O R G A N S T A N L E Y R E S E A R C H
February 10, 2013
Midstream Energy MLPs
Congressional Support for the MLP Structure Grows

Last week, Senator Lisa Murkowski (R-AK) issued a white paper, "Energy 20/20: A Vision for America's Energy Future", detailing a list of starting points for a rethinking of the U.S.'s energy and natural resources policy, with an eye toward implementation by 2020 . Through cooperation between Congress and the President, the Senator's paper seeks to identify ways to align federal law and policy with our national interest to make energy "abundant, affordable, clean, diverse and secure." Ideas put forward in the report fall under seven categories: "producing more, consuming less, clean energy technology, energy delivery infrastructure, effective government, environmental responsibility and *an energy policy that pays for itself*."

¬ **MLPs as a conduit to advance renewable energy development.** Under her list of ideas to support the advancement of clean energy technology, Sen. Murkowski puts forward a proposal for the qualifying income definition to be expanded to allow MLPs to invest in a broad range of alternative energy sources (*see inset at right*). Highlighting the value of the MLP structure in facilitating investment in pipelines, she sees a parallel argument for expanding the policy goals of the structure to move renewable energy development forward.

Perhaps an early signal of traction for expanding the role of MLPs in our domestic energy policy, following introduction of the Master Limited Partnerships Parity Act by Senator Chris Coons (D-DE) in June 2012. The bill, which was co-sponsored by 11 senators (including Sen. Murkowski) and three House members across both parties, seeks to give all sources of domestic energy– both renewable and non-renewable – access to the MLP structure. The intended effect of harmonization of the qualifying income definition would be to attract significant new private investment into renewable energy sources that in turn will allow free markets to determine the relative merits of a wide array of energy options.

Further confirmation of what we have been hearing, as

our most recent conversations with federal legislators have suggested strong appreciation of the MLP structure. The prevailing view from our recent Washington D.C. trip with institutional clients to meet Congressional members/staffers and regulatory agencies was a clear sign that MLP tax treatment was not an explicit target for tax reform. In a departure from previous years, awareness of the MLP structure now appears widespread and acknowledgment of its important role in infrastructure investment, job creation and energy independence was expressed consistently. We walked away from meetings with a belief that both MLP tax treatment was at much lower risk of alteration than perceived by the market and that expansion of the MLP structure to include renewable energy was a materially higher probability than generally assumed by market participants. Expansion of the qualifying income definition if both strong reaffirmation of the permanence of the MLP structure and a harbinger of the next steps in its evolution as a distinct asset class similar to the REIT structure.

MLP Discussion from Sen. Murkowski's
"Energy 20/20" White Paper
Clean Energy Technology
Master Limited Partnerships (p.79)

"Easy and affordable access to capital is critical for any sustainable industry in the free market. Large corporations with established track records, including many energy companies, are able to tap these sources of funds. The task is much harder for smaller companies with unproven technology and unsteady cash flows. Such can be the plight of renewable energy. The challenges of capital formation are also a factor for highly regulated companies, such as energy pipelines. The United States should do what it can – especially within the context of free markets and private investment – to help companies that are developing alternative sources of energy.

The master limited partnership (MLP) is a special business structure that permits a company to raise capital like a corporation but pay taxes like a partnership. Instead of paying corporate income tax, a company distributes its cash flow on a quarterly basis to its investors, who can buy in on the public market and pay their own taxes on these distributions. Companies that have the steady cash flows of pipelines and similar operations have found MLP status to be helpful.

Renewable energy companies, with a few exceptions, are not eligible for the MLP structure and are not able to take advantage of a business framework that holds advantages in both capital-raising and taxation. In order to offer MLPs to renewable energy companies, Congress should:

¬ Consider wholesale reform of the Internal Revenue Code as part of a broader approach to resolve inconsistent tax characteristics within the energy sector.

¬ Make MLPs more widely available by amending the Internal Revenue Code of 1986 to extend the MLP structure to include biodiesel, biomass, hydropower, solar, wind, and virtually every other kind of alternative energy source, with the exception of nuclear energy.”