Master Limited Partnerships

An MLP is a publicly-traded limited partnership or limited liability company (also referred to as a "master limited partnership" due to a typical two-tier structure with the publicly-traded partnership holding the partnership interests of lower-tier operating partnerships).

MLP Tax Basics

- Under basic federal income tax concepts, pass-through entities such as partnerships, limited liability companies and certain trusts have historically not been subject to taxation at the entity level but instead the income, gain or loss of such an entity is "passed through" to its entity owners who in turn report their proportionate share of the income, gain or loss on their individual tax returns.
- This tax treatment was changed in 1987 such that publicly-traded partnerships would be treated in the same manner as C-corporations for federal income tax purposes (and therefore be subject to federal taxation at the entity level).
- At the same time, due to a recognition that energy infrastructure development was a capital intensive, high-volume, low-margin business with regulated rates of return, Congress provided an express exception for publicly-traded partnerships engaged in specified natural resources activities.
- These natural resources MLPs would continue to be exempt from federal taxation at the entity level and their partners would continue to pay federal income taxes with respect to their proportionate share of these partnerships' income, gain or loss.
- To qualify for "pass-through" tax treatment under Section 7704 of the Internal Revenue Code, a partnership must derive at least 90% of its income and gain from specified natural resources and other qualifying activities.
- The qualifying natural resource activities specified in Section 7704(d)(1)(E) consist primarily of the exploration, development, mining and production, processing, refining, transportation, storage or the marketing of certain minerals or natural resources.
- The largest segment of the MLP industry today is the midstream infrastructure segment which consists of pipelines, processing plants, storage and distribution facilities related to the transportation, processing, and storage of natural gas, natural gas liquids, crude oil and refined petroleum products.
- These types of activities are estimated to generate approximately 75% of the total revenue of all MLPs.
- Substantially all of the taxable income of MLPs is ordinary income and therefore the MLP partners generally pay income tax on the "passed through" income at ordinary income tax rates.

Business Characteristics

- MLP's are a capital intensive, high volume, low margin business
- MLP revenue is generally based on long term fee-based contracts that do not have adjustment provisions for increased taxes

- The tariff rates for many pipeline and storage facilities are regulated by the Federal Energy Regulatory Commission and state agencies, resulting in relatively modest rates of returns for their MLP owners
- MLP revenue is not directly the beneficiary of commodity price movement
- MLPs generally pay quarterly cash distributions in the range of 6% - 8% of equity price
- Due to steady cash distributions, the equity interests of MLPs generally trade at 12-15 times annual cash distributions, resulting in a relatively low cost of capital for MLPs which in turn facilitates access to capital necessary for MLPs to construct expensive capital projects

Positive Impact of MLPs on U.S. Economy, Environment and Energy Independence

- Since 2007, MLPs here invested approximately $113 billion to build new energy infrastructure projects
- The MLP industry currently supports 330,000 jobs in the United States through the construction of new pipelines and other energy infrastructure facilities as well as the ongoing operation and maintenance of existing energy infrastructure.
- INGAA projects $250 billion of capital investment will be necessary over 25 years for future energy infrastructure requirements.
- MLP industry heavily engaged in natural gas infrastructure development
    - Natural gas now fuels 25% of U.S. electricity generation
    - Access to new supplies of natural gas has reduced U.S. energy costs for industrial and consumer needs
- MLP industry is also heavily engaged in NGL and crude oil infrastructure development
    - NGL infrastructure development promotes domestic petro chemical production
    - Crude oil infrastructure development facilitates domestic crude oil production
- The development of natural gas, natural gas liquids and crude oil in the U.S. results in lower U.S. energy prices and reduced dependence on foreign energy

Conclusion

- Twenty five years of proven development of capital intensive energy infrastructure development is proof of the success of the pass-through structure for MLPs. New supplies of natural gas, natural gas liquids and crude oil from shale sources must have the means of transport from non-traditional supply locations to market. The MLP pass-through structure provides a cost-effective structure to continue to make significant capital expenditures to develop energy infrastructure to meet these transportation needs. Alteration of the MLP structure, if contemplated by changes to the tax code, will be detrimental to all stakeholders.