Stop Beating that Dead Horse: THE Premier EB-5 Franchise-Based Regional Center Proposal was Overwhelmingly Inadequate and was Denied in 2010

By Joseph P. Whalen (October 3, 2013)

The Non Precedent AAO Decision found at **Nov162010_03K1610.pdf** , attempted to justify the designation a Regional Center in Southern California submitted by some sort of an investment "professional" who wanted to help pair immigrant investors with franchise offers. Many of these deals would have cost less than the bare minimum $500,000 EB-5 investment and none would support sufficient job creation to meet EB-5 requirements, even with reasonably calculated "EB-5 indirect jobs". I previously wrote about this case beginning in September 2012, when it was first posted, and followed up with another article in October 2012, and finally consolidated those articles and the AAO Decision in April 2013. Previous articles were written in order to point out how extremely bad math skills; joined with poor selection of data for inputs, no grasp of the use of an economic model, and a really bad business concept for EB-5, lead to nothing but disastrous results.

To set the stage for the current topic, I include some excerpts from the above linked decision. This article shall endeavor to illustrate the virtual uselessness of franchises for Regional Center concepts, and, let's face it; they usually stink for an EB-5 direct or stand-alone investment as well.[1]

> "The director determined that the applicant had not established that the proposed projects would benefit the regional center as a whole,[2] had not provided a sufficient economic analysis that explained how the invested funds would create jobs and had not explained how the $30,000 balance in the regional center's account would cover the initial costs.
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> On appeal, the applicant submits a new analysis and evidence that the regional center now has a bank balance of $230,096.78. For the reasons discussed below, the applicant has not overcome all of the director's concerns especially as the direct employment projection for the **Holiday Inn Express** lacks credibility. In addition, a review of the proposed limited partnership agreement reveals a term that is problematic.

[1] Granted, on a rare occasion, under the perfect set of circumstances, the RIGHT franchise might work for EB-5 such as a Reb Lobster, Olive Garden, certain retail outlets, or nearly anything at a major international airport that is open 24/7. However, probably all or nearly all of such ideal locations are already taken!

[2] Highlighting added throughout for emphasis.

An application or petition that fails to comply with the technical requirements of the law may be denied by the AAO even if the Service Center does not identify all of the grounds for denial in the initial decision. *See Spencer Enterprises, Inc. v. United States*, 229 F. Supp. 2d 1025, 1043 (E.D. Cal. 2001), *aff'd*, 345 F.3d 683 (9th Cir. 2003); *see also Soltane v. DOJ*, 381 F.3d 143, 145 (3d Cir. 2004) (noting that the AAO conducts appellate review on a *de novo* basis)." At p. 2

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"Table 14 purports to reflect the amount of an investment required in each sub industry to create the necessary employment. It does not identify any specific franchise that would actually require an investment of this amount. Thus, the plan does not explain how the regional center would locate franchises requiring the large investments identified in Table 14. We reiterate that most of the franchises identified in the plan require an investment of less than $500,000 and very few require an investment of $1 ,000,000 or more. The plan also fails to explain how the limited partnerships investing in the regional center would invest in these small-scale franchises. A limited partnership pooling at least two investors' investments, for example, could not invest in a single $500,000 franchise investment. As the regional center plan appears to rely on the eventual investment in several small-scale franchises, it is significant that the plan lacks any explanation as to who will manage these individual franchises. For example, the plan fails to explain whether the limited partnerships investing in the regional center would own each franchise and secure a manager or merely loan capital to individuals interested in starting a franchise. If the latter, the regional center must not only have a plan for marketing the regional center to potential investors, but also to potential franchise owners." At p. 6

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"........ In response to the director's request for additional evidence, the applicant submitted an Updated Economic Analysis and Job Creation Report for the regional center. Rather than addressing 26 sub industries, this plan focuses on four industries: automotive repair and maintenance, real estate agencies, home health care and dining. The plan lists the franchise fees for several franchises in these industries but does not project what the actual investment costs would be. The plan then discusses a potential investment in a **Holiday Inn Express**, which does not fall under any of the four industries identified. On page 18, the plan states:

> The size of the proposed hotel is 63,080 square feet. According to the U.S. Department of Energy and its Energy Information Administration's 2003 Commercial Buildings Energy Conservation Survey: Table B 1 [footnote with website address omitted], the mean square feet per worker for lodging are 2,074. This means that the 63,080 square foot hotel would support 30.4 employees each of whom work an average of 167 hours per week. Thus the total number of direct employees that would be needed for the hotel are 145.9 (= 30.4 x 4.8).

The plan then uses this direct employee number to calculate indirect and induced jobs. Specifically, the plan multiplies 145.9 by the IMPLAN Type III employment multiplier for hotels of 1.43 to conclude that the Holiday Inn Express would create a total of 208.6 jobs through direct, indirect and induced employment.

We accessed the chart referenced in the plan, prepared by the Department of Energy (DOE), at http://www.eia.doe.gov/emeu/cbecs/cbecs2003/detailed tables 2003/2003set1/2003excellbl.xls on November 12, 2010 and incorporated it into the record of proceeding. It includes the following information regarding lodging:"[3]

Table B1. Summary Table: Total and Means of Floorspace, Number of Workers, and Hours of Operation for Non-Mall Buildings, 2003

	Number of Buildings (thousand)	Total Floorspace (million square feet)	Total Workers in All Buildings (thousand)	Mean Square Feet per Building (thousand)	Mean Square Feet per Worker	Mean Hours per Week
All Buildings*................................	4,645	64,783	72,807	13.9	890	61
Lodging	142	5,096	2,457	35.8	2,074	167

At pp. 6-7

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"The director concluded that this plan still did not adequately explain the projected impact on the regional center as a whole rather than county by county. The director also concluded that the plan for the Holiday Inn Express was "scattered" and that the remaining plan was too generic and lacked an explanation as to how the limited partnerships would invest their funds." At P. 8

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Finally, while not addressed by the director, the proposed limited partnership agreement contains a problematic term. Specifically, section 3(b) of the agreement allows limited partners to contribute "services." The regulation at 8 C.F.R. § 204.6(e) defines capital as "cash, equipment, inventory, other tangible property, cash equivalents" and certain indebtedness. The regulation at 8 C.F.R. § 204.6(j)(2) does not allow [a] [*sic*] qualifying investor pursuant to section 203(b)(5) of the Act to establish an investment through the contribution of services. At p. 10

I would add to the above remark as to the investor's "services" that the investor and the immediate nuclear family members: spouse, sons and daughters (of any age); simply don't count and would likely prevent achieving the minimum of ten (10) full-time jobs for qualifying U.S. workers. Study the EB-5 requirements or just stay out of it completely. Also, real estate agents should stick to their usual tasks, NOT EB-5.

That's my two-cents, for now.

[3] This subject matter is covered in a previous article, see it via the "April 2013" hyperlink on page one.