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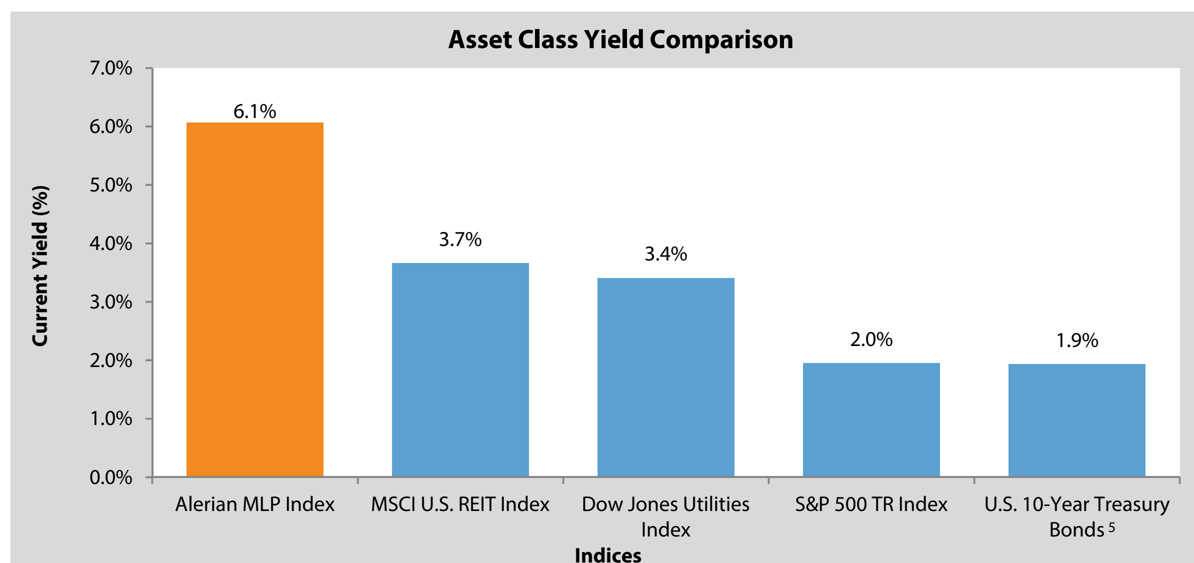
# 1. Introduction

Master Limited Partnerships ("MLPs") are a unique asset class in the investment landscape. They have historically generated competitive total returns (approximately 13.2% annually since 2006) through a combination of current yield and growth in distributions, while also providing portfolio diversification and a potential hedge against inflation.[1,2] Historically, MLPs have been primarily owned by high net worth and retail investors due in part to the tax complexities. However, MLPs have started to gain a wider acceptance amongst institutional investors as many MLP-focused vehicles (total return swaps, ETFs, ETNs, mutual funds, etc.) have been introduced to the marketplace that are designed to minimize the tax reporting issues that had previously hindered institutional ownership.

## Attractive Yields Compared to the Alternatives

Perhaps the best known benchmark for MLPs is the Alerian MLP Index (AMZ), which formally launched in June 2006. On March 31, 2015, the yield on the AMZ was 6.1%,[3] which was greater than utilities, REITs, the S&P 500, and Treasuries.[4]




For illustrative purposes only. Past performance is not necessarily indicative of how the indices will perform in the future. The indices reflect the reinvestment of dividends and income and do not reflect deductions for fees, expenses, or taxes. The indices are unmanaged and are not available for direct investment. Source: Bloomberg at March 31, 2015.

[1] Pertrac, April 2015.

[2] The Federal Energy Regulatory Commission allows certain tariff-based MLPs to increase their pipeline fees according to the Producer Price Index (PPI), and many storage contracts adjust to the Consumer Price Index (CPI), so a rise in inflation may be partially offset by these pricing abilities.

[3] Alerian Capital Management, March 2015. The AMZ yield is calculated by income divided by current price. MLP distributions are not guaranteed and subject to change based on market or other conditions. All or a portion of MLP distributions may be considered a return of capital.

[4] Bloomberg, March 2015.

[5] U.S. treasury bonds are guaranteed by the U.S. government and, if held to maturity, offer a fixed rate of return and guaranteed principal value. U.S. treasury bonds are issued and guaranteed as to the timely payment of principal and interest.

Please see the glossary for a list of terms and index definitions.

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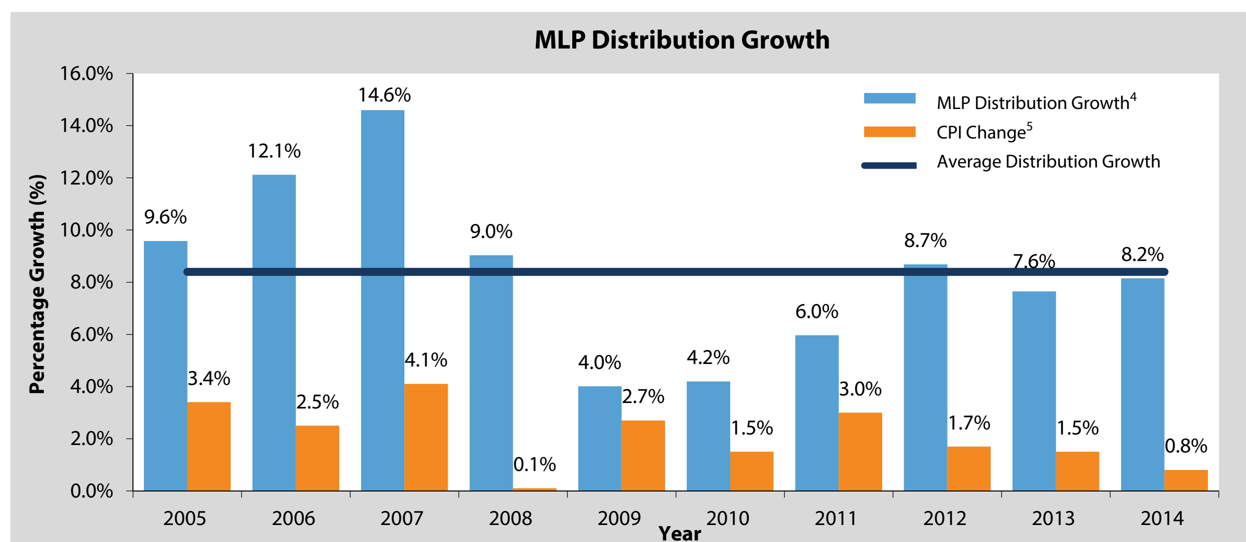
## Distribution Growth Has Exceeded Inflation

Since 2005, distribution growth for MLPs has averaged 8.4%,[1] which has been approximately 3.8x higher than the average rate of inflation (2.2%) as measured by the Consumer Price Index (CPI).[2] Growth has come from a combination of organic growth and acquisitions, and recent shale discoveries have provided an additional avenue for growth. It is also worth mentioning that certain types of pipelines that are regulated by the FERC (Federal Energy Regulatory Commission) – particularly interstate crude and refined products pipelines – are able to increase their tariffs annually at Producer Price Index-Finished Goods (PPI-FG) +2.65% through 2015, which provides a potential inflation hedge for those businesses.[3]




For illustrative purposes only. Past performance is not indicative of future results.

[1] Barclays Research estimate, March 2015. Average annual distribution growth rate is calculated by taking the total distribution growth per year and then calculating the average since June 2005 to March 2015. MLP distributions are not guaranteed and subject to change based on market or other conditions. All or a portion of MLP distributions may be considered a return of capital. The Barclays MLP coverage universe is inclusive of all MLPs covered by Barclays Research, which may differ meaningfully from the overall MLP universe.

[2] Bloomberg, March 31, 2015.

[3] Federal Energy Regulatory Commission (FERC), April 2012.

[4] Barclays Research estimate on MLP distribution growth per Barclays MLP coverage universe, as of December 2014. The MLP distribution growth rate is the rate at which an MLP grows its distribution. An individual MLP's annual distribution growth rate is calculated by dividing its Year 1 distribution by its Year 0 distribution and subtracting 1 (dist yr 1/dist yr 0-1). The Barclays MLP coverage universe is inclusive of all MLPs covered by Barclays Research, over the review period, which may differ meaningfully from the overall MLP universe.

[5] Citi Investment Research and Analysis as of March 31, 2015. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.

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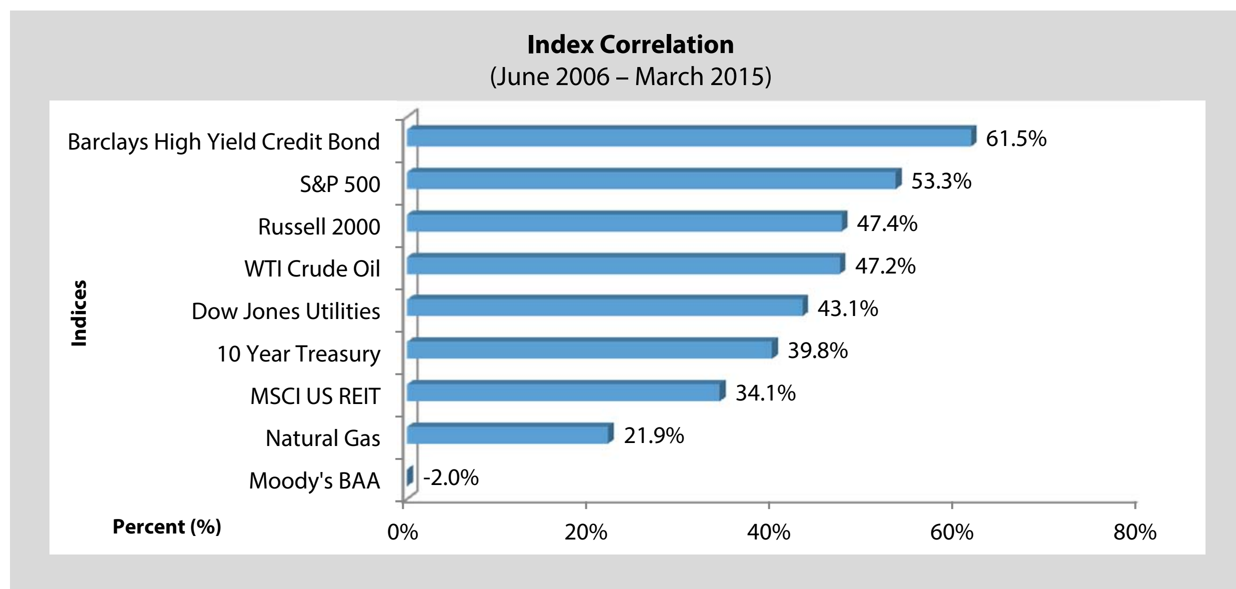
### Correlations (or Lack Thereof)

MLPs may be valuable to the portfolio construction process since they typically do not exhibit high correlations with other asset classes. As shown in the graph below, the highest correlation since June 2006 has been to high yield bonds (62%), while the correlation to the S&P 500 has been 53%.[1] The relatively low correlation to oil and gas prices often surprises investors as well.




For illustrative purposes only.
Past performance is not necessarily indicative of how the indices will perform in the future.
The indices reflect the reinvestment of dividends and income and do not reflect deductions for fees, expenses, or taxes.
The indices are unmanaged and are not available for direct investment.
Source: Pertrac, March 31, 2015.

# 2. What is an MLP?

### Section 7704 of the U.S. Tax Code

An MLP is a publicly-traded partnership that receives special treatment under the U.S. tax code. Specifically, MLPs do not have to pay income taxes at the corporate level if 90% or more of gross income is considered to be "qualifying." Note that the 90% requirement for MLPs is related to *income generation*. Unlike REITs, there is not a requirement that MLPs *pay out* 90% of net income (or cash flow). In fact, MLPs are not required to pay out *any* distributions. This distinction is often misunderstood and/or misrepresented.

Section 7704 of the tax code defines qualifying income as "income and gains derived from the exploration, development, mining or production, processing, refining, transportation (including pipelines transporting gas, oil, or similar products), or the marketing of any mineral or natural resource

[1] Pertrac, June 2006 – March 2015.

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(including fertilizer, geothermal energy, and timber)." As a result, the vast majority of MLPs are related to energy and natural resources.

The IRS has been more accommodating in its definition of what constitutes "qualifying income" as demonstrated by a surge in the number of private letter rulings (PLRs) in recent years. The chart below shows the number of PLRs issued from 2004 through 2014, which averaged 4.6 per year.[1] The numbers jumped to 18 in 2012 and 28 in 2013, and nine were issued in 2014 before the IRS announced a moratorium on additional PLRs in March 2014.[2] On March 6, 2015, the IRS lifted its moratorium but provided little guidance as to how its procedures had evolved during the pause. The IRS is expected to publish its new regulations in 3Q15.

For illustrative purposes only.
Source: Wells Fargo, April 2014.

Ownership of an MLP consists of the general partner and the limited partners. The general partner manages the partnership and typically has unlimited liability in legal matters. The limited partners are the primary providers of capital and receive cash "distributions" (not "dividends") from the partnership, but they are only liable to the extent of their investment as it relates to legal matters. The limited partners' ownership is in the form of common "units" (not "shares"), which trade publicly on stock exchanges. In addition, several general partners are publicly-traded – some structured as MLPs and some as C-Corporations.

MLPs are designed to be a more tax efficient structure than the traditional corporation since they seek to avoid double taxation. In general, MLPs do not pay income tax at the corporate level. Instead, unit holders pay taxes at ordinary income tax rates on a portion of the distributions they receive. For more information on taxation, see page 19.

[1] Source: Wells Fargo, April 2014.
[2] Reuters, April 2014.

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## Current Thoughts on Tax Status

It is no secret that the U.S. has been running some rather large budget deficits over the past several years. As a result, there has been increased debate about an overhaul of the tax code in order to increase tax revenues to help reduce the deficit. While the tax status of MLPs has not been specifically targeted, a complete overhaul of the tax system could potentially impact MLPs. We believe there are several items worth pointing out regarding this topic.

First, in March 2015, the Joint Committee on Taxation ("JCT") published its latest report on estimated tax "expenditures" (i.e. tax breaks) for the House Ways and Means and the Senate Finance Committee. In that report, the JCT estimated the expenditure related to MLPs to be $1.16B over five years ($232mm annually).[1] This latest figure is substantially below last year's estimate of $1.2 to $1.5 billion per year. The federal budget for 2015 is expected to approach $3.7 *trillion,* which means that taxing MLPs would only cover roughly .006 of 1% of the federal outlay if the JCT's estimate is correct.[2] The amount of revenue raised would literally be a rounding error in the context of Washington spending.

Second, the current administration has been vocal about the need for both energy independence and infrastructure in the United States. MLPs may be seen as key conduits in achieving both of these goals and have the added potential benefit of creating jobs. Interestingly, in April 2013, the administration proposed exempting foreign pension funds from federal taxes under the Foreign Investment in Real Property Tax Act (FIRPTA). We interpret this to be a sign of how serious the government is about rebuilding infrastructure, and if enacted, may clear the way for non-U.S. pensions to invest in infrastructure (including energy infrastructure). Now if only they would get rid of the Unrelated Business Taxable Income!

Third, we do not believe that the current ideological divide in Congress is conducive to the bipartisan cooperation necessary to enact major legislative reforms. There have been several bitterly partisan moments in recent years (executive amnesty, government shutdown in October 2013, fiscal cliff in December 2012, tax ceiling issue in summer 2011 just to name a few). Tax reform could prove to be a very lengthy, contentious process. And, in our opinion, the tax status of MLPs is unlikely to be changed without a complete overhaul of the U.S. tax code.

Fourth, between the proposed "MLP Parity Act" and the proliferation of IRS private letter rulings cited earlier, the bias has been toward expanding the definition of "qualifying income" under Section 7704 – not eliminating it. The MLP Parity Act proposes to allow wind, solar, and other renewable energy sources to be treated as qualifying income. Despite bipartisan sponsorship, this legislation has stalled in Congress primarily because there are higher priority items on the agenda. In the meantime, some power generation companies have gone forward with creating an MLP-like structure known as a "yield-co" for some of their assets.[3] For instance, utility NRG Energy (NYSE: NRG) created NRG Yield (NYSE: NYLD) in July 2013 to own several of its power generation assets that have long-term contracts. We have seen four other yield-co's come public since NYLD as the space continues to grow.

[1] Source: Credit Suisse, March 9, 2015.
[2] Source: whitehouse.gov, February 2015.
[3] Yield Co. is a publicly traded company that is formed to own operating assets that produce a predictable cash flow.

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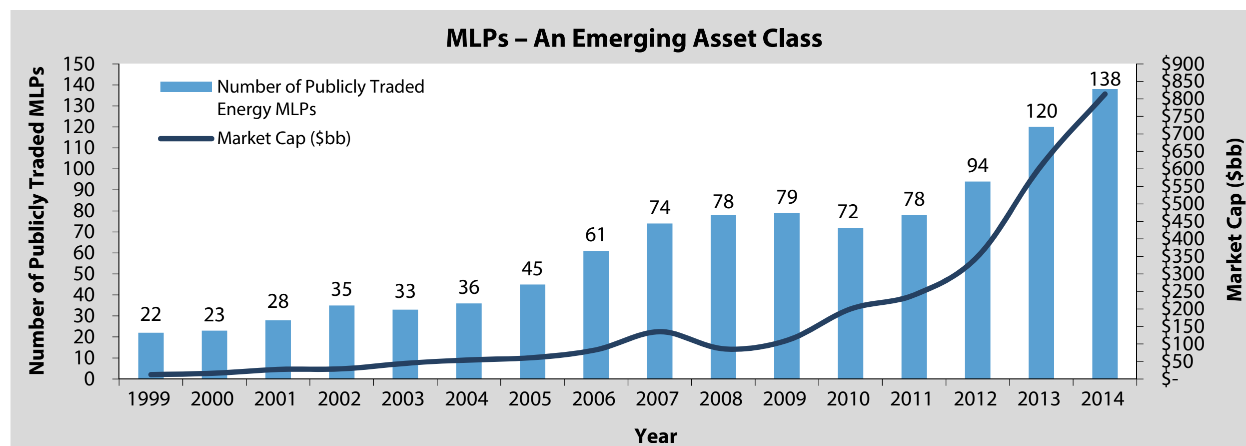
## The Evolution and Size of the Space

Prior to 1997, the MLP space was primarily comprised of long haul pipeline and propane MLPs that generated stable cash flow but were generally not concerned about distribution growth. As a result, MLPs tended to trade like bond substitutes. In early 1997, Rich Kinder and Bill Morgan changed the game when they formed Kinder Morgan Energy Partners, L.P. ("Kinder Morgan") after acquiring liquids pipeline assets from Enron Corporation. Kinder Morgan is often cited as the "original growth MLP", as the partnership grew very rapidly by acquiring third party midstream assets. We believe growth is now one of the primary goals of many MLP management teams.

Historically, companies with predictable fee-based cash flow streams (such as pipelines) have been the norm in the MLP space. After all, the objective is to provide investors with steady (and potentially increasing) distributions. However, over the last several years, a number of MLPs have come to market that have direct exposure to commodity prices including oil, natural gas, natural gas liquids ("NGLs"), and coal. In fact, there are now six refining MLPs, 12 Exploration & Production ("E&P") MLPs, and four coal producers structured as MLPs. Oil service MLPs and some one-off businesses are also new to the MLP structure, with two frac sand producers, two offshore drillers, a petroleum coking facility, an ethylene plant, and a soda ash mining MLP having gone public over the past few years.[1]

We believe that the ability of a partnership to hedge its commodity exposure has been a major contributor to more commodity sensitive businesses forming MLPs. Hedging essentially allows a partnership to turn a highly volatile cash flow stream into more predictable near term cash flows, which we think are essential in the MLP structure. However, even those businesses that have hedged their commodity exposure in the near term face "rollover risk" in future years when those hedges expire. If commodity prices turn downward, those companies could have issues in the future. During the financial crisis of late 2008 and the crude oil price correction of mid-2014 to early 2015, these partnerships were among the worst performers due to such concerns.

As of December 31, 2014, there were approximately 120 publicly-traded energy MLPs with a total market capitalization approaching $500 billion. When C-Corp general partners are included, the universe is 138 names with a market cap of roughly $814 billion.[2]




For illustrative purposes only. Past performance is not indicative of future results. There are certain tax risks associated with an investment in MLP units and conflicts of interest exist between common unit holders and the general partner of the MLP.
Source: Salient Capital Advisors, LLC, March 31, 2015.

[1] Securities and Exchange Commission (www.sec.gov), January 2014.
[2] Alerian Capital Management, March 2015.

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Generally, MLPs fall in the small- to mid-cap category. As of December 31, 2014, only 13 MLPs had a market capitalization of greater than $10 billion, 36 MLPs fell between $2 and $10 billion, and the rest were below $2 billion. The average market cap as of that date was $4.1 billion, while the median market cap was only $1.4 billion. Note that the one remaining mega-cap MLP – Enterprise Products ($67.1 billion market cap) skews the average calculation.[1]

In general, MLPs can be categorized into ten different "subsectors" based on the type of assets owned and products transported:

- **Diversified.** The Diversified MLPs are generally large cap in nature and operate in several of the subsectors listed below.

- **Natural Gas Pipelines & Storage.** MLPs in this subsector own both interstate and intrastate natural gas pipelines and/or natural gas storage. Historically, natural gas pipelines have generated stable cash flow due to long-term contracts with a large "take or pay" component. Natural gas storage has been a weak spot over the past few years due to a combination of lower natural gas prices, lower volatility in the natural gas curve, and a lack of basis between hubs. The emergence of the Marcellus Shale in recent years has re-routed the historical flow of natural gas in the U.S. For decades, natural gas was produced in the Midwest and Gulf Coast and shipped via pipeline to the heavily populated northeastern states. However, Marcellus production has been so strong that the northeast only needs natural gas in the winter months when demand is highest and actually has a surplus of gas during the other months. The owners of those pipelines are now actively gauging interest in reversing flow on existing pipelines and/or scoping new projects to deliver Marcellus gas to other regions.

- **Liquids Pipelines & Storage.** Crude oil and refined products pipelines and storage fall into this category. Revenues are largely fee-based, and for interstate pipelines, the FERC allows a PPI-FG + 2.65% tariff increase every year through 2015 which provides a potential inflation hedge.[2] Crude pipelines have experienced a renaissance of late due to new shale discoveries (Bakken, Eagle Ford, Niobrara), while the associated marketing and logistics businesses have profited by the wide differentials between WTI (West Texas Intermediate) and Brent crude prices.

- **Gathering & Processing ("G&P").** G&P MLPs aggregate natural gas from multiple wells in a field and deliver it to a processing plant that removes NGLs. Historically, G&P has been one of the more commodity-sensitive subsectors due to keep-whole, percent-of-liquids (POL), and percent-of-proceeds (POP) contract structures through which the processors were long or short natural gas and/or NGLs. As natural gas prices have collapsed over the last few years, many of these contracts have shifted to fee-based as E&P companies need proceeds from their NGL production to increase returns. As a result, there has been some natural de-risking in this subsector. In fact, there are now several G&P MLPs that are entirely fee-based, though they still face volumetric risks should drilling decline in their areas of operation.

[1] Salient Capital Advisors, LLC, FactSet, March 2015.
[2] Federal Energy Regulatory Commission (FERC), April 2012. The FERC resets this inflator every five years.

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- **Propane.** Propane MLPs typically have both wholesale and retail distribution divisions that sell propane for heating, crop drying, and cooking purposes. Volumes are highly dependent on the winter weather, while margins can swing based on wholesale propane prices and the ability/inability to pass those price changes through to customers.

- **Exploration & Production ("E&P").** E&P MLPs typically own long-lived reserves with low decline rates and focus more on production than exploration. Most hedge out a high percentage of expected production, but they are still highly exposed to commodity prices. Several E&P MLPs have cut their distributions thus far in 2015 due to the decline in crude oil and NGL prices.

- **Shipping.** Currently, there are 12 shipping MLPs that transport products such as liquefied natural gas ("LNG"), refined products, crude oil, and dry bulk. In addition, some of these MLPs own floating storage and LNG regasification vessels. Typically, the shippers have long-term, fee-based charters, but could face issues if those charters are renewed at lower rates.

- **Coal.** Currently, there are four coal production MLPs and two that own reserves that generate royalty revenues. In most cases, production is sold forward on multi-year contracts, but like E&P MLPs, coal MLPs face the risk of lower pricing once those contracts expire. Regulatory issues and escalating costs can also be a headwind for coal MLPs.

- **Refining & Marketing.** This subsector includes four refineries that convert crude oil into refined products (such as gasoline, diesel, and jet fuel) and two that produce fertilizer. We also include wholesale marketers of crude and refined products as well as the "convenience store MLPs" in this subsector.

- **Oil Service and Other Specialty.** The "Oil Service" portion of this subsector includes compression MLPs, producers of sand used in the hydraulic fracturing process, and two offshore drillers. The "Other" portion consists of MLPs that do not fit perfectly in any subsector like LNG plants, petroleum coking facilities, and other one-off MLPs.

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The graphic below touches on key characteristics inherent in some of the different types of businesses in the MLP structure.

| Cash Flow Stability | Type of Business | Contract Length | Revenue Type | Exposure to Commodity Prices | Types of Customers |
|---|---|---|---|---|---|
| Very High | Natural gas pipelines | 10+ Yrs | Rental fee / "Ship-or-pay" | Little | Gas distributors, Utilities, Producers, Marketers and other gas pipelines |
| | Crude oil pipelines | 5-10+ Yrs | Rental fee / Volume | Little | Refiners, Producers, Financials |
| | Storage | 3-5 Yrs | Rental fee / Volume | Little (forward curve, contango) | Utilities, Marketers, Financials |
| | Refined prod. pipelines | 1-5 Yrs | Rental fee / Volume | Little | Refiners, Marketers |
| | NGL pipelines | 1-5 Yrs | Rental fee / Volume | Little | Petrochemical plants, Producers |
| | Gathering | Ranging from month-to-month to life of lease dedications | Rental fee / Volume | Little | Producers |
| | Fractionation | Typically short-term contracts but trending more long-term | Fee-based / "Frac-or-Pay" | Little | Producers |
| | Terminals | 1-3 Yrs | Volume / Ancillary services | Little (contango) | Refiners, Financials |
| | Processing | Month-to-month to life of lease dedications | Fee-based / Volume | More (NGL prices, contract mix) | Producers |
| | Marine shipping | 1-3 Yrs | Fee-based / Indexed charter rates | Little | Refiners, Petrochemical companies, Integrateds, Marketers |
| Very Low | E&P | -- | Market rates / Hedging | Significant | Midstream operators |

For illustrative purposes only.
Source: Morgan Stanley, March 2015.

## Why Do Companies Put Assets into MLPs?

Early on, companies formed MLPs in order to divest assets and focus on core competencies. In the late 1980s, many large energy companies found that they had significant amounts of capital tied up in cash-generating assets such as pipelines. Since the income from those assets typically met the definition of qualifying income, energy companies sought to monetize those assets and create a more efficient capital structure for their ownership in these assets. Placing those assets into a publicly-traded partnership structure enabled many owners to be compensated for those assets and focus on their core competencies.

While that is still a motivation for many companies, we believe several issuers are now simply exploiting the valuation gap. Because of their tax structure and yield-oriented nature, MLPs have a lower cost of capital which typically leads to higher market valuations (and vice versa). For instance, let's say that a traditional E&P company that also owns high quality pipeline assets trades at an EBITDA (earnings before interest, taxes, depreciation, and amortization) multiple of 6x, while MLPs with similar assets trade at 14x. Given the major difference in valuation, the company would be highly motivated to either form its own MLP or sell the assets to an existing MLP to maximize shareholder value. This valuation discrepancy has been the motivation behind the formation of MLPs such as Williams Partners, L.P. (natural gas pipelines), Western Gas Partners, L.P. (gathering & processing), Phillips 66 Partners, L.P. (liquids transportation & storage), and Teekay LNG Partners, L.P. (shipping). Even the majors have started to form MLPs, as Royal Dutch Shell formed Shell Midstream Partners in late 2014.[1]

By spinning out qualifying assets, the parent company is typically able to receive cash upfront while maintaining operational control and a meaningful financial stake in the assets through ownership of common units, the general partner interest, and incentive distribution rights.

[1] Source: Company filings, October 2014.

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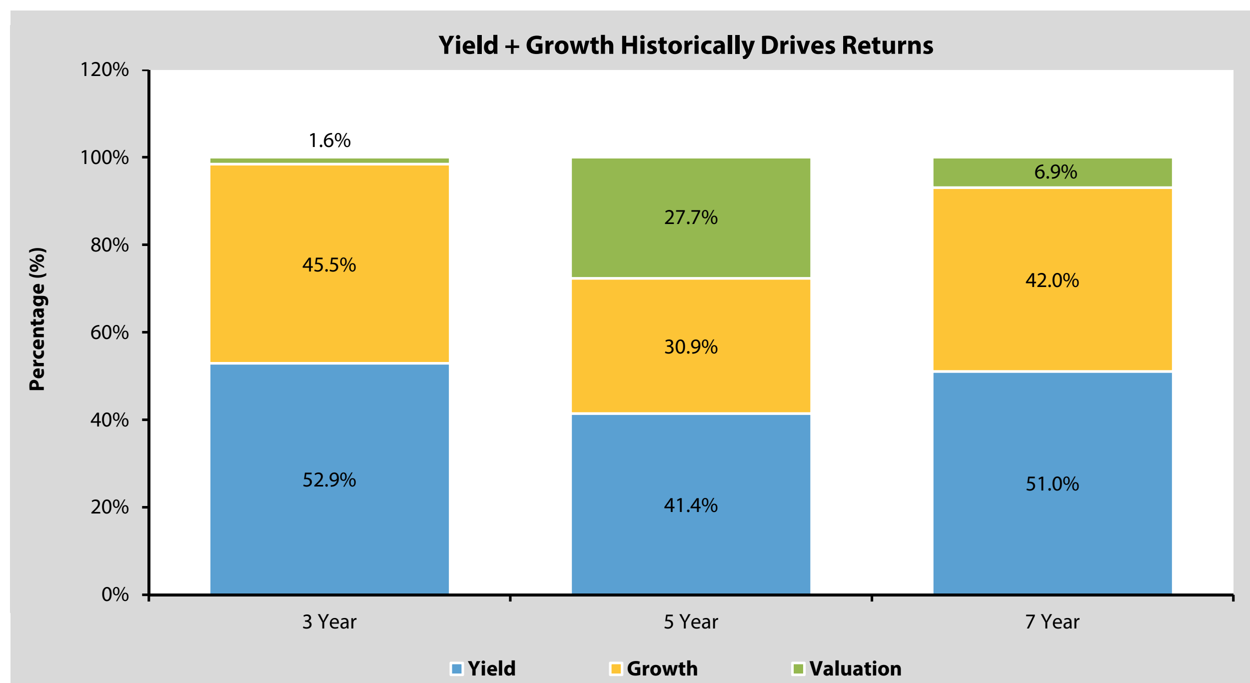
# 3. The MLP Value Proposition

Over the past seven years, MLPs have generated attractive total returns through a combination of high current yield and growth in distributions.[1] In fact, according to Barclays Capital, this yield plus growth equation has explained 98.4% over the past three years, 72.3% over the past five years, and 93.0% of the MLP total returns over the past seven years (with the remainder due to changes in yield/valuation). Note that the five year returns (2010–2014) were more driven by revaluation as MLPs continued to recover following the 2008/2009 financial crisis.




For illustrative purposes only. Past performance is not indicative of how the index may perform in the future. The index reflects the reinvestment of dividends and income and does not reflect deductions for fees, expenses, or taxes. The index is unmanaged and not available for direct investment.
Source: Barclays Capital, March 31, 2015.
Please see the glossary for a list of terms.

[1] Past performance is not indicative of future results.

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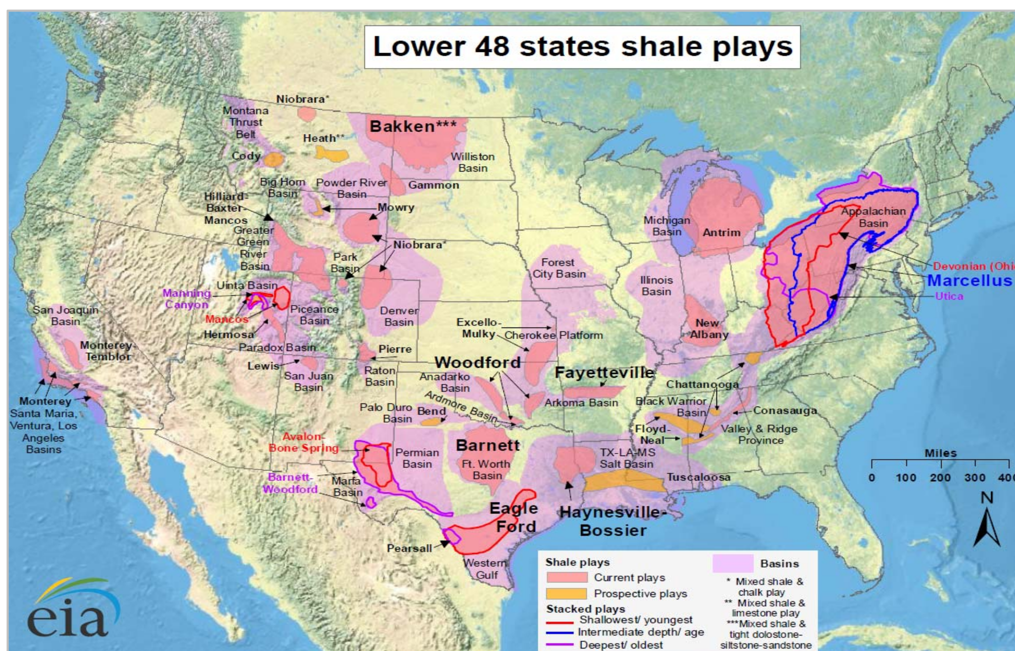
## Potential Opportunities for Growth

Historically, MLPs have typically increased their cash flow through a combination of organic growth projects and acquisitions. Over the last decade, one of the key drivers of growth for MLPs has been the need for infrastructure resulting from the discovery of numerous shale plays (both crude oil and natural gas). The graphic below shows the major producing basins, including recent shale discoveries.




For illustrative purposes only.
Source: Energy Information Administration based on date from various published studies. Updated May 9, 2011.

To put some numbers to the growth potential, ICF International (on behalf of the Interstate Natural Gas Association) published an updated report on future North American energy infrastructure needs and capital spending in March 2014. In its report, ICF estimates that infrastructure expenditures will total $640.9 billion between 2014 and 2035. This estimate is significantly higher than its original estimate (in June 2011) of $261.0 billion, with the lion's share of the increase occurring in crude oil infrastructure spending. On average, annual natural gas capital expenditures are expected to be $14.2 billion over the next 21 years ($313.1 billion in total), while crude oil and NGL-related capex is expected to average $15.0 billion ($327.8 billion in total). MLPs may account for a significant portion of the spending, which could bode well for long term growth. The table below summarizes the findings of the study.

| Estimated Midstream Infrastructure Expenditures Through 2035 | | | | |
|---|---|---|---|---|
| Billions of Real Dollars | Current Estimate 2014 – 2035 (2012$) | Current Study Average Annual (2012$) | Prior Study 2011 – 2035 (2012$) | Prior Study Average Annual (2012$) |
| Natural Gas | **$313.1** | **$14.2** | **$213.3** | **$8.5** |
| NGLs | **$56.0** | **$2.6** | **$15.1** | **$0.6** |
| Crude Oil | **$271.8** | **$12.4** | **$32.6** | **$1.4** |
| Total | $640.9 | $29.2 | $261.0 | $10.5 |

For illustrative purposes only. Estimates provided are subject to change without notice. Actual results may materially differ from those provided.
Source: "North American Midstream Infrastructure through 2035 – A Secure Energy Future" by ICF International, March 2014.

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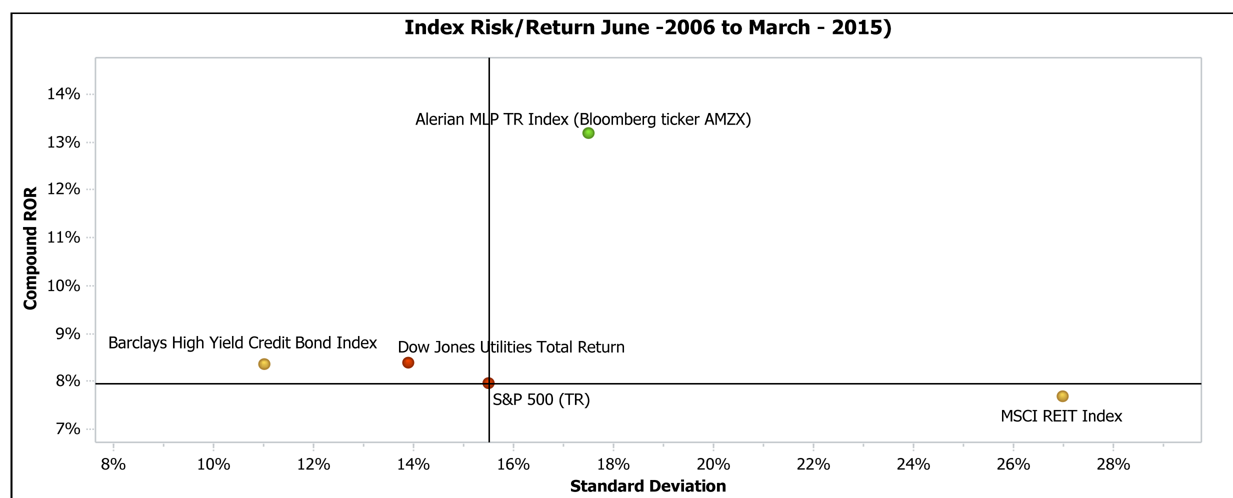
## Relative Performance vs. Alternative Yield Investments

MLPs have outperformed the S&P 500 and other yield-based investments on a total return basis since the inception of the AMZ in June 2006. As shown in the graph below, the Alerian MLP Index has returned 13.2% annually since 2006 as compared to the S&P 500 annual return of 8.0%, with only a slightly higher standard deviation than the S&P 500 (17.5% vs. 15.5% for the S&P 500). The Alpha (9.2%), Beta (0.58), and Sharpe Ratio (0.70) metrics also compare favorably to the S&P 500.




| June-2006 to March-2015 | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Compound ROR | Cumulative Return | Standard Deviation | Max Drawdown | Sharpe Ratio (1.81%) | Sortino Ratio (10%) | Up Capture Ratio | Down Capture Ratio | Alpha | Beta |
| Alerian MLP TR | 13.2% | 198.5% | 17.5% | -41.1% | 0.70 | 0.24 | 67.0% | 68.1% | 9.1% | 0.58 |
| Barclays High Yield Credit Bond | 8.4% | 103.2% | 11.0% | -33.3% | 0.62 | -0.18 | 34.1% | 58.3% | 4.1% | 0.52 |
| Dow Jones Utilities | 8.4% | 103.3% | 13.9% | -36.4% | 0.52 | -0.14 | 35.6% | 60.5% | 4.9% | 0.48 |
| MSCI REIT | 7.7% | 92.0% | 27.0% | -69.2% | 0.35 | -0.11 | 161.2% | 110.2% | -0.4% | 1.30 |
| S&P 500 TR | 7.9% | 96.5% | 15.5% | -50.9% | 0.46 | -0.16 | 100.0% | 100.0% | 0.0% | 1.00 |

For illustrative purposes only. Past performance is not necessarily indicative of how the indices will perform in the future. The indices reflect the reinvestment of dividends and income and do not reflect deductions for fees, expenses or taxes. The indices are unmanaged and are not available for direct investment.
Please see the glossary for a list of terms and index definitions.
Source: PerTrac, Data from June 2006 – March 2015.

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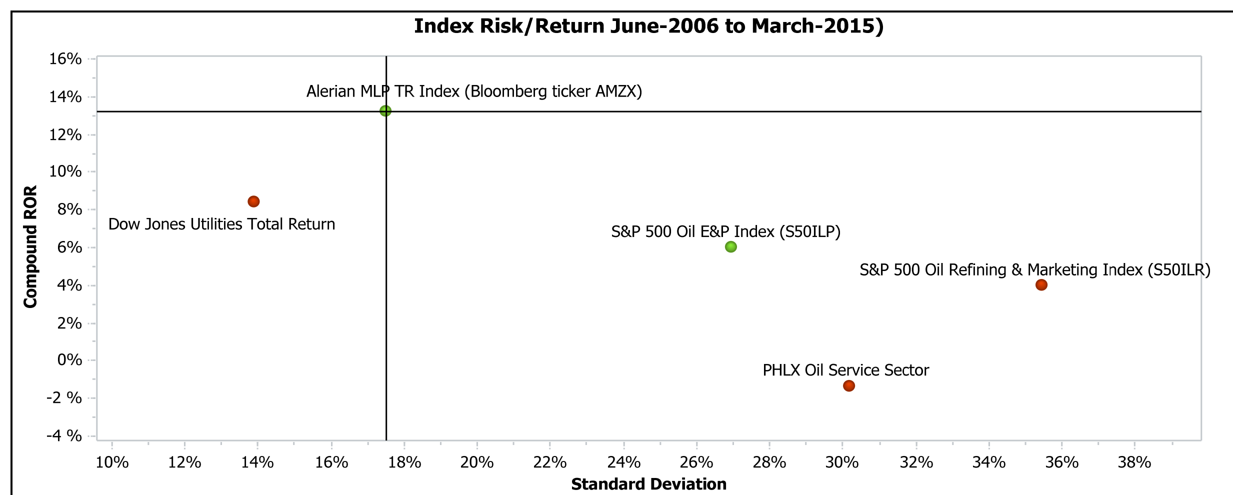
## Risk-Adjusted Returns vs. Other Energy Sectors

In addition to outperforming the S&P 500 and other yield-based investments (as shown in the previous graph), MLPs have also generated the highest risk-adjusted returns among other energy sectors. The annualized return of the AMZ (13.2%) has been higher than utilities, E&P, oil service, and refining, as defined by the indices in the graph below. While utilities did exhibit lower volatility than the AMZ, we would note that the standard deviation of the AMZ has been much lower than those of the more commodity-sensitive, cyclical sectors.




June-2006 to March-2015

| | Compound ROR | Cumulative Return | Standard Deviation | Max Drawdown | Sharpe Ratio (1.81%) | Sortino Ratio (10%) | Up Capture Ratio | Down Capture Ratio | Alpha | Beta |
|---|---|---|---|---|---|---|---|---|---|---|
| Alerian MLP TR | 13.2% | 198.5% | 17.5% | -41.1% | 0.70 | 0.24 | 67.0% | 68.1% | 9.1% | 0.58 |
| PHLX Oil Service Sector | -1.3% | -11.2% | 30.2% | -66.2% | 0.05 | -0.46 | 94.0% | 114.5% | -8.5% | 1.39 |
| S&P 500 Oil E&P | 6.0% | 67.4% | 27.0% | -59.5% | 0.29 | -0.18 | 103.1% | 104.8% | -0.3% | 1.11 |
| S&P 500 Oil Refining & Marketing | 4.0% | 41.1% | 35.5% | -75.3% | 0.24 | -0.21 | 211.7% | 117.8% | -1.6% | 1.35 |
| Dow Jones Utilities Total Return | 8.4% | 103.3% | 13.9% | -36.4% | 0.52 | -0.14 | 35.6% | 60.5% | 4.9% | 0.48 |

For illustrative purposes only. Past performance is not indicative of how the index may perform in the future. Indices are unmanaged, and investors cannot invest directly in an index. Index performance does not reflect the deductions of fees and expenses.
Please see the glossary for a list of terms and index definitions.
Source: PerTrac, Data from June 2006 – March 2015.

# 4. Partnership Structure

MLP ownership is comprised of the general partner and the limited partners. The general partner manages the partnership and typically owns some common units, the 2% general partner interest, and the incentive distribution rights. The limited partners are the primary providers of equity capital and typically receive quarterly cash distributions from the partnership. The limited partners' ownership is in the form of publicly-traded common units and several general partners are publicly-traded as well (some structured as MLPs and some as C-Corporations). The graphic on the following page shows a typical MLP organizational structure.

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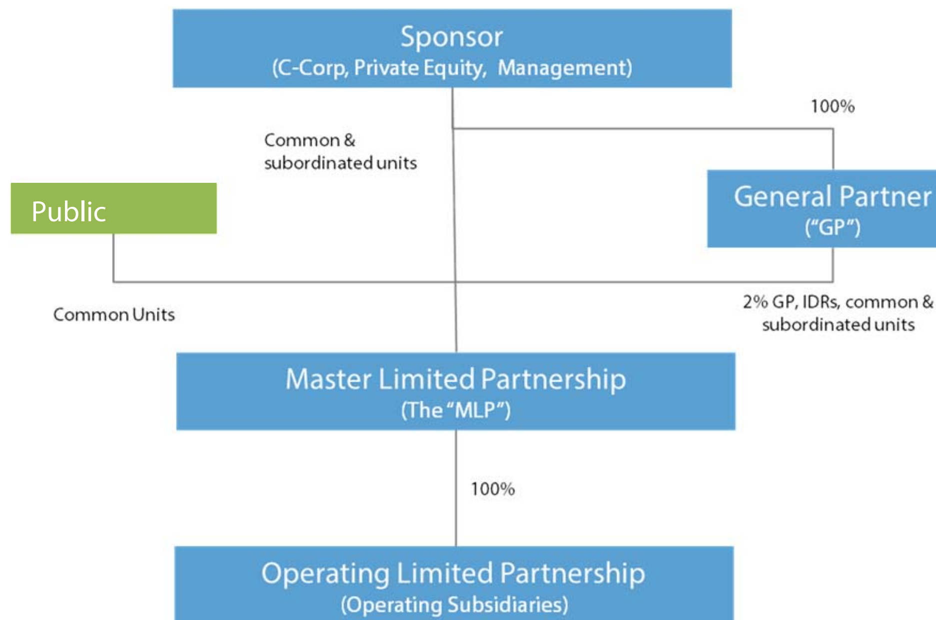


For illustrative purposes only.
Source: Salient Capital Advisors, LLC.

## Governance: The "Limited" in Limited Partner

MLPs are managed by the general partner, and in most cases, limited partners have limited voting rights regarding partnership matters such as acquisitions and electing the board of directors. Further, removing the general partner can be very difficult and often requires a 66 $^{2}/_{3}$% majority vote of the common unit holders, sometimes including the common units owned by the general partner. That said, major stock exchanges typically require at least three independent members on the general partner's board of directors and the general partner does have certain fiduciary duties to the limited partners.

## The Mechanics of Incentive Distribution Rights ("IDRs")

MLP management teams are strongly incentivized to increase quarterly distributions to unit holders. Under the MLP structure, management is represented by the general partner, which typically has a 2% cash flow interest. Even though the equity stake of the GP is small, IDRs provide substantial upside and encourage the GP to grow distributions to unit holders as quickly as possible. As distributions increase and certain targets are met, the general partner receives a larger percentage of the incremental distributions.

In general, the tiers are set at 15.0%, 25.0%, and 50.0% above the minimum quarterly distribution (some cap the IDRs at 25.0%, some don't have IDRs at all). Perhaps not coincidentally, the general partner receives that same percentage of incremental distributions once the tier is surpassed. In other words, if distributions were increased by 15.0%, the general partner would receive 15.0% of the incremental distributions above that level.

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By way of illustration, the table below shows a typical IDR structure for an MLP.

| Typical MLP Incentive Distribution Rights Structure | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Distribution Schedule | | | % Split | | Incremental Distributions | | Total Quarterly Distributions | | | |
| | Quarterly | Annually | L.P. | G.P. | L.P. | G.P. | L.P. | G.P. | TOTAL |
| | MQD of $0.35 | $1.40 | 98% | 2% | $0.3500 | $0.0071 | $0.3500 | $0.0071 | $0.3571 |
| Tier 1 | up to $0.4025 | $1.61 | 98% | 2% | $0.0525 | $0.0011 | $0.4025 | $0.0082 | $0.4107 |
| Tier 2 | above $0.4025 to $0.4375 | $1.75 | 85% | 15% | $0.0350 | $0.0062 | $0.4375 | $0.0144 | $0.4519 |
| Tier 3 | above $0.4375 to $0.5250 | $2.10 | 75% | 25% | $0.0875 | $0.0292 | $0.5250 | $0.0436 | $0.5686 |
| Tier 4 | above $0.5250 | > $2.10 | 50% | 50% | $0.0250 | $0.0250 | $0.5500 | $0.0686 | $0.6186 |
| % of Total Distribution | | | | | | | 88.9% | 11.1% | |

For illustrative purposes only.
Source: SEC Filings; Tier 4 assumes $2.20 annual distribution to limited partners.
Please see the glossary for a list of terms and definitions.

Let's assume that "MLP" went public in January 2005 with a minimum quarterly distribution (MQD) of $0.35 per unit. At the MQD level, the MLP unit holders receive a quarterly distribution of $0.35 per unit, while the general partner receives $0.0071 per unit, or 2% of the total distribution.

From the MQD to the top-end of the first tier of distributions ($0.4025 per unit), the general partner receives 2% of the total distribution, for a total quarterly distribution between MLP unit holders and the general partner of $0.4107 per unit.

At the high end of the second tier, the MLP limited partners will receive $0.4375 per unit ($1.75 annually). This represents 98% of the tier one distribution and 85% of the distributions beyond that amount. The general partner will receive a total of $0.0144 per unit, for a total distribution between the LP and GP of $0.4519 per unit.

At the high end of the third tier, the MLP limited partners will receive $0.525 per unit ($2.10 annually) while the general partner will receive a total of $0.0436 per unit, for a total distribution between the LP and GP of $0.5686 per unit.

At distribution levels above $0.525 per unit, the MLP limited partners and the general partner will each receive 50% of the incremental distributions. For example, if the quarterly distribution was increased to $0.55 per unit, both the limited partners and the general partner would receive an additional $0.025 per unit as shown in the table above.

## Impact of IDRs on MLP Cost of Equity

To put it simply, IDRs increase a partnership's cost of equity capital. As shown in the example above, the general partner receives an increasing portion of the distributions as the distribution to limited partners grows over time. Once a partnership reaches the 50% splits (Tier 4 in the table above), it has to increase distributable cash flow by $0.02 per unit in order to increase distributions to limited partners by $0.01 (since the general partner receives $0.01 as well).

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In the example on the previous page, the partnership has to generate almost $0.62 per unit of cash flow to pay a $0.55 distribution to limited partners, and that is based on a partnership being only slightly ($0.025 per unit) into the high splits. If the distribution to limited partners were to increase to $3.00 per unit ($0.75 per quarter) in the example above, the partnership would have to generate cash flow of almost $1.02 per quarter after accounting for the general partner. Clearly, the general partner IDRs come at a cost to an MLP's limited partners; and the IDRs are also the reason that publicly-traded general partners may be such powerful growth stocks.

Due to the impact on an MLP's cost of equity, several MLPs have bought out their general partner IDRs in recent years by issuing additional limited units to the general partner in lieu of the IDRs. For the most part, distribution growth rates have increased over time for those MLPs subsequent to the IDR buyout.

Kinder Morgan, however, flipped the script. We believe a non-competitive cost of equity was arguably the key driver behind the $140 billion consolidation of the Kinder Morgan companies in 2014.[1] Kinder Morgan Energy Partners (KMP, the underlying MLP) had essentially become a victim of its own success and had raised its distribution so deep into its 50/50 splits that the IDR burden paid to Kinder Morgan Inc. (KMI) had become, well, burdensome. At the time of the consolidation, KMI was receiving ~$0.46 of every dollar distributed by KMP. This had the effect of raising KMP's cost of equity capital to roughly ~13%, which raised KMP's overall cost of capital despite having one of the highest credit ratings (lowest cost of debt) in the MLP space. Distribution growth had slowed considerably at KMP over the last few years and management felt that changes had to be made. What made the Kinder Morgan consolidation unique in our opinion was that the general partner, KMI, was the surviving entity and is a regular C-corp. Kinder Morgan management was banking on the idea that investors would continue to assign MLP-type valuation multiples to KMI despite the fact that it was not an MLP. Thus far at least, they have been proven correct.

## Investing in General Partners

We believe the same IDR dynamic that creates a headwind for MLP distribution growth also provides the potential for publicly-traded general partners to generate higher distribution (or dividend) growth. Not all general partners are publicly-traded, but there are currently several trading in both C-Corp form and MLP form. Note that the GPs that are structured as corporations may have to pay corporate level income tax.

Typically, general partners have lower yields but tend to grow their dividends or distributions by approximately 1.5x to 3x the rate of their underlying MLPs. The reason is fairly straightforward: operating leverage. General partners, in most cases, have very little general and administrative (G&A), interest, and other expenses. As the IDRs to the general partner increase, expenses typically do not increase by the same magnitude (if at all). Therefore, distributable cash flow and dividends/distributions to shareholders may grow at a faster rate.[2]

[1] Kinder Morgan (2014). Kinder Morgan Inc. to Purchase KMP, KMR and EPB; 2015 KMI Dividend to Increase $2 per Share [Press release]. Retrieved from http://phx.corporate-ir.net/phoenix.zhtml?c=93621&p=irol-newsArticle&ID=1957206&highlight=

[2] Salient Capital Advisors, LLC, March 2015.

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# 5. Tax Basics

MLPs pay distributions to unit holders in cash. However, since MLPs are pass-through entities, each limited partner unit is entitled to its share of the non-cash deductions (such as depreciation and amortization) associated with the business. The portion of these non-cash expenses allocated to the limited partners reduces taxable income on the distribution by an equal amount. However, the passive loss limitations under Section 469(k) of the Internal Revenue Code of 1986, as amended ("IRC") may affect the timing of when the deductions may be taken. In many cases, a new MLP may have a tax deferral of greater than 80%. In other words, for every dollar of cash received, only 20 cents is taxed at the unit holder's ordinary income rate in the year in which it is received.

It is important that investors understand that in general, ordinary deductions allocated to the investor will be recaptured as ordinary income when the units are sold.[1] Taxes on the deferred portion of the distribution will be "recaptured" when the units are sold rather than in the year in which the distribution is received up to the amount previously recognized as depletion. In addition to the recapture of distributions, unit holders will be subject to capital gains taxes when the units are sold at a gain for the portion above the initial cost.

For example, assume an individual buys an MLP unit for $20.00 which is yielding 10% and has a tax deferral of 80%. Each year, the unit holder receives a $2.00 distribution, of which $1.60 is deferred (80% x $2.00). The remaining $0.40 of the distribution is subject to ordinary income tax in the year received. At the end of year three, suppose the unit holder sells the unit for $23.00. The capital gain would be $3.00 ($23.00 minus $20.00), and the amount of recapture allocated to the unit holder's ordinary income would be $4.80 ($1.60 per year times three years). Please see the table below.

**Hypothetical Example of MLP Taxation**

| | Year 1 | Year 2 | Year 3 |
|---|---|---|---|
| Purchase Price | $20.00 | - | - |
| Sale Price | - | - | $23.00 |
| Capital Gain | - | - | $3.00 |
| | | | |
| Distribution per Unit | $2.00 | $2.00 | $2.00 |
| Distribution Subject to Tax (20%) | $0.40 | $0.40 | $0.40 |
| | | | |
| Deferred Distributions (cumulative) | $1.60 | $3.20 | $4.80 |
| | | | |
| Taxation: | | | |
| Current Year Distribution | $0.12 | $0.12 | $0.12 |
| Deferred Distributions (30% tax rate) | - | - | $1.44 |
| Capital Gains (15 % tax rate) | - | - | $0.45 |
| | | | |
| **Total Tax** | **$0.12** | **$0.12** | **$2.01** |
| **Total Holding Period Return, Net of Taxes (%)** | | | **33.80%** |

For illustrative purposes only. Salient Capital Advisors, LLC does not provide tax advice. Please contact your tax professional to determine how the information contained in this presentation may apply to your situation.
Source: Salient Capital Advisors, LLC.

[1] As pursuant to IRC §§ 751 and 1245.

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Like inherited stock, inherited MLP units receive a "step-up" in basis upon the death of the owner.[1] For estate tax purposes, the value of the unit is its fair market value, and that becomes the new basis for the heir going forward. Any capital gains or recapture of ordinary income is eliminated, which typically makes MLP units a viable option for estate tax management.

## Unrelated Business Taxable Income ("UBTI")

Many tax-exempt investors are apprehensive about investing in MLPs due to Unrelated Business Taxable Income[2], which is typically generated from any activity engaged in by a tax-exempt organization that is not related to the purpose of that organization.

In general, a business activity is an unrelated business (and generates unrelated business income subject to taxation) if it meets three requirements:[3]

1. It is a trade or business,
2. It is regularly carried on, and
3. It is not substantially related to furthering the exempt purpose of the organization.

Since MLPs are publicly-traded partnerships which pass income and cash flow through to unit holders, public unit holders are therefore considered to be "partners" in the business. Said another way, a unit holder in a natural gas pipeline MLP is considered to be in the natural gas pipeline business. For a tax-exempt institution, the natural gas pipeline business would likely violate all three of the requirements above and income generated by the partnership would therefore be subject to taxation.

MLP K-1s can often be complicated, and it is quite difficult to predict in advance whether or not UBTI will be generated. In order to avoid potential UBTI issues, some tax-exempt institutions invest in MLPs utilizing total return swaps. In a total return swap, an outside counterparty – typically an investment bank – utilizes its own balance sheet to purchase the MLP, and passes through (or swaps) the income and capital gains/losses to the investor in exchange for a pre-determined borrowing rate. Since the investment bank is viewed as the owner of the MLP portfolio, the UBTI risk to the tax-exempt institution is usually eliminated. In addition, Treasury Regulation 1.512(b)-1 specifically excludes income from notional principal contracts from UBTI.

Other structures also exist that help mitigate the UBTI issues, including open- and closed-end funds structured as C-Corporations, exchange traded notes and funds, and MLP i-shares (the "i" stands for "institutional"). Please see "Alternative Means of Investing in MLPs" below for further details.

[1] As pursuant to IRC §§ 754 and 1014.
[2] As defined by IRC § 512.
[3] As pursuant to IRC §513.

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## Alternative Means of Investing in MLPs

For many individual investors, the administrative burden of receiving a Schedule K-1 is reason enough not to invest in MLPs. Likewise, tax-exempt investors have sometimes avoided investing in MLPs due to potential UBTI issues. Since necessity is the mother of invention, several structures have been created that attempt to address the K-1 and UBTI concerns including closed-end funds, open-end funds, exchange traded funds, and exchange traded notes. However, each of these structures has potential drawbacks.

Closed-end funds ("CEFs") provide investors with a 1099 instead of a K-1, which eases the tax filing process for most investors. Further, CEFs do not generate UBTI, thus alleviating the concerns of tax-exempt investors and IRAs. Distributions received from CEFs typically are treated as some mix of return of capital, qualified dividends, and capital gains for income tax purposes. However, many CEFs are structured as C-Corporations since traditional Registered Investment Company (RIC) structures have limitations on owning MLPs. This can be a headwind to net asset value ("NAV") growth since the funds must accrue a tax liability at corporate tax rates. Further, since they trade like equity securities on an exchange, CEFs may trade at a discount or premium to the underlying NAV.

Open-end funds also provide a 1099 and avoid UBTI, and alleviate the premium/discount issues of CEFs since subscriptions and redemptions are done at NAV. However, many open-end funds currently on the market are also structured as C-Corporations and must accrue a tax liability, which serves to reduce NAV.

Exchange traded funds ("ETFs") are passive vehicles that are typically based on an MLP index, provide a 1099, avoid UBTI, and trade freely on a stock exchange. However, the current ETFs are structured as C-Corporations and have the same inherent tax liability impact on NAV as CEFs and open-end funds.

Like ETFs, exchange traded notes ("ETNs") are passive vehicles that are typically based on an MLP index, provide investors with a 1099, avoid UBTI, and trade freely on a stock exchange. However, strictly speaking, ETN investors are exposed to the full faith and credit of the institution that issues the note. In addition, since they are structured as notes, distributions from ETNs are considered interest income (not dividend income). Further, fees for some ETNs are similar to actively managed strategies.

The table below summarizes the alternative structures.

| | Open-End Funds | Closed-End Funds | ETNs | ETFs |
|---|---|---|---|---|
| **Active Management** | ✓ | ✓ | | |
| **Publicly-Traded** | ✓ | ✓ | ✓ | ✓ |
| **NAV Pricing** | ✓ | | | |
| **Use of Leverage** | | ✓ | Some | |
| **Counterparty Risk** | | | ✓ | |
| **Legal Structure** | Taxable C-Corp or RIC | Taxable C-Corp or RIC | Note | Taxable C-Corp or RIC |
| **Corporate Level Tax Drag*** | ✓ | ✓ | | ✓ |
| **Tax Form** | 1099 | 1099 | 1099 | 1099 |
| **Blocks UBTI** | ✓ | ✓ | ✓ | ✓ |
| **Dividend Treatment** | Mostly Return of Capital | Mostly Return of Capital | Ordinary Income | Mostly Return of Capital |

For illustrative purposes only. Salient Capital Advisors, LLC does not provide tax advice. Please contact your tax professional to determine how the information contained in this document may apply to your situation. *Applies to C-Corp Funds only.
Source: Salient Capital Advisors, LLC, March 2015.

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# 6. Risks

Each individual partnership has its own set of risks, which generally include (but are not limited to) commodity price movements, declines in throughput volumes, integration and execution risks associated with acquisitions, damages from natural disasters or terrorism, and interest rate risks. Some of the risks to the MLP space as a whole are discussed below.

**Economic Weakness.** While equity markets have performed relatively well following the 2008 financial crisis, the U.S. and global economies have not recovered as quickly as they have following previous recessions. Many economists expect the economy to continue to limp along at a 2-3% growth rate, but there are some that argue for higher growth and yet others that see a looming recession. If the economy experiences another round of weakness, MLP returns may be impacted.

**Treasury Rates.**[1] As of March 31, 2014, the yield on the 10-Year Treasury was 1.95% vs. the December 2014 close of 2.17%. On average, economists at the major investment banks expect the yield on the 10-Year Treasury to be 3.24% at the end of 2015. While MLPs have historically had a low correlation to Treasury rates, a rapid, dramatic move upward in Treasury yields may create some near-term pressure on MLPs.

**Credit Spreads.** MLPs have historically exhibited a relatively high correlation to major credit spread widening (and tightening) events. It has been relatively quiet recently, but if debt issues in either the U.S. or globally begin to escalate once again, both investment grade and high yield credit spreads could be negatively impacted. Such a situation would most likely negatively impact MLP valuations.

**Commodities.** Prices for both natural gas and NGLs have been weak for a while now (natural gas since 2009, NGLs since May 2012). Crude oil prices peaked in June 2014 and have declined dramatically since that time. Should oil prices stay “lower for longer”, it may lead to lower future production and thus fewer growth opportunities for MLPs which, in turn, may negatively impact valuations.

**Fund Flows.** Positive fund flows have been a major contributor to the performance of MLPs over the past few years. Investors remain concerned about the low rates on bonds and CDs not meeting their income needs, as well as the potential drop in bond prices if yields increase rapidly. MLPs have often been seen as an alternative to bonds due to higher yields and the ability to grow the distribution to offset any potential increase in interest rates. While we believe near term fund flows will continue to be strong, we could see investors ultimately return to traditional fixed income instruments if rates rise quickly.

**Tax Law Changes.** We believe this is unlikely in the absence of overall tax reform (see page 6 for reasoning), but any negative change in the tax code would likely have a detrimental impact on MLPs.

[1] Source: Bloomberg, Salient Capital Advisors, LLC. December 31, 2014.

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# 7. Glossary

1. **10-Year Treasury** is a debt obligation issued by the United States government that matures in 10 years. A 10-year Treasury note pays interest at a fixed rate once every six months and pays the face value to the holder at maturity. **RISKS:** Interest rate risk (as interest rates rise bond prices usually fall), and inflation risk exist.
2. **% Split** is the percentage split of the incremental cash flow between the limited partner and general partner.
3. **Alerian MLP Index (AMZ)** is a composite of the 50 most prominent energy MLPs that provides investors with a comprehensive benchmark for this emerging asset class. **RISKS:** Discussed throughout this material include tax related risks due to their partnership status, unlike the other asset classes discussed, as well as possible higher volatility than the majority of the other asset classes discussed.
4. **Alpha** is the excess return of the fund relative to the return of the benchmark index's return.
5. **Barclays Capital U.S. Aggregate Bond Index:** a composite comprised of the Barclays Capital U.S. Intermediate Government/Credit Index and the Barclay Capital Mortgage-Backed Securities Index. All issues in the index are rated investment grade or higher, have a least one year to maturity, and have an outstanding par value of at least $100 million. **RISKS:** Interest rate risk (as interest rates rise bond prices usually fall), the risk of issuer default, and inflation risk exist. As a lower-quality debt security, this involves greater risk of default or price changes and is more volatile than Bonds and T-Bills.
6. **Barclays U.S. High Yield Bond Index:** a U. S. Aggregate index that is comprised of fixed-rate, publicly issued, non-investment grade debt. **RISKS:** Interest rate risk (as interest rates rise bond prices usually fall), the risk of issuer default, and inflation risk exist. As a lower-quality debt security, this involves greater risk of default or price changes and is more volatile than Bonds and T-Bills.
7. **Beta** is a measure of the volatility, or systematic risk, of a security or a portfolio in comparison to the market as a whole. A beta of 1 indicates that the security's price will move with the market. A beta of less than 1 means that the security will be less volatile than the market. A beta of greater than 1 indicates that the security's price will be more volatile than the market.
8. **Brent Crude** is a major trading classification of light sweet crude oil that serves as a major benchmark price for purchases of oil worldwide.
9. **Compound Return** is the rate of return that represents the cumulative effect that a series of gains or losses has on an original amount of capital over a period of time.
10. **Consumer Price Index (CPI)** is the measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.
11. **Contango** is a situation where the futures price of a commodity is above the expected future spot price. Contango refers to a situation where the future spot price is below the current price, and people are willing to pay more for a commodity at some point in the future than the actual expected price of the commodity. This may be due to people's desire to pay a premium to have the commodity in the future rather than paying the costs of storage and carry costs of buying the commodity today.
12. **Cumulative Return** is the aggregate amount that an investment has gained or lost over time, independent of the period of time involved.
13. **Distribution Schedule** is the schedule of distributions at an annual rate.
14. **Dow Jones U.S. Utilities Index:** measures the performance of utility companies within the United States. **RISKS:** Non-diversified and therefore may be more volatile than the S&P 500 Index.
15. **Down-Market Capture Ratio** evaluates how well or poorly an investment manager performed relative to an index during periods when that index has dropped.
16. **Exploration & Production (E&P)** is a group of companies that explore for, and produce oil and gas.
17. **Gathering & Processing** involves moving natural gas from the wellhead to a natural gas processing plant, where NGLs and other impurities are removed from the natural gas stream.
18. **Growth** is the process of improving an enterprise's success, which can be achieved either by greater revenue or by increasing the bottom line or profitability of the operation by minimizing costs. In the context of the piece, growth refers to distribution growth.
19. **Incremental Distributions** is the limited partner's and general partner's share of the incremental increase in the distribution rate.
20. **Liquefied Natural Gas (LNG)** consists mostly of methane and is cooled to approximately -256 degrees Farenheit so that it can be transported from countries that have more natural gas than they need to countries that use more natural

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gas than they produce. In its liquefied state, natural gas takes up 1/600th of the space, making it much easier to ship and store when pipeline transport is not feasible. As world energy consumption increases, experts anticipate that the LNG trade will grow in importance.

21. **Max Drawdown** is the maximum peak-to-trough decline during a specific record period of an investment, fund or commodity.
22. **Moody's Baa** is an investment index comprised of medium grade, moderate risk bonds as rated by Moody's (an independent, unaffiliated research company that rates fixed income securities). **RISKS:** Interest rate risk (as interest rates rise bond prices usually fall), the risk of issuer default, and inflation risk exist.
23. **MSCI U.S. REIT Index:** a free float-adjusted market capitalization index consists of equity REITs that are included in the MSCI US Investable Market 2500 Index, except for specialty equity REITs that do not generate a majority of their revenue and income from real estate rental and leasing operations. **RISKS:** Real estate industry concentration risk (non-diversification), interest rate risk (as interest rates rise bond prices usually fall), the risk of issuer default, and inflation risk exist.
24. **Natural Gas Liquids (NGLs)** are hydrocarbons that are contained in natural gas and include ethane, propane, butane, isobutene, and natural gasoline.
25. **Russell 2000 Index:** an index measuring the performance of the 2,000 smallest companies in the Russell 3000 Index, which is made up of 3,000 of the biggest U.S. stocks.
26. **S&P 500 Total Return (TR) Index:** a stock market index based on the common stock prices of 500 top publicly traded American companies. **RISKS:** Can be affected by general market or economic conditions.
27. **S&P 500 Utilities Index:** an unmanaged index considered representative of the utilities market. **RISKS:** Can be affected by general market or economic conditions.
28. **Sharpe Ratio** measures the risk-adjusted performance of an investment.
29. **Sortino Ratio** differentiates between upward and downward volatility, allowing the calculation to provide a risk-adjusted measure of a security or fund's performance without penalizing it for upward price changes.
30. **Standard Deviation** is the annual rate of return of an investment to measure the investment's volatility.
31. **Total Quarterly Distribution** is the total quarterly distribution rate allocated between the limited partner and general partner, including the general partner's incentive distribution rights.
32. **Up-Capture Ratio** evaluates performance relative to an index during periods when the index has risen.
33. **Valuation** is the change in yield during the period ((Beginning yield - ending yield)/Beginning yield).
34. **West Texas Intermediate (WTI)** is also known as Texas light sweet, a grade of crude oil used as a benchmark in oil pricing.
35. **Yield** reflects the income return on an investment expressed as a ratio of income divided by current value of investment expressed as an annualized rate (annualized income/value of investment = yield).
36. **Yield Companies (Yield Cos)** are publicly traded companies that are formed to own operating assets that produce a predictable cash flow.

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