

# Show Me the Money: Proving Lawful Source of Funds for EB-5 Immigrant Investors

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## Introduction

Seeking classification as an immigrant investor under the employment-based fifth preference category (EB-5) carries a heavy evidentiary burden. Much of this burden derives not from the statute or regulations, but from Administrative Appeals Office (AAO) decisions. Drawing on a quartet of 1998 precedent decisions,[1] the AAO has demanded a much more stringent burden of proof than the EB-5 regulations seem to require. This is particularly true concerning proving the lawful source of the petitioner's funds for a qualified investment. Almost all recent nonprecedent AAO EB-5 decisions have dealt with this requirement. In almost every case, the appeal has been dismissed with the same language: "the petitioner has failed to demonstrate a qualifying investment of lawfully obtained funds." [2]

This article summarizes 17 recent nonprecedent AAO EB-5 decisions. All of the cases were decided in 2004 or 2005. The decisions indicate the AAO's focus on requiring comprehensive and effective documentation in EB-5 cases. Where the source of funds is at issue, the AAO describes its emphasis as finding the "path" of funds from source to investment in the enterprise. Detection of a "pattern of income" from evidentiary submission is also a primary AAO preoccupation. Practitioners who note and follow these trends will be more likely to gain EB-5 status for their clients.

## The EB-5 Classification: General Requirements

To qualify for EB-5 classification a foreign investor must: have invested at least \$1 million (or at least \$500,000 if investing in a "targeted employment area") in a new commercial enterprise. The new company must benefit the U.S. economy and create full-time jobs for at least 10 U.S. workers. Moreover, the investor must have at least a policy-making role in the enterprise.[3] The investor must also prove that he or she "has invested or is actively in the process of investing lawfully obtained capital." [4] Most unsuccessful EB-5 applicants trip up on this last requirement.

The AAO's 1998 four precedent EB-5 decisions established a high standard for proving lawful source of funds. The four decisions addressed many issues concerning investment funds, ranging from the legality of funds obtained by loan [5] to the legality of loaning investment funds to the enterprise with the expectation of redemption later. [6] The AAO also created new procedural rules for proving the legality of funds.

Of the 17 AAO decisions reviewed for this article, [7] the AAO ruled in favor of the EB-5 petitioner in just one instance, [8] and remanded one case. [9] In the other 15 cases the AAO dismissed the appeal. All of the denials dealt in whole or in part on the petitioner's inability to meet evidentiary requirements for source of funds. Thus, a discussion of the requirements for proving source of funds is in order.

## Source of Funds: Regulatory Provisions

8 C.F.R. § 204.6(e) defines "capital" to include "cash, equipment, inventory, other tangible property, cash equivalents, and indebtedness." The regulations allow funds obtained by loan, but only for "indebtedness secured by assets owned by the alien entrepreneur, provided that the alien entrepreneur is personally and primarily liable and that the assets of the new commercial enterprise upon which the petition is based are not used to secure any of the indebtedness." [10] The regulations prohibit the use of "assets acquired, directly or indirectly, by unlawful means (such as criminal activities)." [11]

The AAO distinguishes between proving the "source" of funds and proving lawful investment of the funds. This distinction flows from 8 C.F.R. § 204.6(j), which separately presents requirements for documenting a petitioner's investments [12] and the legal acquisition of the investment funds. [13]

8 C.F.R. § 204.6(j)(3) lists the documentation required to prove the lawfulness of funds used in EB-5 cases:

- \* Foreign business registration records;
- \* Corporate, partnership (or any other entity in any form which has filed in any country or subdivision thereof any return described in this subpart), and personal tax returns including income, franchise, property (whether real, personal, or intangible), or any other tax returns of any kind filed within five years, with any taxing jurisdiction in or outside the United States by or on behalf of the petitioner;
- \* Evidence identifying any other source(s) of capital; or
- \* Certified copies of any judgments or evidence of all pending governmental civil or criminal actions, governmental administrative proceedings, and any private civil actions (pending or otherwise) involving monetary judgments against the petitioner from any court in or outside the United States within the past fifteen years. [14]

Recent AAO nonprecedent EB-5 decisions have reinforced the importance of documentary evidence for both investments and source of funds. The AAO has consistently held statements on record without documentary support as being deficient and ultimately unpersuasive. [15] Yet most notably with source of funds, the AAO has expanded on the regulatory requirements, treating them as necessary but not sufficient for EB-5 purposes. The specific ways in which the AAO has expanded this burden warrant analysis. We start by reviewing the four 1998 EB-5 precedent decisions.

### **The Four EB-5 1998 Precedents**

One trend in recent AAO EB-5 decisions is their focus on documenting the "path of funds" from source to investment. In *Matter of Izummi* [16] the immigration agency set the standard upon which the AAO would build in future years. *Izummi* explained that without documentation of the path of funds, a petitioner cannot meet the burden of establishing that the investment funds belong to the petitioner. [17] In *Izummi* the petitioner's level of income was at question. The decision held that the petitioner failed to document his level of income. [18] The decision also admonished the petitioner for the lack of wire-transfer funds on record. [19]

In *Matter of Soffici*, [20] the immigration agency held that the source of funds lent to a petitioner was not adequately documented. The AAO sought out sales contracts for capital raised through sale of real property, and the deed or contract establishing new ownership of this property. The AAO cited a lack of wire-transfer statements as being particularly detrimental to establishing a path of funds from the real estate sale to the petitioner's EB-5 investment. [21] While 8 C.F.R. § 204.6(j)(3) does not explicitly require sales contracts for real estate sales, the AAO held that such documentation was pertinent to establishing the petitioner's sources as part of a path. Without such evidence, the AAO held that it could not determine the true ownership of these funds.

*Matter of Ho* [22] extended these requirements to a different fact pattern. Seeking to lease a commercial office space for a wholesale importing operation, the EB-5 petitioner provided bank account statements and personal letters indicating investments. The immigration agency was not satisfied. The AAO decision cited lack of "evidence of his having engaged in [his] occupation" and lack of income tax or income-verifying statements. [23] Interestingly, Mr. Ho did include wire-transfer statements between accounts, but did not provide certain account statements.

*Matter of Hsiung*, [24] the fourth precedent 1998 EB-5 decision, addressed the legality of investments themselves in addition to the source of the funds. At issue was whether the investment made by the petitioner was truly "at risk." The AAO restricted the use of indebtedness as a form of capital by raising the bar for proving the legality of a loan. Hsiung states that a promissory note secured by assets owned by a petitioner can constitute capital under 8 C.F.R. § 204.6(e) only if: (1) the assets are specifically identified as securing the note; (2) the security interests in the note are perfected in the jurisdiction in which the assets are located; (3) the assets are fully amenable to seizure by a U.S. note holder; and (4) the assets have an adequate fair market value. [25]

### **Recent AAO Trends in Proving EB-5 Source of Funds**

The documentary burden on petitioners in post-1998 AAO EB-5 decisions can be best characterized by "hypertechnicality," to use the AAO's own oft-quoted descriptor. [26] The focus on path of funds remains strong in recent AAO EB-5 decisions, as the 1998 precedents have been heavily cited in most decisions. It is particularly useful to examine the extension of the doctrine to ever more specific fact-patterns, and in a more and more hypertechnical fashion. The most valuable information gleaned from these decisions relates to evidentiary requirements.

### **Path of Funds Post-1998**

In some respects, the 1998 precedents have been closely followed and directly applied to new facts. *Matter of Ho* in particular has figured prominently in recent AAO EB-5 decisions. Several of the 17 decisions reviewed for this article repeat Ho's directive demanding more than just bank letters and statements to depict a path of funds. The AAO's boilerplate language on this issue states:

"A petitioner cannot establish the lawful source of funds merely by submitting bank letters or statements documenting the deposit of funds. *Matter of Ho*, 22 I&N Dec. 206, 211 (Comm. 1998); *Matter of Izummi*, supra at 195. Without documentation of the path of the funds, the petitioner cannot meet his burden of establishing that the

funds are his own funds. Id. Simply going on record without supporting documentary evidence is not sufficient for the purpose of meeting the burden of proof in these proceedings. Matter of Treasure Craft of California, 14 I&N Dec. 190 (Reg. Comm. 1972)."[27]

For example, in one case an EB-5 petitioner claimed five real properties and a cash account (holding \$250,000) as the sources of her funds.[28] The petitioner intended to contribute the properties as part of her EB-5 investment. The petitioner submitted a summary of the real estate transactions, tax returns of the enterprise (indicating assets and cash contributions), and numerous single ledger balance reports relating to the purchase of the real property. The investor also provided bank statements (depicting transactional history but lacking account numbers for the account and the depicted transactions), deposit slips, and receipts for the cash investment. Despite this evidence, the AAO affirmed the EB-5 denial. The AAO held that the investor failed to provide sufficient documentation for the sale of the real estate, even though the investor had included accountant letters testifying to the sale.[29]

In another case a pair of investors created "for the benefit of" accounts to fund personal assets into an EB-5 enterprise organized by Interbank.[30] To support their EB-5 petition the investors submitted bank statements, evidence of their income, and evidence that they owned certain real estate. They also provided a computer printout of funds in a personal account.[31] The AAO held the evidence to be insufficient: "[Documentation] reflecting that funds existed in an account at one time is not evidence that those funds constitute the personal investment of the individual identified as the 'for the benefit of' account-holder." [32]

As noted above, 8 C.F.R. § 204.6(j)(3) lists the documentation required to prove the lawfulness of funds used in EB-5 cases. Although the regulation lists these requirements in the disjunctive, meaning that submission of any one type of document should suffice, the AAO routinely requires more. For example, consider the following quote:

"[The petitioner] asserts that the use of the word "or" in the regulation quoted above means that a petitioner need only submit one type of documentation. We cannot agree. The regulation states that the evidence must be submitted 'as applicable.'"[33]

In that case the petitioner, who had invested in a restaurant, initially submitted no documentation asserting the legality of his source of funds. The petitioner argued that as the past recipient of an E-2 treaty investor visa, he was already cleared for approval in the EB-5 immigrant investor category. The AAO disagreed, explaining that approval of a nonimmigrant visa "does not mandate approval of an immigrant visa in a similar classification; especially, as in this case, where the regulatory requirements for the two classifications are significantly different." [34]

On appeal the restaurant investor had submitted a broad range of information, including a certified letter from a professional tax consulting agency attesting to the proceeds from a sale of property, as well as all the tax information for the petitioner for the last six years, proof of all proceeds from sale of prior property being counted toward the investment, documentation of taxes paid on these properties, copies of legal statutes from his home country providing definitional terms and guidance as to foreign business documentation and requirements, and withdrawal/deposit

documentation from all accounts in which all cash came in and left. Despite all this evidence, the AAO dismissed the EB-5 investor's appeal.

### **"Pattern of Income"**

The AAO also looks for a "pattern of income" to justify the EB-5 investment.[35] For example, in one case the EB-5 petitioner had obtained £750,000 by selling property in Britain. As evidence of this sale the petitioner provided the sales contract and several letters from accountants verifying the sale. The AAO nevertheless denied the appeal, noting the absence of a path for the funds into the new enterprise, an absence of significant income in the five years of tax returns filed, and no evidence of "a pattern of income that could account for owning property of [the indicated] value." [36]

The one case where the AAO approved an EB-5 petition on appeal[37] also indicates the extent of AAO expectations on "pattern of income." In that case the petitioner submitted seven years of tax returns. She also submitted letters from every employer for which she had worked over the past 20 years. Each letter confirmed her salary and retirement benefits. A string of savings account deposit slips and statements proving 26 years of income rounded out her package. As the AAO noted, "[w]hile the petitioner has not demonstrated an unusually large income, she has demonstrated a pattern of steady income and 26 years of professional employment that is not inconsistent with the accumulation of \$500,000 at the time of retirement." [38]

### **Proving the Source of Funds Obtained by Loan**

Clearly, it is difficult enough to prove that one's own funds are, indeed, one's own. When the funds are obtained by loan, expect even greater scrutiny. As discussed above, the regulations expressly prohibit using loan money for EB-5 purposes if the loan is obtained by using the new commercial enterprise as security.[39] It does not matter if the loan is from a third party lender or the enterprise itself. In either case the petition will be denied if the loan is secured by the new commercial enterprise.[40]

### **Where Funds Were Obtained Illegally**

The regulations clearly prohibit the use of assets acquired by unlawful means.[41] How does one prove that one's money was lawfully obtained? The AAO has held that criminal background checks alone are not enough to establish the lawful source of funds.[42]

### **Practice Pointers**

Showing the path of an investor's money and the pattern of his or her past income are both important in winning an EB-5 case. In this regard it is helpful to view every dollar in an applicant's portfolio as being tagged, so to speak. Should the AAO seek to track down the tagged fund at any point in time from receipt by the client to eventual investment in the enterprise, this should be made possible through appropriate documentation. Bank statements, account numbers and deposit/withdrawal slips, and any and all wire-transfers between accounts tied to the

investment are important for this tagging purpose. Charts showing both the path of money invested and the pattern of an investor's past income are helpful.

The AAO also wants confirmation that the invested funds are actually being put to use in the enterprise. Articles of organization for the enterprise are essential in proving the existence of the business. However, one should also consider providing supporting letters from accountants, employers, and attorneys, any or all of whom might be able to paint a picture of how the monies are actually being used.

EB-5 petitioners' past income has also been another AAO concern in EB-5 decisions. Income tax records should be submitted, preferably for a period beyond the five years required by the regulations. As a "pattern" of income is the key phrase used by the AAO, also provide savings and personal investment records to prove that even if a petitioner has not earned a substantial annual income, there is a credible claim that the necessary funds were accumulated over time.[43]

Use common sense when considering the myriad potential sources of an EB-5 petitioner's investment income. Where funds are inherited, a will or trust forms are instructive. Where funds are earned from income on an investment, stock certificates, dividend letters, and account statements are vital. Where funds were earned from income on a previous business investment, the corporate tax returns for the business, complete with evidence of payouts to the owners, should be included.

Given the AAO decisions, some may be tempted to include all conceivable documents relating to the petitioner's source of funds in an EB-5 petition, hoping that the sheer mass of documentation will persuade the immigration agency that the money is sufficient and legitimately acquired. Do not yield to this temptation. As the AAO has often reminded losing EB-5 applicants, its review of the source and path of funds is "hypertechnical." [44] Simply submitting more documents in a "kitchen-sink" approach may prompt the immigration agency or the AAO to find fault in one minor transaction and thus deny the whole petition. [45] Instead, organize the petition carefully to show a clear path of funds from the investor to the investment, and the lawful source of those funds. In EB-5 cases as in life, organization is key. To paraphrase William Blake, an EB-5 petition cannot succeed "but in minutely organized particulars." [46]

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[1] 1 Matter of Soffici, 22 I. & N. Dec. 158, 19 Immigr. Rep. B2-25 (Assoc. Comm'r, Examinations 1998); Matter of Izummi, 22 I. & N. Dec. 169, 19 Immigr. Rep. B2-32 (Assoc. Comm'r, Examinations 1998); Matter of Hsiung, 22 I. & N. Dec. 201, 19 Immigr. Rep. B2-106 (Assoc. Comm'r, Examinations 1998); Matter of Ho, 22 I. & N. Dec. 206, 19 Immigr. Rep. B2-99 (Assoc. Comm'r, Examinations 1998).

[2] See, e.g., Matter of [name not provided], EAC-98229-50661 (AAO Jan. 18, 2005) (dismissing EB-5 appeal).

[3] INA § 203(b)(5), 8 USC § 1153(b)(5). See generally Charles Gordon, Stanley Mailman & Stephen Yale-Loehr, *Immigration Law and Procedure* § 39.07 (2006).

[4] 8 C.F.R. § 204.6(j) (emphasis added).

30 Matter of [name not provided], EAC 98 229 50661, Vermont Service Center (AAO Jan. 18, 2005), at 4. The Interbank promoters were eventually convicted of fraud. *United States v. O'Connor*, 158 F. Supp. 2d 697 (E.D. Va. 2001). Individual EB-5 investors in Interbank were victims, not perpetrators, of the fraud.

[5] Matter of Hsiung, 22 I. & N. Dec. 201, 19 Immigr. Rep. B2-106 (Assoc. Comm'r, Examinations 1998).

[6] Matter of Izummi, 22 I. & N. Dec. 169, 175, 19 Immigr. Rep. B2-32 (Assoc. Comm'r, Examinations 1998).

[7] Matter of [name and case number not provided], Vermont Service Center (AAO May 19, 2004); Matter of [name and case number not provided], California Service Center (AAO June 20, 2004); Matter of [name and case number not provided], Texas Service Center (AAO Oct. 2004); Matter of [name not provided], WAC 00 252 53507, California Service Center (AAO Dec. 30, 2004); Matter of [name not provided], EAC 98 229 50661, Vermont Service Center (AAO Jan. 18, 2005); Matter of [name not provided], EAC 98 076 50508, Vermont Service Center (AAO Jan. 18, 2005); Matter of [name and case number not provided], California Service Center (AAO Jan. 18, 2005); Matter of [name not provided], SRC 05 012 50927, Texas Service Center (AAO Feb. 16, 2005); Matter of [name not provided], SRC 98 104 52598, Texas Service Center (AAO Feb. 16, 2005); Matter of [name not provided], WAC 03 095 54561, California Service Center (AAO Mar. 28, 2005); Matter of [name not provided], WAC 00 070 52366, California Service Center (AAO Apr. 21, 2005); Matter of [name not provided], SRC 04 219 50014, Texas Service Center (AAO June 10, 2005); Matter of [name not provided], EAC 98 075 51559, Vermont Service Center (AAO June 14, 2005); Matter of [name not provided], EAC 98 075 51390, Vermont Service Center (AAO June 18, 2005); Matter of [name not provided], SRC 05 004 50875, Texas Service Center (AAO Aug. 25, 2005); Matter of [name not provided], SRC 04 078 52977, Texas Service Center (AAO Oct. 4, 2005); Matter of

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[name not provided], WAC 04 060 53288, California Service Center (AAO Oct. 31, 2005). All of the cases are on file with the authors.

[8] Matter of [name not provided], WAC 00 252 53507, California Service Center (AAO Dec. 30, 2004).

[9] Matter of [name not provided], SRC 05 012 50927, Texas Service Center (AAO Feb. 16, 2005).

[10] 8 C.F.R. § 204.6(e).

[11] Id.

[12] 8 C.F.R. § 204.6(j)(2).

[13] 8 C.F.R. § 204.6(j)(3).

[14] 8 C.F.R. § 204.6(j)(3) (emphasis added).

[15] Matter of Treasure Craft of California, 14 I. & N. Dec. 190 (Reg. Comm'r 1972).

[16] 22 I. & N. Dec. 169, 19 Immigr. Rep. B2-32 (Assoc. Comm'r, Examinations 1998).

[17] Id. at 195.

[18] Id.

[19] Id.

[20] 22 I. & N. Dec. 158, 19 Immigr. Rep. B2-25 (Assoc. Comm'r, Examinations 1998).

[21] Id. at 164-65.

[22] 22 I. & N. Dec. 206, 19 Immigr. Rep. B2-99 (Assoc. Comm'r, Examinations 1998).

[23] Id. at 211.

[24] 22 I. & N. Dec. 201, 19 Immigr. Rep. B2-99 (Assoc. Comm'r, Examinations 1998).

[25] Id. at 202-04.

[26] See, e.g., Matter of [name not provided], EAC 98 076 50508 (AAO Jan. 18, 2005), at 8 ("the 'hypertechnical' requirements for establishing the lawful source of an investor's funds serve a valid government interest: confirming that the funds

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utilized are not of suspect origin.") (citing *Spencer Enterprises v. United States*, 229 F. Supp. 2d 1025, 1040 (E.D. Calif. 2001), *aff'd*, 345 F. 3d. 683 (9th Cir. 2003)).

[27] See, e.g., Matter of [name and case number not provided], Vermont Service Center (AAO May 19, 2004), at 7.

[28] Matter of [name and case number not provided], Texas Service Center (AAO Oct. 2004), at 6.

[29] *Id.*

[30] Matter of [name not provided], EAC 98 229 50661, Vermont Service Center (AAO Jan. 18, 2005), at 4. The Interbank promoters were eventually convicted of fraud. *United States v. O'Connor*, 158 F. Supp. 2d 697 (E.D. Va. 2001). Individual EB-5 investors in Interbank were victims, not perpetrators, of the fraud.

[31] *Id.*

[32] *Id.*

[33] Matter of [name and case number not provided], California Service Center (AAO Jan. 18, 2005), at 5.

[34] *Id.*

[35] 35 See, e.g., Matter of [name and case number not provided], Texas Service Center (AAO Oct. 2004), at 6; Matter of [name not provided], WAC 00 252 53507, California Service Center (AAO Dec. 30, 2004), at 3.

[36] Matter of [name and case number not provided], Texas Service Center (AAO Oct. 2004), at 6.

[37] Matter of [name not provided], WAC 00 252 53507, California Service Center (AAO Dec. 30, 2004).

[38] *Id.* at 3.

[39] 8 C.F.R. § 204.6(e). See, e.g., Matter of [name not provided], EAC 98 076 50508, Vermont Service Center (AAO Jan. 18, 2005) (EB-5 petition denied where petitioner had been required by her lenders to pledge her interest in her enterprise as security for her loan).

[40] Matter of [name and case number not provided], Vermont Service Center (AAO May 19, 2004).

[41] 8 C.F.R. § 204.6(e).

[42] See Matter of [name and case number not provided], Vermont Service Center (AAO May 19, 2004), at 8 ("counsel is not persuasive when she argues that a mere

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criminal background check is sufficient to establish the lawful source of the invested funds."); Matter of [name not provided], EAC 98 229 50661, Vermont Service Center (AAO Jan. 18, 2005), at 5 (same).

[43] Matter of [name not provided], SRC 05 012 50927, Texas Service Center (AAO Feb. 16, 2005), at 5.

[44] See, e.g., Matter of [name not provided], EAC 98 076 50508 (AAO Jan. 18, 2005), at 8 ("the 'hypertechnical' requirements for establishing the lawful source of an investor's funds serve a valid government interest: confirming that the funds utilized are not of suspect origin.") (citing *Spencer Enterprises v. United States*, 229 F. Supp. 2d 1025, 1040 (E.D. Calif. 2001), *aff'd*, 345 F. 3d. 683 (9th Cir. 2003)).

[45] See, e.g., Matter of [name not provided], WAC 03 095 54561, California Service Center (AAO Mar. 28, 2005), at 3-5 (confusing list of investments over a two-year period in a cabinet company constituted one reason why AAO denied the EB-5 appeal); Matter of [name not provided], SRC 98 104 52598, Texas Service Center (AAO Feb. 16, 2005), at 4-9 (confusing list of investments over a five-year period in a small grocery store and deli constituted one reason why AAO denied the EB-5 appeal).

[46] William Blake, *To the Public*, ch. 3, plate 55, line 60, in *Bartlett's Familiar Quotations* 407 (15th ed. 1980).