designated individual in the state where the property is located (as an extra precaution, the Secretary of State of the state where the property is located could also be designated as a party to accept service or process on behalf of the indemnitor or guarantor). (In recent years, some institutional mortgage lenders have attached a “Foreclosure Rider” to a mortgage given by foreign individual or entity. The rider appoints a specific domestic individual to receive service of process.)

A corporate indemnitor or guarantor should provide proof that it has duly authorized the corporate action through appropriate corporate resolutions and provide a certificate of incumbency (or similar documentation) as proof that each signatory is authorized to bind the corporation. If possible, an attorney’s opinion should be obtained from the indemnitor’s or guarantor’s legal counsel confirming that a U.S. judgment against the indemnitor or guarantor will be enforceable in the foreign jurisdiction. Different jurisdictions can have vastly different requirements and rules regarding contracting and entering into indemnification agreements and guaranties, and the indemnified party or beneficiary of the guaranty would be wise to consider consulting with an attorney in the indemnitor’s or guarantor’s country with respect to all legal requirements and restrictions that would affect the validity and enforceability of the indemnity or guaranty agreement. If all or most of the foregoing suggested requirements cannot be obtained from the indemnitor or guarantor because of lack of bargaining or negotiating strength (or for other reasons), consideration should be given to requiring the indemnity or guaranty to be obtained from a subsidiary of a foreign corporate entity in good standing in the United States, or a U.S. individual with satisfactory and demonstrable net worth to support the indemnity or guaranty.

See generally Pamela Westhoff, Charles Donovan and Lydia Lake, *Commercial Lease Guaranties From Foreign Entities: What You Need to Know to Safeguard Your Security*, Real Estate, Land Use and Environmental Law Blog, Sheppard Mullin (July 28, 2015), available at: <http://www.realestatelanduseandenvironmentallaw.com/commercial-lease-guaranties-from-foreign-entities-what-you-need-to-know-to-safeguard-your-security.html>.

D. Notarization

With the increase in foreign investment in U.S. real estate, it may be necessary for a deed, power of attorney, or even a mortgage to be notarized in a foreign country. Although foreign notarizations generally have not been accepted in the United States, notarization can be performed at the American Consulate in the foreign country where the person or entity is domiciled or as the result of an “apostille” in which the signing party is physically located. The literal meaning of apostille is certification (which comes from French). An apostille is a form of authentication issued to documents for use in countries that participate in the Hague Convention of 1961, a treaty among over 100 countries (including the United States) that allows public documents issued in one country to be accepted in another. (A list of countries that accept apostilles is provided by the US State Department.)

The apostille is not a person and it is not something that a foreign notary or US notary provide themselves. If a document is notarized in a foreign country, the notary signs, dates and stamps it similarly as to how it is done in the US (although sometimes notary may put ribbons, etc., on it to attach or bind to the document). If it is to be sent out of that country then either the client or the notary may send the notarized document to the relevant authority for that nation or jurisdiction for an apostille. The apostille is a card that simply confirms that the notary is in fact a notary of that jurisdiction or nation. The notary will not be able to produce an apostille, as he or she doesn’t sign or otherwise make them. The cost of an apostille is not inexpensive; in some countries the fee is a percentage of the sales price of the property

If the country of intended use does not participate in the Hague Convention, documents being sent to that country generally can be “authenticated” or “certified.” Notarizing officers at any U.S. Embassy or Consulate abroad can provide a service similar to the functions of a notary public in the United States. Also, a Canadian notary is accepted in the United States, and it is also possible to have a document notarized by a local foreign notary and then have the document authenticated for use in the United States. Florida has a statute, F.S.A. § 695.03, which provides that a Florida “civil law notary” may affix his or her seal to the document in a foreign jurisdiction, which will then be deemed proof of the execution of the document or deed in full compliance with that jurisdiction. The statute states that “All affidavits, legalizations, authentications, and acknowledgments heretofore made or taken in the manner set forth above are hereby validated.” See F.S.A. § 695.03(3), which states that:

If the acknowledgment, legalization, authentication, or proof is made in a foreign country, it may be made before a commissioner of deeds appointed by the Governor of this state to act in such country; before a notary public of such foreign country or a civil-law notary of this state or of such foreign country who has an official seal; before an ambassador, envoy extraordinary, minister plenipotentiary, minister, commissioner, charge d’affaires, consul general, consul, vice consul, consular agent, or other diplomatic or consular officer of the United States appointed to reside in such country; or before a military or naval officer authorized by the Laws or Articles of War of the United States to perform the duties of notary public, and the certificate of acknowledgment, legalization, authentication, or proof must be under the seal of the officer. A certificate legalizing or authenticating the signature of a person executing an instrument concerning real property and to which a civil-law notary or notary public of that country has affixed her or his official seal is sufficient as an acknowledgment. For the purposes of this section, the term “civil-law notary” means a civil-law notary as defined in chapter 118 or an official of a foreign country who has an official seal and who is authorized to make legal or lawful the execution of any document in that jurisdiction, in which jurisdiction the affixing of her or his official seal is deemed proof of the execution of the document or deed in full compliance with the laws of that jurisdiction.

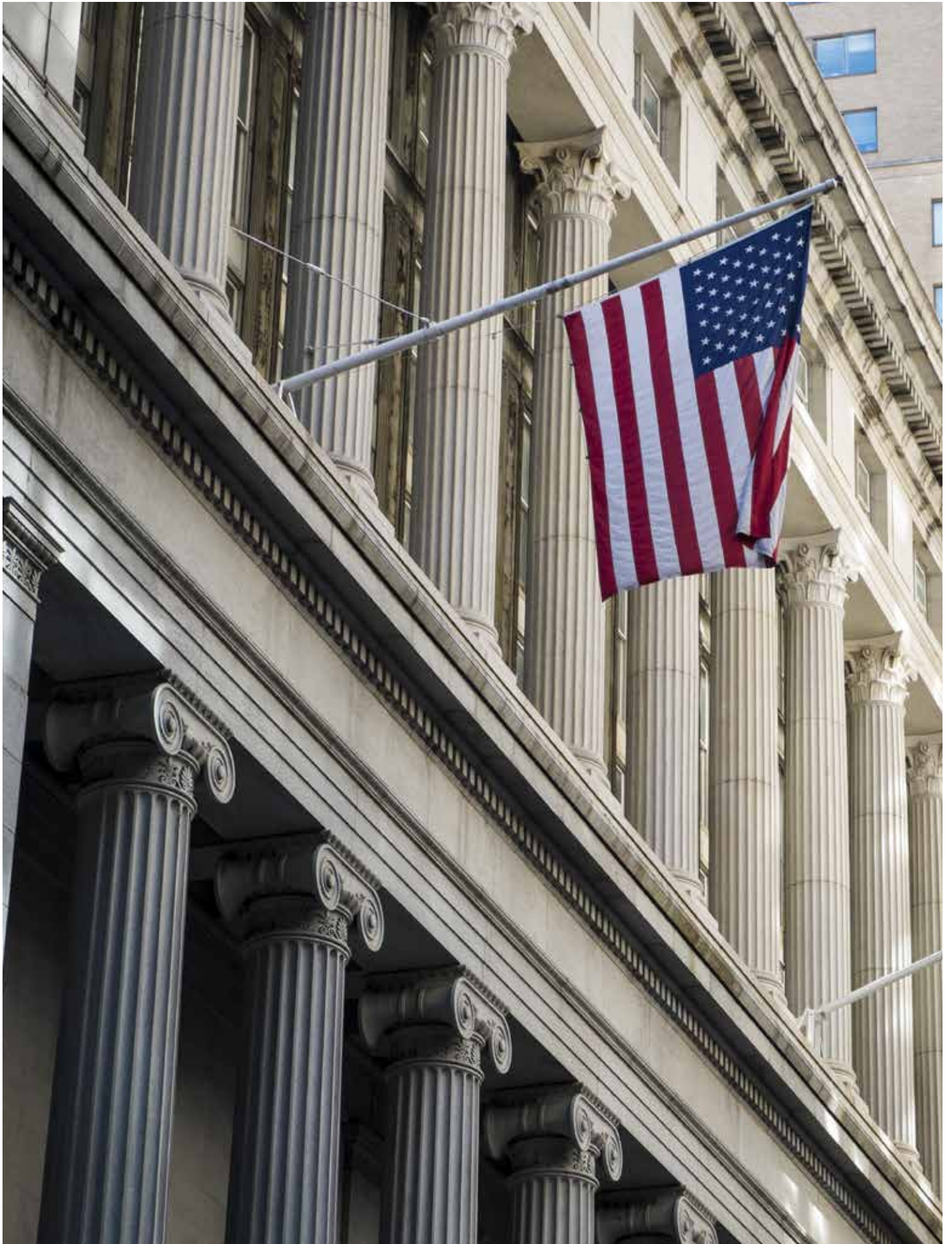


EXHIBIT A

Sample Mortgage Provisions (Anti-Terrorism)

_____. Prohibited Person: Any person or entity that (i) is specifically named or listed in, or otherwise subject to, any Anti-Terrorism Laws, (ii) is owned or controlled by, or acting for or on behalf of any person or entity specifically named or listed in, or otherwise subject to, any Anti-Terrorism Laws, (iii) Mortgagee is prohibited from dealing with, or engaging in any transaction with, pursuant to any Anti-Terrorism Laws, or (iv) is affiliated with any person or entity described in clauses (i) to (iii) of this definition.

_____. Prohibited Person Compliance: Mortgagor acknowledges and understands that Mortgagee may be required, and hereby authorizes Mortgagee, to obtain, verify and record information that identifies Mortgagor, each Constituent Party and/or Guarantor, which information may include the names and addresses of such parties and other information that will allow Mortgagee to identify such parties in accordance with the requirements of certain Anti-Terrorism Laws.

Alternative Sample Mortgage Provisions (Anti-Terrorism)

_____. Anti-Terrorism Regulations.

Neither Mortgagor, any affiliate of Mortgagor, nor any person owning an interest in either of the foregoing is a “Specially Designated National” or a “Blocked Person” as those terms are defined in the Office of Foreign Asset Control Regulations, 31 C.F.R. Pt. 500.

_____. Prohibited Person Compliance.

Mortgagor warrants, represents, and covenants that neither Mortgagor, any guarantor, nor any of their respective affiliated entities is or will be an entity or person (i) that is listed in the Annex to or is otherwise subject to the provisions of Executive Order 13,224, issued on September 24, 2001 (Exec. Order No. 13224); (ii) whose name appears on the United States Treasury Department's Office of Foreign Assets Control's (OFAC) most current list of “Specially Designated National and Blocked Persons” (which list may be published from time-to-time in various mediums including, but not limited to, the OFAC website, www.treas.gov/ofac/t11sdn.pdf); (iii) who commits, threatens to commit, or supports “terrorism,” as that term is defined in Exec. Order No. 13,224; or (iv) who is otherwise affiliated with any entity or person listed above (any and all parties or persons described in items (i) to (iv) above are referred to in this Mortgage as a “Prohibited Person”). Mortgagor agrees that neither Mortgagor, nor any guarantor nor any of their respective affiliated entities, will knowingly (i) conduct any business, nor engage in any transaction or dealing, with any Prohibited Person, including but not limited to the making or receiving of any contribution of funds, goods, or services to or for the benefit of a Prohibited Person; or (ii) engage in or

conspire to engage in any transaction that evades or avoids, has the purpose of evading or avoiding, or attempts to violate any of the prohibitions set forth in Exec. Order No. 13,224. Mortgagor further agrees to deliver (from time-to-time) to Mortgagee any such certification or other evidence as may be requested by Mortgagee in its sole and absolute discretion, confirming that, to the best of Mortgagor's knowledge, (i) neither Mortgagor nor any guarantor is a Prohibited Person and (ii) neither Mortgagor nor any guarantor has engaged in any business, transaction, or dealings with a Prohibited Person, including but not limited to the making or receiving of any contribution of funds, goods, or services to or for the benefit of a Prohibited Person.

Sample Lease Provisions (Anti-Terrorism)

____. Compliance with the USA Patriot Act.

Tenant is not, as of the date hereof: (a) conducting any business or engaging in any transaction or dealing with any Prohibited Person, including the making or receiving of any contribution of funds, goods or services to or for the benefit of any Prohibited Person; (b) dealing in, or otherwise engaging in any transaction relating to, any property or interests in property blocked pursuant to Executive Order No. 13224; or (c) engaging in or conspiring to engage in any transaction that evades or avoids, or has the purpose of evading or avoiding, or attempts to violate any of the prohibitions set forth in, any Anti-Terrorism Law. Neither Tenant nor any of its affiliates, officers, directors, shareholders, members or lease guarantor, as applicable, is a Prohibited Person.

____. Tenant's Representations and Warranties.

Tenant hereby makes the following representations and warranties, each of which is material and being relied upon by Landlord, is true in all respects as of the date of this Lease, and will survive the expiration or termination of this Lease. Tenant will re-certify such representations and warranties to Landlord periodically, upon Landlord's reasonable request.

(a) Tenant is not in violation of any Anti-Terrorism Law.

(b) Tenant is not as of the Effective Date: (i) conducting any business or engaging in any transaction or dealing with any Prohibited Person, including the making or receiving of any contribution of funds, goods or services to or for the benefit of any Prohibited Person; (ii) dealing in, or otherwise engaging in any transaction relating to, any property or interests in property blocked pursuant to Executive Order No. 13224; or (iii) engaging in or conspiring to engage in any transaction that evades or avoids, or has the purpose of evading or avoiding, or attempts to violate any of the prohibitions set forth in any Anti-Terrorism Law.

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