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VISAS-FOR-DOLLARS PROGRAM A BOON TO HOTEL DEVELOPERS

By Janet Morrissey
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When Marriott International wanted to open a new hotel in downtown Seattle, the company's developers didn't sell bonds, take out a mortgage or tap other traditional forms of financing for the $88 million project. Instead, it raised the bulk of the money from wealthy immigrants who wanted a green card.

A government program, which grants so-called EB-5 visas to foreigners who invest at least $500,000 in an American business, is now a popular source of financing for new Marriott hotels. Since the Seattle deal in 2008, the company has endorsed 14 projects that use EB-5 financing, including the downtown Milwaukee Marriott, a Courtyard Marriott in Midtown Manhattan and a $168 million hotel near the Staples Center in Los Angeles.

"It's created liquidity in a relatively illiquid market," said Anthony Capuano, the chief development officer at Marriott.

The EB-5 program has been around since 1990, but small hotel developers started flocking to it in the aftermath of the financial crisis of 2008. They didn't have much choice. With the economy in tatters and the travel market tanking, many projects stalled or were canceled altogether when financing evaporated. Even now as the industry fundamentals improve and room occupancy rates rise, money is hard to come by – expensive for some, nonexistent for others.

The federal government offers an alternative. Under the Citizenship and Immigration Services' Immigrant Investor Program, foreigners can obtain EB-5 visas – essentially temporary residency status – by investing $1 million, or $500,000 in high unemployment areas, in a commercial venture that generates 10 jobs over two years.

It has proved to be a relatively cheap source of financing. Hotel developers can raise money through the EB-5 program by offering returns of less than 4 percent. In contrast, the interest rates on debt starts at 6 percent, with some riskier forms of financing running at 10 percent or higher. Investors who take an equity stake in a hotel project aim for returns of 20 percent.

"Foreigners are buying visas and are much less concerned about the rate of return they earn on their investment," said David Loeb, a senior analyst at Robert W. Baird.

Despite the potential advantages, big industry players were reticent at first. Many dismissed it as a marginal program for questionable projects that couldn't get financing any other way. They also wondered how developers could round up 200 investors to pay for a $100 million project.

"We would go to conferences and talk about the program, and people just didn't believe it was real – they didn't believe you could raise that much money," said Catherine D. Holmes, partner at the law firm Jeffer Mangels Butler & Mitchell. Once Marriott was in the picture, “people started to take it more seriously,” said Ms. Holmes, whose firm is helping clients use EB-5 financing for 40 different hotel projects.

Over the last 18 months, developers for Hilton Worldwide, Hyatt Hotels and Starwood Hotels & Resorts Worldwide have turned to EB-5 financing. In July, FelCor Lodging Trust announced plans to raise $45 million through EB-5 financing as part of its planned $230 million redevelopment of the Knickerbocker Hotel in Times Square. Sam Nazarian, the hospitality magnate known for his celebrity-packed hotels, restaurants and nightclubs in Los Angeles, plans to build the first SLS hotel in New York with EB-5 money.

“It’s a method of financing that’s current, available and very credible,” said Craig Mance, Hilton’s senior vice president for development for North America “It’s helping deals move forward.” Hilton has 10 projects relying on EB-5 financing.

EB-5 financing has been a boon to development broadly.

So far this year, the government has issued 3,002 temporary visas through the program, up from 640 in 2008. Most have gone to Chinese immigrants, with a number handed out to investors in Britain, India, the Netherlands and South Korea.

Developers often work with so-called regional centers, federally approved organizations that help them draw up business plans and recruit potential investors.

While the regional center program is slated to end on Sept. 30, the Senate approved a bill to extend it for three years. It is expected to pass Congress, although a date has not been set for the vote in the House.

The program has been a good fit for hotels, which create direct jobs – desk people, housekeepers and managers – as well as indirect employment for the companies providing towels and other supplies. “Hotels are 24-hour-a-day, 365-day businesses,” said Mr. Capuano of Marriott. “They’re ideal for driving job growth.”

Marriott’s 377-room hotel under construction in Los Angeles is estimated to generate 4,240 direct and indirect jobs by 2016, above its EB-5 goal of 3,360. The developers benefit in part from the hotel’s proximity to the Staples Center, which houses four professional sports teams; Marriott guests are expected to help drive the sales of tickets and team souvenirs. The project even gets a boost from the jumbo electronic billboard outside the hotel, which should lead to jobs for advertising, marketing and leasing the sign.

“The idea is that more money in the economy equates to more jobs,” said Henry Liebman, the president of American Life, a regional center that worked with Marriott’s developers.

The program has had its share of problems. It was suspended from 1998 to 2003 over complaints of fraud and corruption, according to the government agency that oversees that program. In some cases, a foreign investor would commit money with a promissory note, then never hand over the cash. There were also cases where middlemen would siphon off cash, leaving little for the developers. Other times, developers took the cash but never built the project.

“There were some issues with investors trying to circumvent the capital and job-creation requirements,” said Claire Nicholson, a spokeswoman for Citizenship and Immigration Services.

The government has worked to clean up the program. Investors are now required to pay the full amount upfront and any fees to middlemen must be paid separately.

“We’re committed to ensuring the program achieves its job creation mission efficiently and effectively,” Ms. Nicholson said.

As Marriott and other big hoteliers have jumped on board, they have also helped improve the credibility of the program, according to industry players.

The hotel companies closely analyze each project, whether or not they use EB-5 financing. They want to ensure the hotel meets brand standards and the debt levels are manageable.

“If someone tells me they’ve got a $10 million project and they’ve got $10.5 million in debt, that’s a project that I’m going to question because it’s overleveraged,” Mr. Mance of Hilton said. It’s up to the developers and the regional centers to ensure the project meets the EB-5 requirements.

Even after traditional financing comes back significantly, Marriott, Hilton and others say they are likely to continue using the EB-5 program. It’s relatively cheap and stable, and it complements other financing sources. Said Mr. Mance: “If it works, why not use it again?”