JAMES A. GRAASKAMP COLLECTION OF TEACHING MATERIALS

V. INDUSTRY SEMINARS AND SPEECHES - SHORT TERM

I. Other Presentations In Which Either The Date And / Or Sponsoring Organization Is Missing

1. Risk Management/Investment Related Topics

s. "Introduction to Limited Partnerships", no date

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Introduction to Limited Partnerships

I. The high capital cost of Real Estate and the potential variance in the time line of development and realization has always lead investors to find methods which would permit group participation to reduce individual cost of entry, reduce maximum loss per venture, and permit diversification of capital, as well as dollar averaging with a series of investments over time.

   A. A ~~R~~real ~~E~~estate development ventures out on the sea of the future of unknown variables much like the fragile sailing ships of old. Marine underwriting began with wealthy investors subscribing to fractional shares of a venture with a maximum potential loss and a proratis are of profits after compensation of the captain and crew with a specific number of shares or front end fees.

   B. The great trading companies of the colonial era were generally open end syndications speculating in land.

   C. The French plan in the 1920's would sell an investment unit of $5,000 consisting of a $2500 mortgage bond, $1500 cullible preferred shares and $1000 of par value common stock. If the building project subceeded it would first amortize the bond, then call the preferred, and ultimately the investor would have a proratishare of a fully paid for property. Thus, he had the benefits of ownership but a preferred position as creditor for half the capital required.

   D. In the 1920's, mortgage bonds were popular investment, many of which went into default in 1930. In subsequent reorganizations the holders of the mortgage bonds became limited participants in the remaining assets and could on occasion take control of the property from the original developer borrower.

   E. In the 1950's, group ownership of real estate began to be popular, particularly partnerships which allowed a single tax conduit treatment. The limited partnership permitted the investor to limit his liability to his initial investment and delegate management decisions to a partner, two desirable characteristics for group ownership not true of a tendency in common.

II. While a few large limited partnerships failed and made headlines, most were organized at local levels involving small groups of people who shared confidence in a single real estate broker or developer. In each state the process is a little diferent, but relatively simple. The complexities are not informing the limited partnership but rather in the difficulties of selling shares within the state and federal blue sky laws.

   A. In order to form a limited partnership under Wisconsin law, all persons desiring to form the partnership shall sign and swear to a certificate of limited partnership. There must be no less than two persons, one, the general partner and one the limited partner.

      1. The certificate must be filed with the register of deeds in the county in which the partnerships principal ~~location~~ place of business is located (Wisconsin stats 179.02 (2))

2. Thus, county records become an excellent prospecting device to identify who in the county is investing in local limited partnerships.

3. If additional partnerships are sold an amended certificate must be filed - thus maintaining constructive notice of the relative responsibilities of investors associated with the project.

B. The certificate must contain the following information (also useful for market intelligence):

1. Name of partnership.
2. Character of business.
3. Location of principal place of business
4. Name and residence of every general and limited partners.
5. Term of partnership.
6. Cash and description of other property contributed.
7. Terms of further contributions obligated to be made.
8. Time that contribution of limited partner is to be returned, if agreed upon.
9. Terms of profit distribution.
10. Terms of substitution by the limited partner of an assignee, if agreed to.
11. The right to admit future limited partners, if agreed to.
12. Terms of priority to contributions or compensation among limited partners.
13. Terms of the continuation of the partnership in the event of the deaths general partner by remaining general partners, if agreed to.
14. The right of the limited partner to receive property other than costs, if agreed to.

Wisconsin Stats. 179.02(a)

C. Wisconsin Stats. 179.24(2) sets forth ten situations when the certificate of limited partnership shall be amended. These ten situations involve a change in either the partnership, the partners, or the financial relationship between the partners. Wisconsin Stats. 179.25(5) requires that the certificate's amendment be filed with the register of deeds.

D. The limited partner does not enjoy absolute protection from additional liability because:

1. If the certificate contains a false statement and an innocent third party relies on that statement to his determent, then the limited partner becomes liable for a proratishare of losses suffered by the third party.

2. If the limited partner makes any decisions of a managerial nature other than a vote to dissolve, replace the general partner for mismanagement, or refinance, the law would then consider him a general partner.

E. Wisconsin statues do not require filing a subscription agreement and there is no requirement to file any limited partnership document with the secretary of state's office in Wisconsin. The incentive for regulation for these agreements is in the penalties inherent in violation of state security regulaations, including the right to put the security back to the promoters for a refund with interest and possibly trouble damages after the project has failed. This is different from a corporation which must file a corporate statement with the Secretary of State each year to remain viable and operational.

III. Syndication in the early 1960's featured either very large, strong identity buildings such as the Empire State building deal or large vacant land speculations in the West.

A. On the East coast, the small investor identified with land marks in his community. One unique venture was Empire State Building Associates.

1. Three general partners sold fractional interests to one set of investors which receive 53% of a defined net profit.

2. A second set of investors bought shares in a collateral trust secured by a 9% mortgage on the building.

3. A third company leased off the building for operations with a complex overage percentage lease. This entity enjoys almost 100% leverage.

4. After the low risk priority mortgage trust receives 9% on the investment, the sponsors receive the next 1,000,000 dollars of revenue. Any profit above this amount is shared 47% with the investors in the participation mortgage trust and 53% to the general partnership sponsor. Roulac reports investors receive cash on cash in excess of 14%.

B. In California, promoters merchandized tracks of land by creating a master plan defining lots for industrial, commercial, residential use.

1. Promoters received a commission of 10% of the acquisition price and another 10% on the eventual sales price of the lots.

2. Raw land was acquired for downpayment consisting of prepaid interests on a non-recourse land contract with interest only payments. High tax bracket investors such as athletes, could deduct the downpayment and the carrying charges so that the net cost was only 30-50% of each dollar.

3. Many of these were for dessert land, but a few firms such as Property Research, Inc. would analyze the rate and direction of urban growth, the schedule for public improvements, and other trends and locate their land purchases to enjoy a significant 5 or 10 year pay-off as Los Angeles and Orange County expanded.

C. In the late 1960's, the emphasis on accelerated depreciation as a tax shelter on earned income became the conventional wisdom. Apartments not only took a great portion of annual housing starts, but the design took a radical change in scale as well. A project might have several hundred units rather than 24 or less and represented a total living environment.