REUTERS

Tax woes drag on Blackstone

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By Emily Chasan

NEW YORK - Blackstone Group LP's initial public offering raised billions of dollars for its employees, but the private equity firm's shares might have performed even better if it weren't for the potential tax headaches, analysts said on Friday.

The company's shares rose 13 percent on their first day of trading on Friday, which is respectable for most IPOs, but paltry for a company as widely hyped as Blackstone.

The $4.13 billion offering was the largest U.S. IPO in five years and the eighth-biggest by a U.S. company ever, excluding overallotments.

Investors are likely concerned about Blackstone's master limited partnership status, which qualifies it for hefty tax breaks, analysts said.

Senators last week introduced bipartisan legislation that would sharply raise taxes for private equity firms that go public. Democrats in the U.S. House of Representatives introduced a similar bill on Friday.

Some investors had expected Blackstone to repeat the performance of Fortress Investment Group, an alternative investment company also structured as a partnership, whose shares rose 68 percent on their first day of trading in February.

But concerns about rising taxes make Blackstone a little harder to swallow.

If the congressional bill is passed Blackstone's maximum federal tax rate could go from 15 percent to the standard corporate rate of 35 percent, and cut into its profits.

And even if the proposed legislation goes nowhere, the tax implications of owning partnership interests may make some investors cringe, said Russ Lundeberg, chief investment officer of Barrett Capital Management in Richmond, Virginia.

Investors have to pay their own taxes on the income they receive from the partnership units they hold in the company. Blackstone already warned in its prospectus that investors should expect to file for a tax extension every year.

"My feeling is most investors are going to be surprised when it comes to tax time," Lundeberg said.

Assuming Blackstone's earnings rise by 20 percent a year it would generate pro forma net economic income of $1.75 billion in 2007. For 2006, that figure was about $1.46 billion.

"Investors may have confidence in Blackstone's ability to make huge amounts of money," said Robert Willens, an accounting and tax analyst at Lehman Brothers in New York.

"But my sense is that people are conceding the fact that there will come a time when Blackstone and Fortress are no longer publicly traded partnerships," he added.

Some investors even suspect that Blackstone's partners' decision to go public now may be linked to their own worries about a rising tax bill.

"At Blackstone you see some really good savvy investors suddenly selling part of their position in the open market," said Drew Kanaly, vice chairman of Kanaly Trust Co., which oversees more than $2 billion in Houston, Texas.

"Maybe they are taking their profits, and maybe they are going to lose their favorable tax treatment down the road, so they want to do it while the tax code is in their favor."