United States General Accounting Office

GAO

Fact Sheet for the Chairman, Subcommittee on Select Revenue Measures, Committee on Ways and Means, House of Representatives

July 1989

TAX POLICY

Costs Associated With Low Income Housing Tax Credit Partnerships

GAO/GGD-89-100FS

GAO

United States
General Accounting Office
Washington, D.C. 20548

General Government Division

B-137762

July 10, 1989

The Honorable Charles B. Rangel
Chairman, Subcommittee on Select
Revenue Measures
Committee on Ways and Means
House of Representatives

Dear Mr. Rangel:

This report is in response to your April 25, 1989, request asking us to obtain information on the various fees and expenses associated with real estate partnership offerings that use the low income housing tax credit. (See appendix I for definitions of these fees.) Specifically, you were concerned with the proportion of equity financing used for fees and expenses which reduces the amount of equity available for actual construction and rehabilitation of low income housing. You also asked us to examine the fees and expenses of low income housing tax credit partnerships which involve tax exempt 501(c)(3) organizations.

Objectives, Scope, and Methodology

To obtain information on the various fees and expenses, we analyzed published and unpublished data collected by Robert A. Stanger and Company--a recognized source of information on the industry. We reviewed prospectuses and/or summary data for all of the 19 public real estate partnership offerings on the market that use the low income housing tax credit. For comparison purposes, we obtained information on the expenses and fees for the 48 residential or residential/commercial public partnership offerings being marketed that do not use the credit.

We interviewed officers of investment syndication and housing development firms; the Executive Director and General Counsel of the North American Securities Administrators Association, Inc.; and representatives of Robert A. Stanger and Company. Officials from tax exempt 501(c)(3) organizations involved in partnership offerings that use the low income tax credit were also interviewed.

We did our work from April 1989 through June 1989 and in accordance with generally accepted government auditing standards.

Results

The 19 publicly offered partnerships being marketed for low income housing tax credit projects on average use a higher proportion of equity to pay fees and expenses than partnerships for residential and residential/commercial investments. The low income housing partnerships devote an average 27 percent of equity for fees and expenses, while the other types of investments use about 21 percent for this purpose, as shown in appendix II.

According to industry analysts, the proportion of fees and expenses spent by publicly offered low income housing tax credit partnerships are generally within guidelines promulgated by the North American Securities Administrators Association, Inc. (NASAA). Twenty-five states formally or informally follow the NASAA guidelines in regulating these offerings. The guidelines allow a higher proportion of equity to be used for fees and expenses by partnerships carrying higher proportions of debt, such as is generally the case for low income housing partnerships.

The 19 low income housing tax credit partnerships have an average debt of 76.7 percent while the 48 non-low income residential or residential/commercial partnerships carry an average debt of 39 percent. One possible explanation is that the tax credit may provide an incentive to acquire low income housing with relatively less equity and higher debt financing than for housing investments that do not use the credit. The reason for this is that the credit is computed on the total qualified costs of the low income units including debt, not just the equity.

Fees and expenses paid out of equity differ among the 19 publicly offered low income housing tax credit partnerships. The fees and expenses range from 17 percent to 33.8 percent of equity, as shown in appendix III. The residual cost category of "Acquisition Fees to Others" varies the most. According to an industry expert, the cost item of third-party brokerage commissions is an important component responsible for this variation. Some partnerships allow for the use of third party real estate brokers in acquiring properties while others do not. Some business practices cause other differences in acquisition costs. For example, acquiring a greater number of smaller buildings increases the cost of items such as legal and accounting fees.

Comprehensive information on the cost structure of low income housing activities of 501(c)(3) tax exempt organizations is not readily available. We were able to interview two organizations selected by your staff that are involved in partnership offerings for low income housing tax credit investments. They provided information on six partnership offerings. Four of the six partnerships appeared to have fees and expenses as a proportion of equity that were similar to those of the publicly offered partnerships marketing low income housing investments. Two of the six offerings had costs and fees lower than the other offerings. However, there was not sufficient information to account for the differences among fees and expenses.

\- - - - -

We are sending copies of this report to interested parties and will make copies available to others upon request.

The major contributors to this report are listed in appendix IV. If you have any questions concerning this report, please call me on 272-7904.

Sincerely yours,

Paul L. Posner

Paul L. Posner
Associate Director
Tax Policy and Administration
Issues

DEFINITIONS OF TERMS

Front-End Costs - The compensation to the general partner and affiliates for reimbursement of organization and offering costs (including commissions) and maximum allowable acquisition fees and expenses payable to all parties in connection with the purchase of partnership properties or equipment (based on maximum allowable leverage or sponsor estimate), expressed as a percentage of limited partner capital contribution. Front-end costs include the following:

-- Selling Commissions - Includes sales commission paid to broker-dealers in connection with the distribution of the program and all advertising expenses.

-- Organizational and Offering Expenses - Those expenses incurred in connection with and in preparing a partnership for registration and subsequently offering and distributing it to the public.

-- Acquisition Expenses - Those expenses related to selection and acquisition of properties, whether or not acquired. These include but are not limited to legal fees and expenses, travel and communications expenses, costs of appraisals, nonrefundable option payments on property not acquired, accounting fees and expenses, title insurance, and miscellaneous expenses.

-- Acquisition Fees - Fees and commissions paid by any party in connection with the making or investing in mortgage loans or the purchase or development of property by a partnership, except a development fee paid to a person not affiliated with a sponsor in connection with the actual development of a project after acquisition of the land by the partnership.

-- Acquisition Fees to Others - The difference between the fees allowable under NASAA guidelines (or the maximum allowed by the partnership if such a limit is included in the prospectus) and the sum of the front end costs specified in the prospectus. This residual cost category includes acquisition fees paid to a party other than the General Partner or an affiliate such as third party brokerage commissions.

Source: Robert A. Stanger & Company; and North American Securities Administrators Association, Inc., Statement of Policy on Real Estate Programs

TOTAL FRONT-END COSTS[a] AS A SHARE OF THE PARTNERSHIP'S EQUITY

	Low income housing	Other residential	Commercial/ residential
	17.0%	12.5%	13.5%
	17.5	14.5	14.9
	18.0	15.1	16.0
	20.8	17.5	16.5
	22.4	17.8	17.0
	22.5	18.0	17.5
	23.5	18.0	17.9
	23.5	18.8	18.0
	24.0	20.0	18.5
	26.0	20.5	20.0
	30.6	21.6	20.0
	31.4	22.2	20.0
	31.4	22.4	20.0
	32.2	22.5	20.0
	32.2	24.8	20.0
	32.2	26.1	20.2
	32.2	26.5	20.8
	33.0	27.7	21.0
	33.8	30.6	24.0
			24.9
			25.6
			26.0
			26.0
			26.0
			26.5
			26.5
			28.0
			29.8
			30.6
Average[b]	26.5%	20.9%	21.6%
Coefficient of variation[c]	0.216	0.222	0.212

[a]Total front-end costs include the compensation to the general partner and affiliates for reimbursement of organization and offering costs (including commissions) and maximum allowable acquisition fees and expenses payable to all parties.

[b]Unweighted average. Average weighted by program size is 26.1 percent.

[c]The coefficient of variation is the standard deviation divided by the mean.

Source: The Stanger Register, April 1989 and Robert A. Stanger and Co., data as of June 13, 1989.

FRONT-END FEES AND EXPENSES FOR LOW INCOME HOUSING TAX CREDIT PARTNERSHIPS

Program	Total front-end costs	Selling commissions	Offering and organizational costs	Acquisition fees	Acquisition expenses
Historic Housing for Seniors II	17.0%	8.0%	5.0%	2.0%	2.0%
Prudential-Bache Tax Credit Properties	17.5	7.5	3.0	6.5	0.5
Liberty Tax Credit Plus III	18.0	7.5	3.5	6.0	1.0
Burton Tax Credit Partners	20.8	8.0	3.9	5.6	3.3
Qualified Housing Partners	22.4	7.0	1.67	12.25	1.43
Gateway Tax Credit Fund, Ltd.	22.5	8.0	4.0	8.0	0.5
Century Pacific Tax Credit Housing Fund II	23.5	9.0	3.5	8.0	3.0
Boston Capital Tax Credit Fund	23.5	7.0	4.5	10.0	2.0
Community Housing Partners I	24.0	8.0	6.0	6.0	1.0
Diversified Historic Investors VII	26.0	8.0	5.0	10.0	3.0
Willow Wood Housing Credit Fund '88	30.6	9.0	5.0	7.0	3.0
American Tax Credit Properties I	31.4	8.0	4.0	5.0	1.0
Federal Tax Credit Partners	31.4	8.0	3.5	5.0	2.5
Boston Financial Qualified Housing Tax Credits IV	32.2	9.0	4.0	7.5	2.0
Boston Financial Qualified Housing Tax Credits III	32.2	9.0	4.0	7.5	2.0
WNC Housing Tax Credit Fund	32.2	10.0	5.0	12.0	N/A
WNC California Housing Tax Credits	32.2	10.0	3.5	12.0	3.0
AFC-Low Income Housing Credit Partners-I	33.0	9.0	5.0	9.0	3.0
National Tax Credit Partners	33.8	9.5	3.5	6.0	1.0
Average	26.5%	8.4%	4.1%	7.7%	1.9%
Coefficient of variation[b]	0.216	0.105	0.230	0.345	0.544

[a]Greenshoe is the General Partner's option to increase the size of the offering by some fixed amount depending upon market demand.

[b]The coefficient of variation is the standard deviation divided by the mean.

Source: Robert A. Stanger and Company, data as of June 13, 1989.

Acquisition fees to others	Front-end costs net of other acq. fees	Program size (millions)	Greenshoe[a] (millions)	Amount sold (millions)	Authorized debt allowances
0.0%	17.0%	$ 10.0	$10.0	$ 8.6	50%
0.0	17.5	50.0	50.0	0.0	Up to 85
0.0	18.0	100.0	0.0	64.0	Up to 85
0.0	20.8	1.8	0.0	1.5	79
0.0	22.4	15.0	10.0	8.7	50-95
2.0	20.5	20.0	30.0	14.4	Up to 85
0.0	23.5	25.0	50.0	2.4	Up to 95
0.0	23.5	100.0	0.0	62.7	85
3.0	21.0	15.0	10.0	0.35	60-90
0.0	26.0	20.0	20.0	0.0	50-75
6.6	24.0	5.0	2.5	2.4	60-97
13.4	18.0	50.0	50.0	0.0	70
12.4	19.0	30.0	30.0	0.0	50-90
9.7	22.5	60.0	40.0	11.6	60-90
9.7	22.5	40.0	60.0	100.0	60-90
5.2	27.0	7.5	0.0	0.275	60-90
3.7	28.5	10.0	10.0	0.35	60-90
7.0	26.0	10.0	90.0	6.2	80
13.8	20.0	75.0	25.0	0.0	Up to 85
4.6%	22.0%				
1.086	0.149				

MAJOR CONTRIBUTORS TO THIS REPORT

GENERAL GOVERNMENT DIVISION, WASHINGTON, D.C.

Martin S. Morris, Assistant Director
Jerry Ford, Assignment Manager
Carol D. Petersen, Economist-In-Charge
Charles Vehorn, Tax Policy Specialist

(268422)