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Master Limited Partnerships (MLPs)

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MLPs are publicly listed partnerships that invest primarily in the energy sector. The market has grown substantially since its inception, though it has leveled off in recent years. MLPs tend to provide attractive current yield and offer the opportunity for price appreciation. However, MLPs are more complicated from tax, accounting, and administrative perspectives.

In this paper, we provide an overview of MLPs' structure, their history, performance and characteristics.

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Description of MLPs

A Master Limited Partnership, or MLP, is a partnership that has its shares (called "units") traded on a public stock exchange. As partnerships, MLPs are pass-through entities for tax purposes, meaning they do not pay taxes at the corporate level. MLPs are required to generate at least 90% of their income from activities with "qualified sources"[1] that are primarily related to depletable natural resources. Such activities include oil & gas exploration & production, mining, gathering & processing, refining, compression, transportation, storage, marketing and distribution.

MLPs operate in a number of natural resources-related businesses and have been popular vehicles for investment due to their tax-advantaged high distribution payout structure and, in certain cases, cash flows backed by long-term contracts. While MLPs typically distribute much of their cash flow, unlike REITs, MLPs do not have statutorily required distribution minimums. MLPs have the ability to grow, and thus increase distributions, through additions to their asset bases by acquisition or development.

MLP structure

Typically, an MLP's ownership consists of a general partner (GP) and limited partners (LP). The LPs provide capital but have no role in managing or operating the MLP and have limited voting rights. They are, however, entitled to receive cash distributions, and their units are publicly traded, thereby allowing for liquidity. In contrast, the GP tends to hold a small stake (e.g., 2%) but have full management responsibility and control of the business (see the following organizational diagram).

[1] Source: Internal Revenue Code Section 7704.

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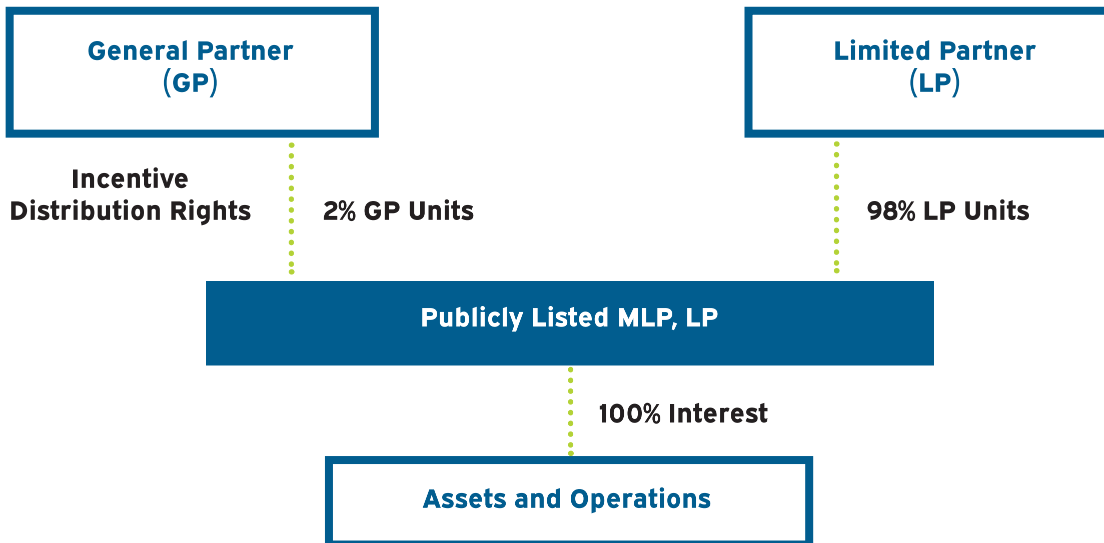

FIGURE 1
Organizational Diagram for a Typical MLP

Source: Meketa Investment Group.

Many MLPs operate what may be described as a "toll-road" business model, meaning they receive a fee for handling the customers' product without taking ownership of the commodity. MLPs can have long-term contracts with their customers, often with attractive features such as "take-or-pay" and inflation escalators that help provide cash flow stability and limit commodity price exposure. MLPs typically operate in asset intensive businesses with high barriers to entry, which can also help ensure their cash flow stability.

MLP distributions

MLPs typically pay almost all their distributable cash flow ("DCF") in the form of quarterly distributions. Due to their high payout ratios, MLPs are often reliant on debt and equity capital markets to finance growth. In order to grow, an MLP needs to develop its existing assets and/or acquire new assets, as well as raise the necessary capital to execute its growth plans. To retain access to the capital markets, MLPs are motivated to retain a strong balance sheet and not rely too heavily on debt to finance growth. However, existing investors will experience dilution as more MLP units are issued.

Historically, GPs have owned Incentive Distribution Rights ("IDRs") that entitle the GP to a greater percentage of incremental cash flows that are distributed by the MLP. The IDRs are akin to a performance fee. Initially, the GP is entitled to its pro rata share (e.g., 2%) of the cash distributions. As distributions increase and reach certain levels (i.e., "splits" or "tiers"), the GP is entitled to a larger percentage of the incremental cash distribution – in some cases up to 50% (see the following table for an example). Hence, typical IDR structures provide the GP an incentive to grow distributions. The particular MLP's partnership agreement spells out the terms of its IDRs.

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Tier	LP (%)	GP (%)	Declared Distribution
1	98	2	Up to $1.00
2	85	15	$1.00 to $2.00
3	75	25	$2.00 to $3.00
4	50	50	Over $3.00

FIGURE 2
Incentive Distribution Rights Structure for Example MLP

Source: Meketa Investment Group.

The table below illustrates the mechanics of how cash flows are allocated between the LPs and the GP, based on the Incentive Distribution Rights schedule shown above. The "Declared Distribution" refers to the amount of cash distributable to the GP (prior to the IDR) and the LP at each tier level. As cash distributions grow, the GP (based on its GP interest *plus* the IDR) is allocated a greater percentage of the total distributions.

Tier	LP ($)	GP (2%)	GP (IDR)	GP Total ($)	Total GP Share of Tier Cash Flow (%)
1	0.98	0.02	0.00	0.02	2
2	0.98	0.02	0.15	0.17	17
3	0.98	0.02	0.31	0.33	33
4	0.98	0.02	0.96	0.98	50
Total	**3.92**	**0.08**	**1.42**	**1.50**	**28**

FIGURE 3
Declared Distribution Allocation for Example MLP

Source: Meketa Investment Group.

As the distribution flows through each tier, more incremental cash is allocated to the GP. Note that in this example it would take $5.42 of total distributions to fill each tier, resulting in $3.92 (72%) to the limited partner and $1.50 (28%) to the general partner.

An issue with IDRs is that they effectively raise the cost of capital for the MLP (which only issue LP units when they raise capital). As cash distributions increase (thereby lifting the tier levels), the LP unit gets a smaller share of incremental dollars. MLPs with high splits (e.g., 50%) can find that acquisitions are uneconomic for the LPs as the LPs only receive 50% of incremental distributions but provide virtually 100% of the capital. Some GPs have reduced their splits or exchanged their IDRs for LP units to alleviate this issue. The MLP industry has seen a shift away from IDRs, which in some cases have acted as an incentive to raise capital and increase distributions, allowing GPs to receive a higher proportion of distributions while potentially negatively impacting the balance sheet or diluting LP shareholders. This, in some cases, has caused a misalignment of GP and LP interests.[2]

[2] Examples include Niska Gas Storage L.P., Genesis Energy L.P., and PVR Partners, L.P.

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History of MLPs

MLPs were first formed in the early 1980s in the oil & gas sector. Soon after, other types of businesses formed MLPs as well, including real estate, restaurants, cable TV, amusement parks, and even the Boston Celtics. MLPs provided a way to raise capital from smaller investors by offering them a tax-efficient investment that was also publicly tradable. By the mid-1980's, Congress became concerned that MLPs would provide a way for large numbers of corporations to avoid corporate income tax. In 1987, Congress passed legislation that limited partnership tax treatment to those entities earning at least 90% of their income as "qualifying income," which they defined as follows:

> "income and gains derived from the exploration, development, mining or production, processing, refining, transportation (including pipelines transporting gas, oil, or products thereof), or the marketing of any mineral or natural resource"[3]

[3] Source: Section 7704 of the Internal Revenue Code.

In the late 1980's and the 1990's some integrated energy companies sold or spun off their "midstream" or pipeline-related assets to MLPs. These became the foundation of the current MLP universe. Over time, MLPs engaged in marine transportation of petroleum products, propane distribution, and the coal industry were formed. In the late 2000's, MLPs focused on oil & gas exploration and development, often with hedging to protect cash flow and distributions, were formed. Through the passage of the Renewable Energy and Job Creation Act in September 2008, the definition of "qualifying income" was expanded to include the transportation and storage of renewable fuels, further increasing the MLP universe.

Overview of the MLP market

As of the end of 2021, there were 76 MLPs trading on major US exchanges[4], with oil & gas midstream activities – gathering, processing, natural gas compression, pipelines, storage, refining, distribution, and marketing – representing the dominant activity. However, the MLP asset class has drawn entrants beyond the midstream area (see Figures 4 and 5).

[4] Source: Energy Infrastructure Council, Publicly Traded Partnerships Trading on US Exchanges, as of August 2022.

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FIGURE 4

MLPs Industry Group by Number

Source: Energy Infrastructure Council as of 2022. Totals are subject to rounding errors.

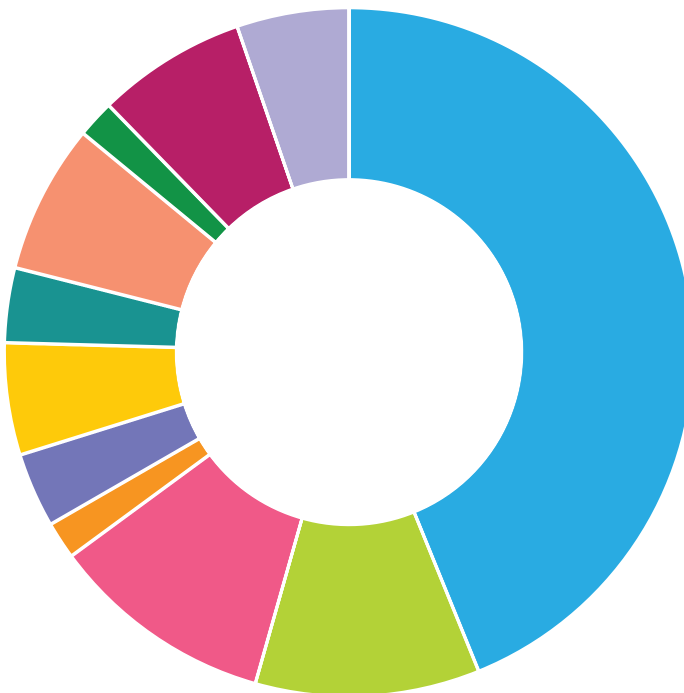
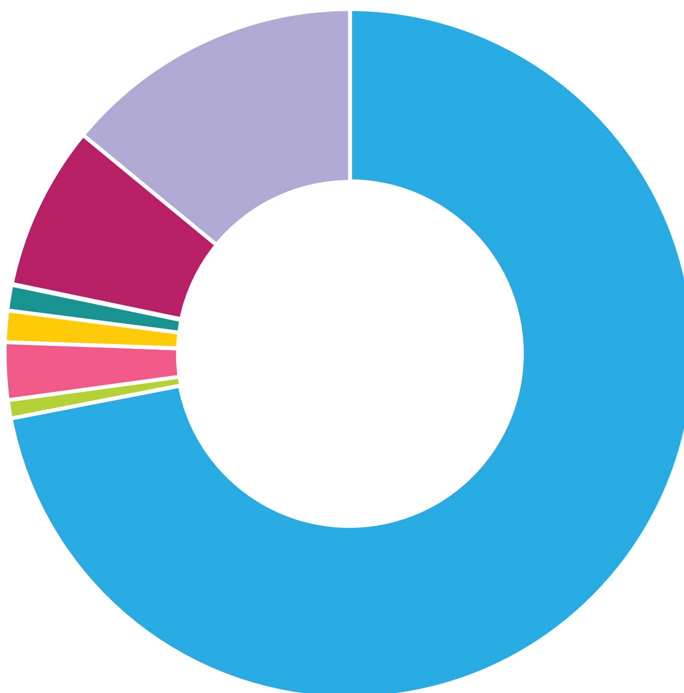


FIGURE 5

MLPs Industry Group by Capitalization

Source: Energy Infrastructure Council as of 2022. Totals are subject to rounding errors.



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The market value of the MLP universe has grown substantially since 2000. This has been the result of IPOs, secondary equity issuance and appreciation.

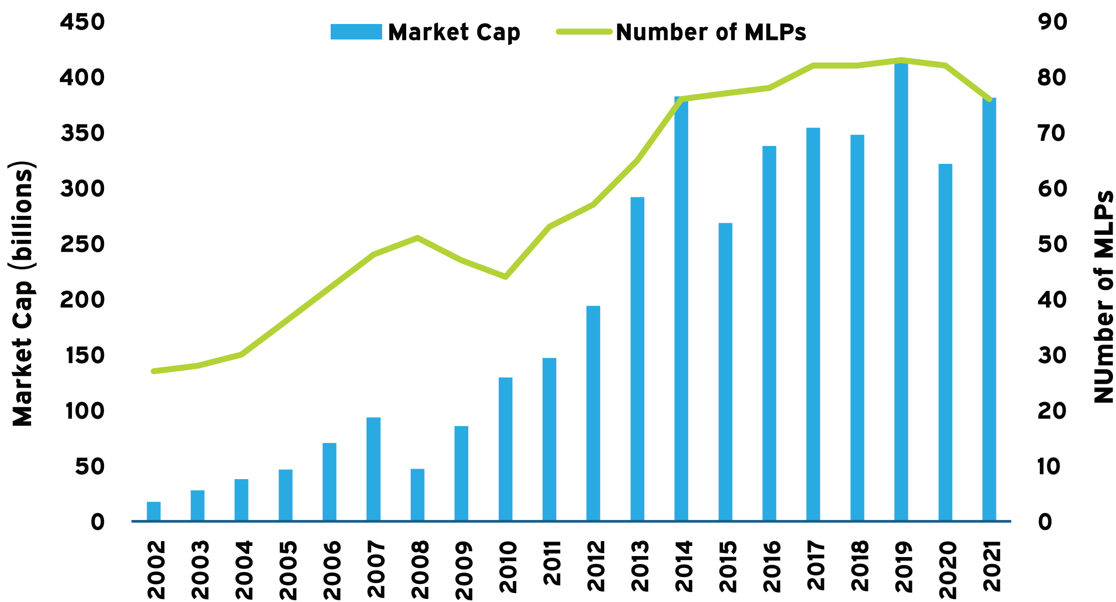

FIGURE 6

Growth of MLP Universe

Source: Energy Infrastructure Council.

As the MLP market has grown, so has its liquidity. Average daily trading volume increased from approximately $45 million in 2016 to a peak of around $90 million[5] in 2020 (see Figure 7). While originally a retail-oriented investment, institutions steadily increased their share of the MLP marketplace. Approximately 44% of MLP interests are held by retail investors as of 2021, with the balance held by institutional investors such as closed-end funds, mutual funds, and hedge funds.[6]

[5] Total MLP market. Source: Alerian, Factset.

[6] Source: PricewaterhouseCoopers LLP, Partnership reports and Wells Fargo Securities, LLC..

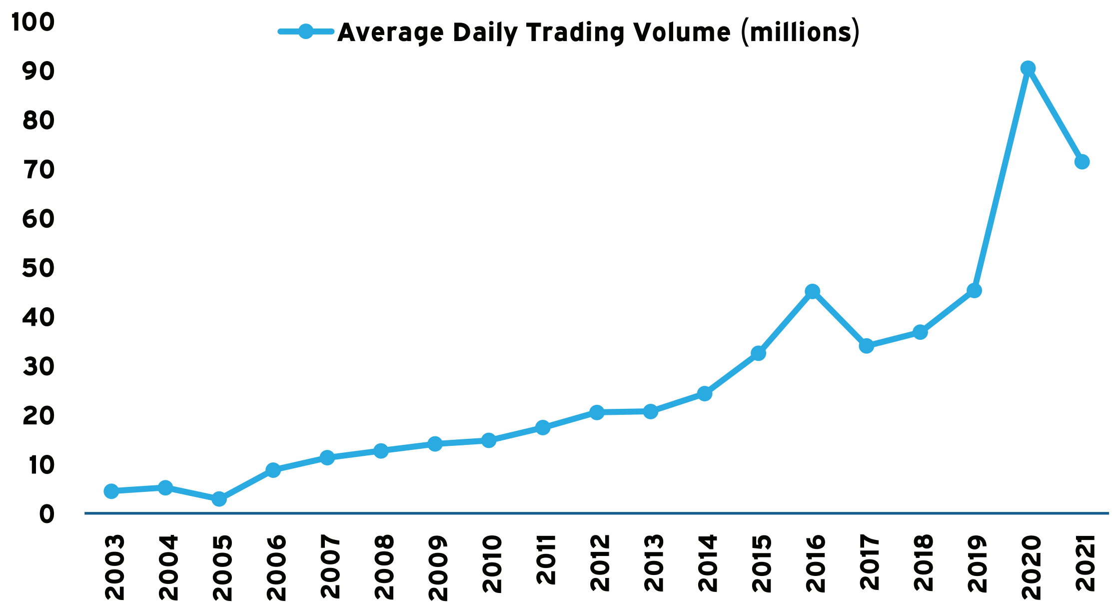

FIGURE 7

Average Daily Trading Volume for Total MLP Market

Source: Wells Fargo.

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While the MLP market has grown substantially, it remains small compared to other asset classes such as corporate bonds and much smaller than the broad equity market. The entire MLP market is similar in size to the market capitalization of Exxon Mobil.

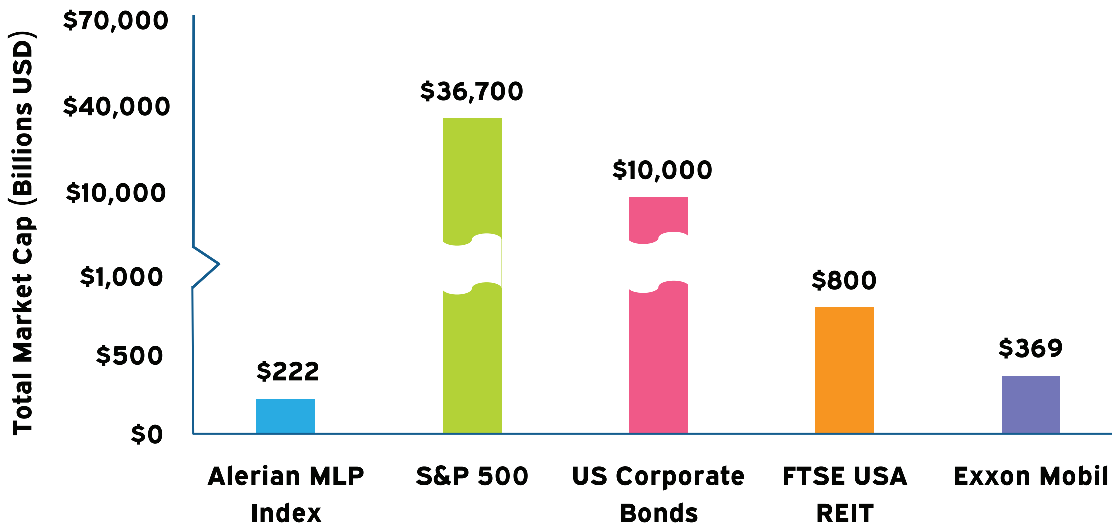

FIGURE 8
Comparison of Market Capitalization

Source: Datastream, S&P Global, FTSE Russell as of July 30, 2022.

On average, MLPs increased their distributions in aggregate through 2014. The rising level of distributions was a key factor in driving investor interest. However, in recent years, MLP distribution growth has been inconsistent, with negative growth periods in most years since 2014. This phenomenon might signify underlying challenges in the MLP market. Distribution cuts by MLPs tend to be large, commonly in the 50% range, and have occurred for reasons such as weak energy markets, addressing IDR concerns, or solving balance sheet issues, with examples of the latter happening during the early portion of the Covid-19 pandemic.

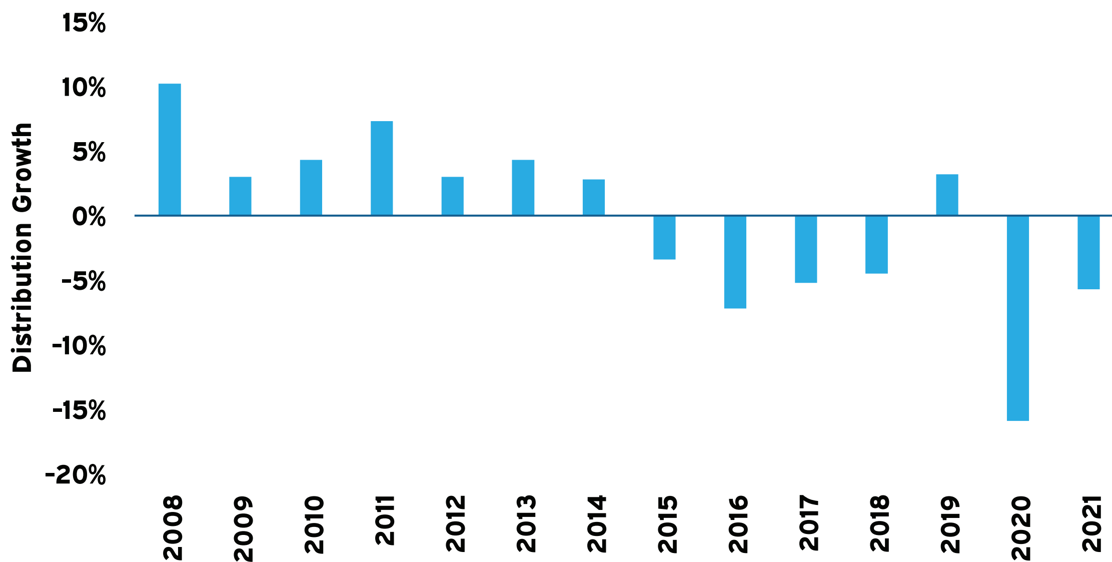

FIGURE 9
MLP Year over Year Distribution Growth

Source: Factset, EIC, Alerian.

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MLPs operate in a number of businesses with a variety of contract structures and sensitivities to commodity prices (see the following diagram). For example, natural gas and crude oil pipelines are often viewed as lower risk businesses given their longer contract lengths and revenue that is either volume based or has take-or-pay structure. In general, pipelines do not take title to the commodities and their revenue is not directly related to commodity prices; however, pipelines do have indirect exposure to commodity prices as their growth is related to continued development of domestic oil and gas. Gathering systems, fractionation, and terminals tend to have shorter contracts and have revenues with more exposure to the volume of product transported or treated. Exploration and production businesses typically operate under market rates with short term-hedging contracts and thus may have more exposure to commodity price changes.

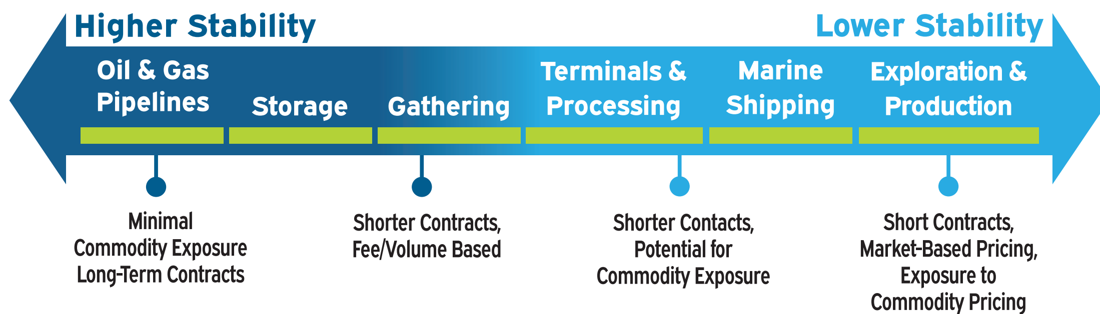

FIGURE 10
MLP Sector Cash Flow Stability

Source: Meketa Investment Group.

Return characteristics

A key driver of investor appetite for MLPs has been their strong yield. Historically, MLPs have provided attractive yields compared to other alternatives such as investment grade bonds and US stocks. As of June 2022, MLP yields are slightly above those for high yield bonds.

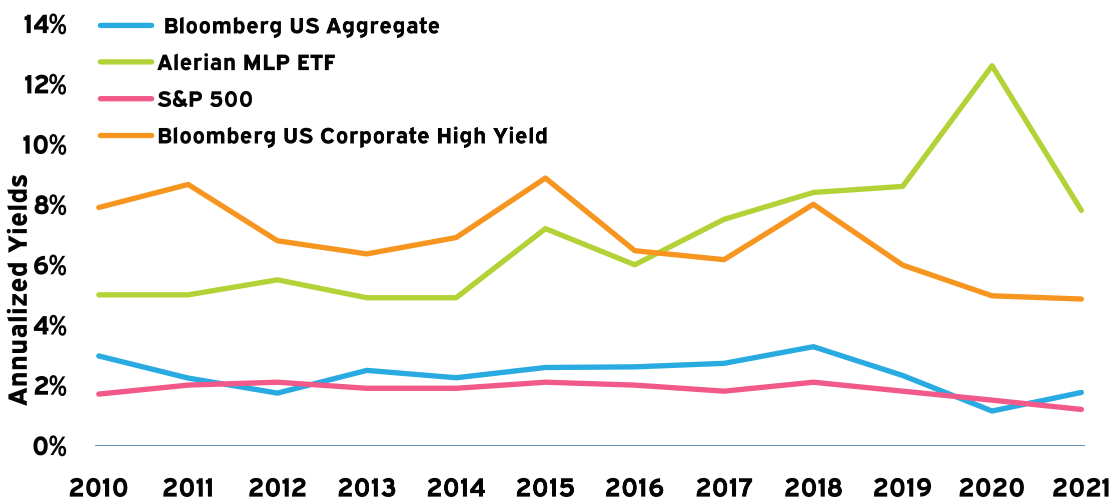

FIGURE 11
Annualized Yields (as of June 30, 2022)

Source: Factset, Bloomberg, VettaFi.

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In addition to yield, MLP investor returns are affected by distribution growth and changes in valuation (e.g., yield compression/expansion). For example, in 2021, the components of the Alerian MLP index yielded 10.9%. In addition, MLP yield spreads compressed (i.e., the "risk premium" compared to US Treasuries became smaller) thereby increasing return by 29.0%. Overall, the Alerian MLP index had a return of 39.9% in 2021 (see the following chart).

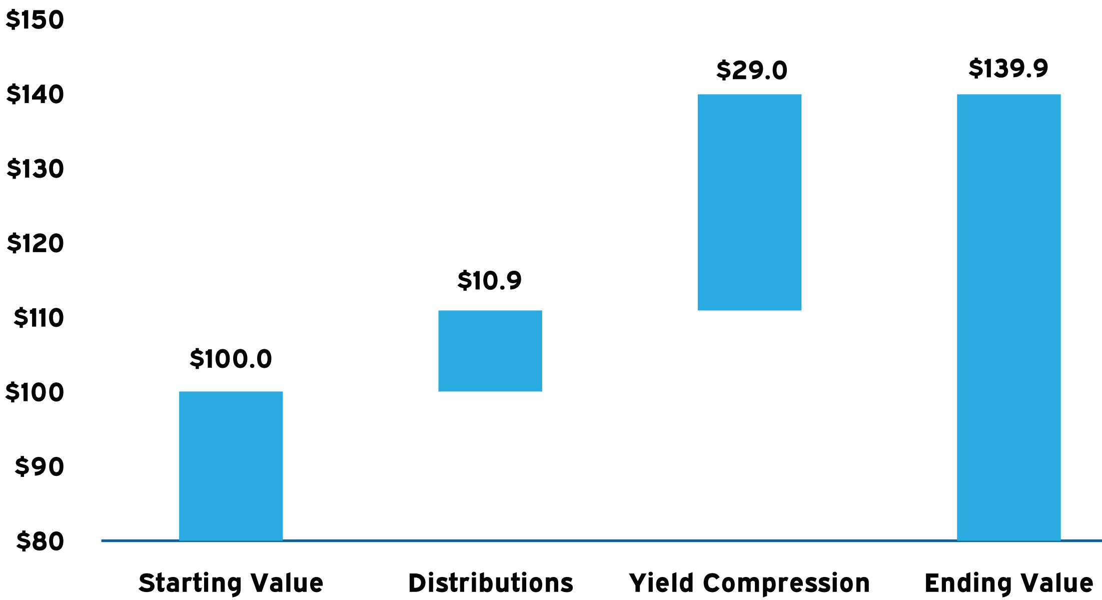

FIGURE 12
Decomposition of 2021 Total Returns (Alerian MLP Total Index)

Source: Bloomberg.

In the early 2000s, the MLP market produced strong positive returns that greatly exceeded the broad equity market (see Figure 13). However, since 2012, MLPs have lagged the stock market more often than not.

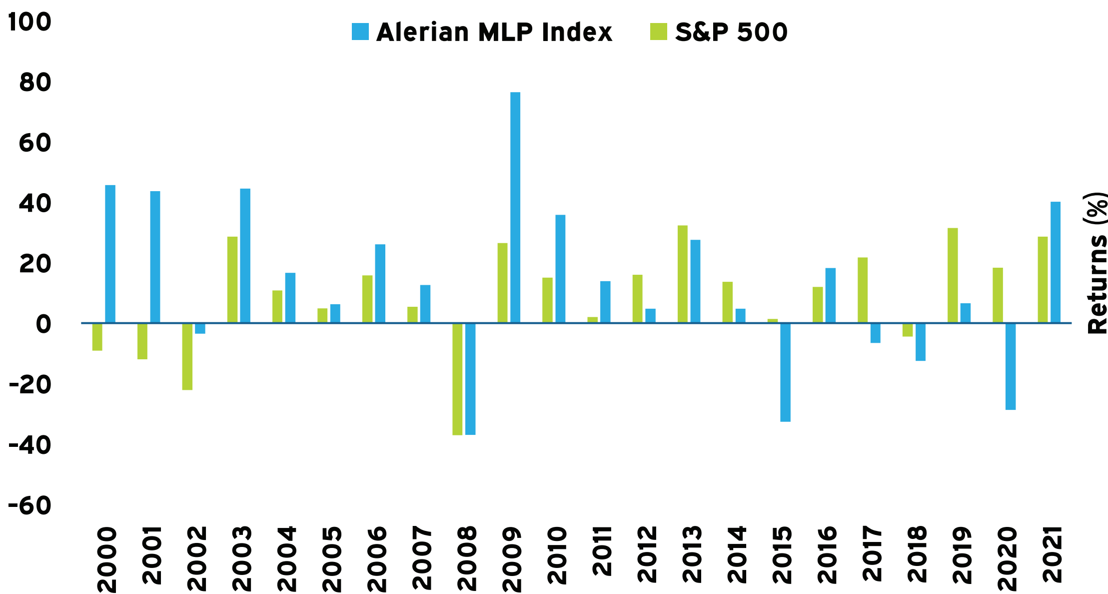

FIGURE 13
Total Return by Calendar Year

Source: Thomson Reuters, Bloomberg, Factset and Ibbotson.

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MLPs have demonstrated volatility and drawdowns similar to the natural resources component of the equity market and much higher than the broad equity market. (see the Figure 14). However, MLPs have delivered attractive overall returns. MLPs have also generated high risk-adjusted returns, as demonstrated by their high Sharpe ratio.

	Alerian MLP Index	S&P 500	S&P North American Natural Resources	S&P 1500 Energy	Bloomberg Aggregate	Bloomberg High Yield	S&P GSCI Commodity	NAREIT Equity
Annualized Return	10.5%	6.3%	5.9%	6.9%	4.2%	6.7%	1.4%	5.6%
Standard Deviation	23.7%	15.2%	23.9%	25.0%	3.6%	9.3%	23.5%	20.3%
Sharpe Ratio	0.38	0.31	0.18	0.22	0.74	0.56	-0.01	0.20
Max Drawdown	-74.3%	-51.0%	-59.5%	-66.4%	-11.9%	-31.4%	-87.2%	-71.4%

FIGURE 14
Risk and Return (January 2000 to June 2022)

Source: Thomson Reuters, Meketa Investment Group and Factset.

As the following table illustrates, the Alerian MLP index has demonstrated a positive and growing correlation to US equities over the past two decades. Unsurprisingly, the correlation between the Alerian MLP Index and the S&P North American Natural Resources Index has been even higher, and it has demonstrated the same trend of increasing over time.

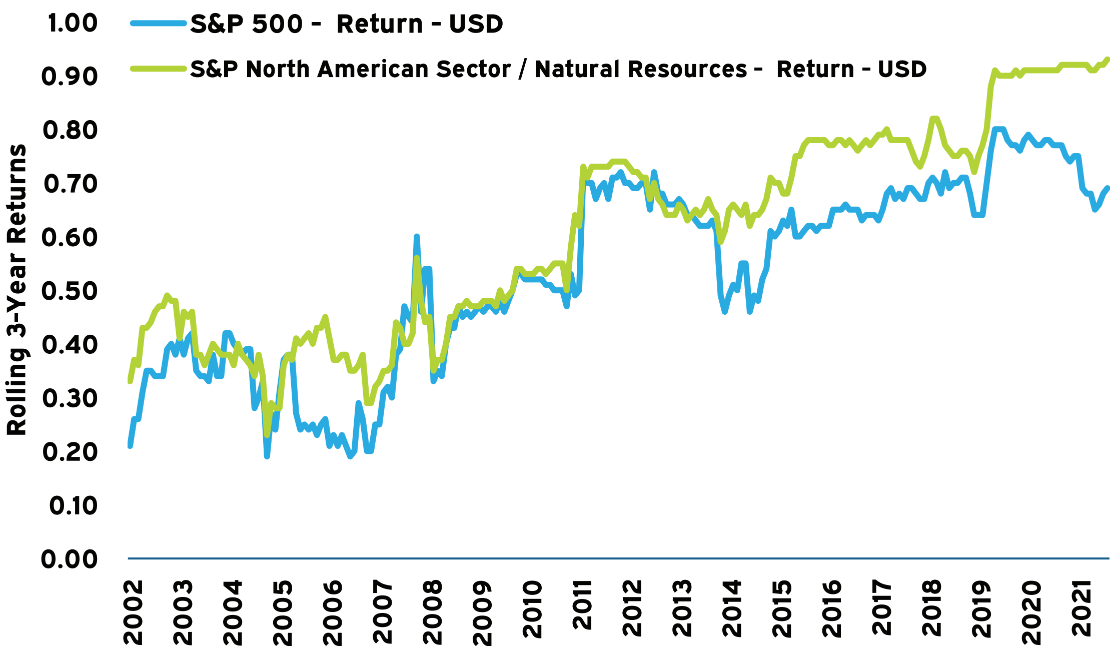

FIGURE 15
Rolling 3-year Correlations (December 2002 to July 2022)

Source: Factset and Federal Reserve Economic Data.

Because MLPs invest in the natural resource sector, investors may consider them to be a good inflation hedge. There have not been many periods during the life of the MLP marketplace to test this hypothesis. However, Figure 16 shows the performance of various sectors in the first half of 2022, the highest inflationary period in forty years. Unsurprisingly, commodities, energy stocks and natural resource stocks all performed strongly during this period. MLPs, however, do not display quite the same relationship. While they did keep pace with inflation, they lagged these other sectors.

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	Alerian MLP Index (%)	S&P 500 (%)	S&P North American Natural Resources (%)	S&P 1500 Energy (%)	S&P GSCI Commodity (%)	FTSE NAREIT (%)	CPI (%)
YTD Returns	10.0	-20.0	15.9	30.9	35.8	-20.4	9.1

FIGURE 16
Performance During 2022 Inflation (YTD Returns of as June 30, 2022)

Source: Factset and Federal Reserve Economic Data.

MLP valuations

A primary consideration when investing in any asset class is its current valuations level. A common measure for assessing valuations for the MLP market is the yield of the Alerian MLP index. Using yields may also allow for a relative comparison to other asset classes that likewise offer a yield component.

As the following chart shows, as of July 2022, MLP yields were near the historical average levels over the past 27 years.

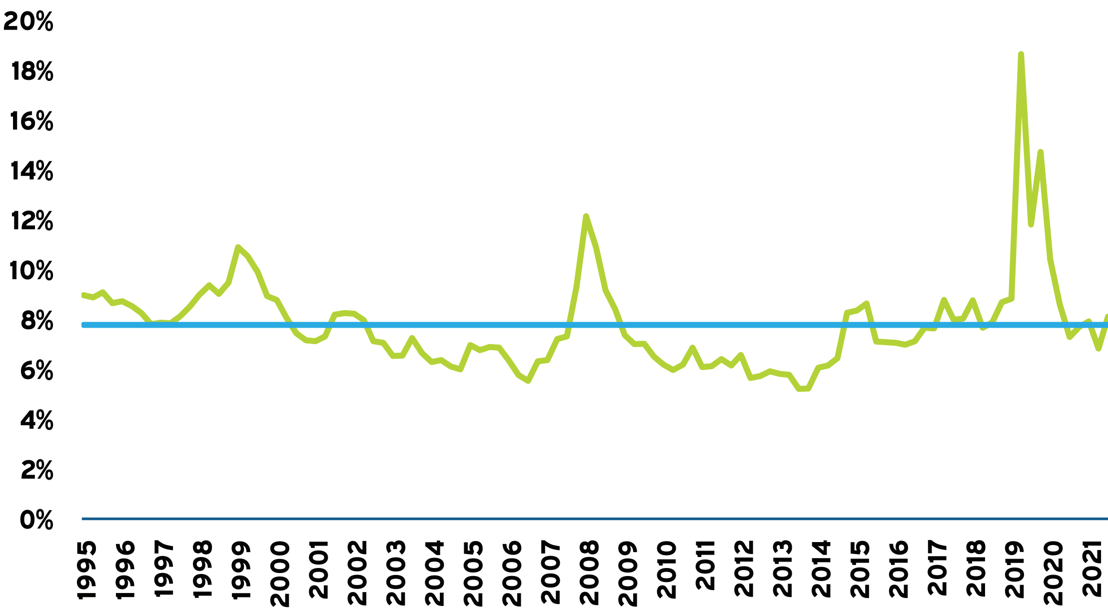

FIGURE 17
MLP Yields

Source: VettaFi and Multpl.com.

Investors should also consider whether MLPs look attractive relative to the other opportunities that are available to them. The following chart shows the difference between MLP yields and the yield on the 10-year US Treasury (i.e., the yield spread). As of July 2022, the spread was near its historical average.

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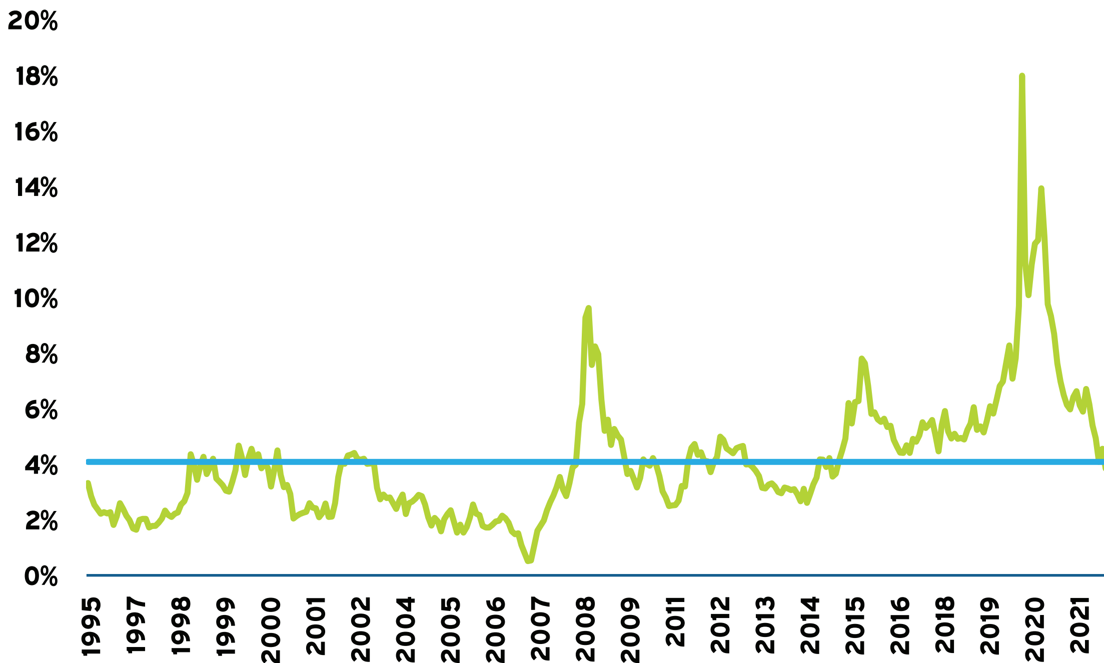

FIGURE 18
MLP Spreads

Source: VettaFi and Multpl.com.

Risks and considerations

As with any investment, there are unique risks related to investing in MLPs. Some of these risks are due to the legal structure of MLPs and some are borne of the market in which they operate.

Return volatility

MLPs, particularly in times of market stress, can become highly correlated with equities and demonstrate high volatility and drawdowns. Retail investor flows are a contributor to return volatility as the majority of MLPs continue to be held by retail investors who may react to negative news by selling their positions.

Changes to distributions

In the past, MLPs had historically increased their distributions in aggregate. This has not been the case since 2015, as distributions shrunk, potentially driven by LPs concerns over unnecessary financing and shareholder dilution, as well as to solve balance sheet issues. Distribution levels can vary based on the level of attractive investment opportunities in the space, IDRs, macroeconomic factors and more.

Market illiquidity

The MLP marketplace remains small compared to domestic equities and bonds. Investors with larger portfolios may experience difficulty in efficiently building or reducing their positions, due to limited trading volumes.

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Limited diversification

Much of the market's investable value is represented by a limited number of MLPs. Specifically, approximately 81% of the Alerian MLP Index value is represented by the index's ten largest MLPs.[7]

[7] Source: Alerian as of June 2022.

Changes in interest rates

A key attraction of MLPs has been their comparatively high yields. An increase in the yields available from other asset classes could diminish MLPs' appeal if they are not able to generate a commensurate growth in distributions or if MLP distributions continue to contract.

Energy market

The MLP market is dominated by domestic oil- and gas-related activity. A decrease in exploration and production activity, whether due to an economic slowdown, regulatory changes, safety issues, substitution, or other factors, could reduce the cash flows available to MLPs.

Access to capital

MLPs typically distribute a very high percentage of their free cash flow and as such need to regularly access the capital markets for debt and equity to finance their growth. Equity capital raises could be dilutive to existing unit holders.

GP/LP structure

Through their IDRs, GPs obtain an increasing share of incremental distributable cash flow. This may serve as an incentive for GPs to rapidly grow distributable cash flow in what could be an unsustainable manner.

Tax and administrative complexity

As tax pass-through vehicles, MLP unit holders are responsible for calculating and paying taxes due. In addition to Federal taxes, the vast majority of MLPs operate in multiple states, potentially requiring the unit holder to review state-level tax obligations as well. Tax-exempt investors may be subject to Unrelated Business Income Tax related to their holdings of MLP units.

Regulatory and tax changes

Congress may re-consider the tax pass-through features of MLPs at a future date. Such a change would likely have a significant impact on the attractiveness of MLPs to taxable investors and the MLP market as a whole. For example, the 2011 changes to the tax treatment of Canadian royalty trusts (which had a similar tax favored structure) led to a significant deterioration in their value. In 2018, the Federal Energy Regulatory Commission (FERC) eliminated tax allowances for MLPs' pipelines and proposed natural gas pipeline rate reviews based on the Tax Cuts and Jobs Act of 2017. The prevailing corporate tax rate also affects the relative attractiveness of the MLP structure.

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Benchmarking

The MLP sector has a number of indices that an investor could choose for measuring the performance of the sector or benchmarking their portfolio. The characteristics of the most prominent MLP indices are outlined below.

Criteria	Alerian MLP Index	S&P MLP Index	Tortoise MLP Index
Number of Constituents	25	27	31
Weighting Method	Market-cap weighted	Market-cap weighted	Market-cap weighted
Rebalance Frequency	Quarterly	Annually	Quarterly
Market Capitalization Threshold	> $200 million	> $200 million	> $200 million
Liquidity Threshold	6-month median daily trading volume > 25,000 units	3-month average value traded > $2 million ($1.5 million for current constituents)	None
Public Float Requirement	Investable Weight Factor >20%	None	None
Float Adjusted	Yes	Yes	Yes
Individual Security Weighting Cap	No	15.4%	10%
Minimum Share Price	> $10 (preferred)	None	None
Exploration & Production Companies Included	Yes	Yes	Yes

FIGURE 19
Characteristics of Major MLP Indices

Source: Meketa Investment Group.

The Alerian MLP index is the most widely followed benchmark. It is a float-adjusted, capitalization-weighted total return index of 25 of the largest energy MLPs. Of note is that all the indexes listed above, like other capitalization weighted indexes, are affected by the price movements of the index's largest holdings; however, they are more concentrated than many traditional equity indices (e.g., in the case of the Alerian MLP index, the top 10 holdings account for approximately 81% of the index value as of July 30, 2022).

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Tax implications of MLP investments for institutions

The MLP structure is considered tax efficient in that the MLP itself does not pay taxes and therefore its distributions are not subject to "double taxation" (i.e., unlike companies, which pay corporate tax, then investors pay taxes on dividends). Unlike a corporation, an MLP is considered to be the aggregate of its partners rather than a separate entity. MLPs pay no corporate-level taxes. Instead, the MLP passes income and losses to the unit holders themselves who are ultimately responsible for paying taxes.

Because MLPs are partnerships, unit holders receive IRS K-1 statements issued by the individual MLPs. Each K-1 will indicate the unitholder's share of net income, gain, loss, and deductions. Additionally, the unit holder will receive information on the MLP's activity in each state in which it conducts business and the unitholder may be required to file taxes in each of those states. To the extent an investor has direct ownership of multiple MLPs, the administrative burden would increase.

Tax-exempt investors have additional tax issues when considering an investment in MLPs. Under current tax law, tax-exempt organizations are exempt from US federal income tax on passive investment income. However, given the MLP's tax pass-through structure, an MLP may generate UBTI (Unrelated Business Taxable Income) for these investors. While certain state and municipal-related investors maintain they are not subject to UBTI, a tax-exempt organization is required to file with the IRS. Investors should evaluate the tax implications and related administrative complexity of MLP investments when considering this asset class.

Ways to invest in MLPs

Institutional investors have used a variety of methods to invest in MLPs. Beyond building a portfolio of MLPs directly, there are asset managers who can build customized portfolios through managed accounts, and a number of publicly traded closed-end funds, ETFs and ETNs. While publicly listed, pooled investment vehicles provide diversification, liquidity, and simplified tax reporting for the investor, they lose the tax efficiency associated with the direct ownership of MLPs. Also, while most open-end funds (e.g., mutual funds) are structured as tax pass-through vehicles, they are limited to no more than 25% of their assets in MLPs (or other tax-pass through investments) otherwise they would lose their tax pass through characteristics.

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FIGURE 20
Fund Structure Pros and Cons

	Description	Benefits	Issues
Direct Investing	Investor builds and manages MLP portfolio internally (i.e., actively managed).	Full control of asset selection and portfolio management. All distributions and income pass through to investor.	Administrative burden related to taxes and record keeping. Lower liquidity (have to sell investments separately). Fees: None (internally managed).
Separate Managed Account (SMA)	Investment manager builds and manages MLP portfolio (i.e., actively managed).	Professional oversight of portfolio. Manager may be able to assist with administrative issues. All distributions and income pass through to investor.	Administrative burden related to taxes and record keeping. Lower liquidity (have to sell investments separately). Fees: Negotiated. May include performance fee.
Closed End Fund	Publicly listed vehicle with a fixed number of shares. Investment focus is MLPs and is often actively managed.	Improved liquidity (can sell entire vehicle). No K-1s, only a single Form 1099. No UBTI.	Can trade at a premium or discount to NAV. Vehicle treated as a corporation for tax purposes and pays taxes on gains and income before passing on to investor, thereby reducing distributions. Can have significant index tracking error due to reserves for future taxes based on portfolio gains. Structure can include leverage. Fees: 0.75% to 1.25%
Exchange Traded Fund (ETF)	Publicly listed vehicle that holds a portfolio of MLPs. Portfolio typically tied to an index (i.e., passively managed).	Improved liquidity (can sell entire vehicle). No K-1s, only a single Form 1099. No UBTI.	Vehicle treated as a corporation for tax purposes and pays taxes on gains and income before passing on to investor, thereby reducing distributions. Can have significant index tracking error due to reserves for future taxes based on portfolio gains. Fees: 0.75% to 1.25%
Exchange Traded Note (ETN)	Debt instrument with return linked to an MLP index (i.e., passively managed).	Improved liquidity (can sell entire vehicle). No K-1s, only a single Form 1099. No UBTI.	Counterparty credit risk. Fees: 0.80% to 1%

Source: Meketa Investment Group.

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As noted in the previous table, closed end funds and ETFs can suffer from potentially significant tracking error issues due to their requirements to reserve for capital gains taxes. As such, these are not likely to be a good alternative for tax-exempt investors. Additionally, those investors seeking to build a portfolio of individual MLPs should recognize that certain securities may have limited float or daily liquidity. Potential investors should research the particular characteristics of individual MLPs (e.g., what basins it has exposure to, the average length of contracts) to understand the underlying risk differences among MLPs. Investors making larger investments may need to carefully plan their trades to avoid disrupting the market price for a particular MLP.

Summary

MLPs provide a way to gain exposure to the US energy infrastructure complex. Many MLPs generate attractive cash distributions from steady, long-term contracts with potential for price appreciation due to growth. However, individual MLPs may experience business changes or competitive threats that could cause them to reduce dividend payments. Also, as publicly traded instruments, MLPs are subject to equity-like market risks, including participating in broad market downturns. While MLPs historically are likely to hedge against inflation to some extent, there are likely better inflation hedges available. Finally, the tax pass-through structure of MLP's could lead to tax filing complexity that should be considered before making an investment.

We believe it is appropriate for certain investors to consider an allocation to MLPs within a broader energy investment portfolio.

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Appendix 1 | Glossary of MLP terms

Qualifying income | As defined by section 7704 of the Internal Revenue Code: "A partnership meets the gross income requirements… for any taxable year if 90 percent or more of the gross income of such partnership for such taxable year consists of qualifying income."

> "The term 'qualifying income' means - (A) interest, (B) dividends, (C) real property rents, (D) gain from the sale or other disposition of real property…, (E) income and gains derived from the exploration, development, mining or production, processing, refining, transportation (including pipelines transporting gas, oil, or products thereof), or the marketing of any mineral or natural resource (including fertilizer, geothermal energy, and timber), (F) any gain from the sale or disposition of a capital asset… held for the production of income… and (G)… income and gains from commodities… or futures, forwards, and options with respect to commodities."
>
> "The term 'mineral or natural resource' means any product of a character with respect to which a deduction for depletion is allowable."

Distributable cash flow | DCF is an indicator of an MLP's ability to generate cash flow that can be used to sustain quarterly distributions to the unit holders. While not a GAAP measure, DCF can be calculated as Net Income adjusted for depreciation, amortization, and other non-cash items and after maintenance capital expenditures. An MLP's specific measure of DCF will be defined in their partnership agreement.

Incentive distribution rights | IDRs are typically set out in the MLP agreement and provide the General Partner with a larger percentage of the MLP's incremental cash flow distributions. These rights are designed to motivate the General Partner to grow distributions to Limited Partners.

Unit holder | The holder of an ownership unit in a publicly traded limited partnership. The unit provides the holder with a stake in the MLP's income and distributable cash flow.

K-1 statements | A K-1 statement is an IRS form that is used to report the beneficiary's share of partnership's income, deductions, and credits.

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Appendix 2 | Glossary of natural resource terms

Exploration and Production (E&P) | Involves extracting the commodity (e.g., crude oil or natural gas) from the ground.

Fractionation | Fractionation is the process of separating a mixed NGL stream into its components.

Gathering | Encompasses smaller capillary-like pipes 4-to-6 inches in diameter and provides short-haul takeaway capacity from the wellhead, drawing oil or gas into the larger long-haul pipelines or for processing.

Hydrocarbons | Refers to a set of compounds extracted in either liquid (petroleum) or gaseous form (natural gas) and used in the energy, transportation, and petrochemical industries.

Midstream | Oil and gas pipelines and related infrastructure that handle, process, and transport oil, gas, and refined products from the point of production to a point of distribution.

Natural Gas Liquids (NGLs) | Many natural gas resources will include a set of gas liquids such as ethane, propane, butane, and natural gasoline known as NGLs. A "liquids rich" natural gas resource tends to have a higher percentage of NGLs. The primary uses for NGLs include: production of plastics, insulation, lubricants, detergents, heating and refrigeration, petrochemical feedstock, gasoline blending and propellant.

Oil sands | Oil Sands contain a mixture of sand, clay, water and a viscous form of petroleum referred to as bitumen. Bitumen is a thick, sticky form of hydrocarbon that will not flow unless it is heated or diluted with lighter hydrocarbons.

Pipelines | Pipelines are used to transport of various types of products across the country including natural gas, refined products, crude oil, and NGLs. These assets tend to have stable cash flows through fixed-fee contracts.

Processing | Involves purging impurities in order to meet specific pipeline specifications for transportation. Processing includes dehydration, treating and the extraction of the gas, natural gas liquids ("NGLs") or oil from the resources stream.

Shale | A fine-grained, sedimentary rock composed of mud flakes from clay minerals and small fragments of other materials. The shale acts as both the source and the reservoir for the hydrocarbon.

Storage | Resources may be put in storage to ensure reliable supply when necessary as well as to take advantage of more favorable pricing. Companies store refined products and crude oil in above-ground facilities while underground facilities typically house natural gas within depleted reservoirs, aquifers, or salt cavern formations.

Terminals | Terminals serve to receive and distribute oil and gas products via vessels or pipelines. Terminals generate revenue from storage and handling activities, as well as from services such as blending and additive injection.

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Appendix 3 | Contract structures

Ship-or-pay contracts | Pipeline companies lock in revenue for the long term, virtually eliminating price and volumetric risks.

Throughput based contracts | Involves locking in a fixed fee per unit of product. This exposes the business to changes in volume which is indirectly linked to the price of the commodity.

Storage contracts | Shippers typically pay a rental fee for usage of the storage so that they can manage varying levels of demand in different seasons. Owners of storage typically charge rates based on the difference between peak and off-peak commodity prices and therefore benefit when the futures price curve is positive.

Commodity linked contracts | These contracts require the owner of the asset to take some level of commodity price risk through either a share of proceeds, share of the product, or a margin off the commodity price. These contracts are more typical in processing, fractionation, and production businesses.

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