



Vinson&Elkins

OCTOBER 2015

ENERGY SERIES: AN INTRODUCTION TO MASTER LIMITED PARTNERSHIPS (MLPS)

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TODAY'S PANEL



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SAVE THE DATE



The graphic is a rectangular box with a blue and white wavy background. At the top right, the text "Vinson & Elkins" is written in a serif font. Below this, the title "V&E Energy Series" is prominently displayed in a large, white, serif font. Underneath the title, the text "Seminars and Continuing Legal Education Courses" is written in a smaller, white, sans-serif font. The main body of the graphic has a white background with blue text. It lists the topic "ENERGY FINANCE" and the specific seminar "Distressed Situations: Duties and Liability Management for Surviving a Downturn". The date "Wednesday, November 18, 2015" is listed, followed by the times "12:00 - 1:00 p.m. (CT); 1:00 - 2:00 p.m. (ET); 6:00 - 7:00 p.m. (BST)". A line of text states "Further information on this program will be posted soon." followed by a blue hyperlink "Read More & Register". Below this, the speakers are listed: "Speakers: Michael Saslaw, Bill Wallander, Erec Winandy". At the bottom left, it says "CLE pending".

Vinson & Elkins

V&E Energy Series

Seminars and Continuing Legal Education Courses

ENERGY FINANCE
Distressed Situations: Duties and Liability Management for Surviving a Downturn

Wednesday, November 18, 2015
12:00 - 1:00 p.m. (CT); 1:00 - 2:00 p.m. (ET); 6:00 - 7:00 p.m. (BST)
Further information on this program will be posted soon. [Read More & Register](#)

Speakers: [Michael Saslaw](#), [Bill Wallander](#), [Erec Winandy](#)

CLE pending

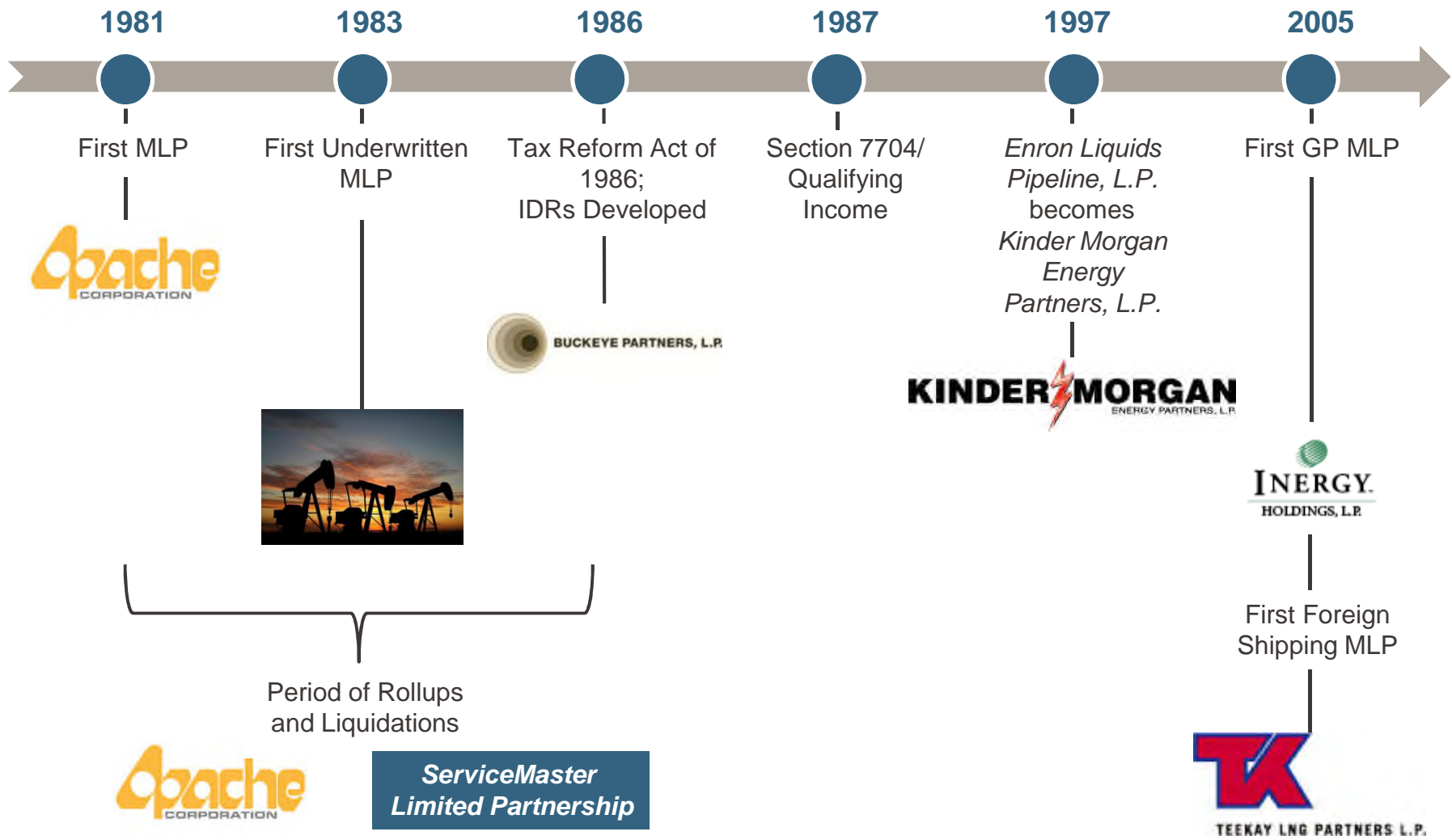
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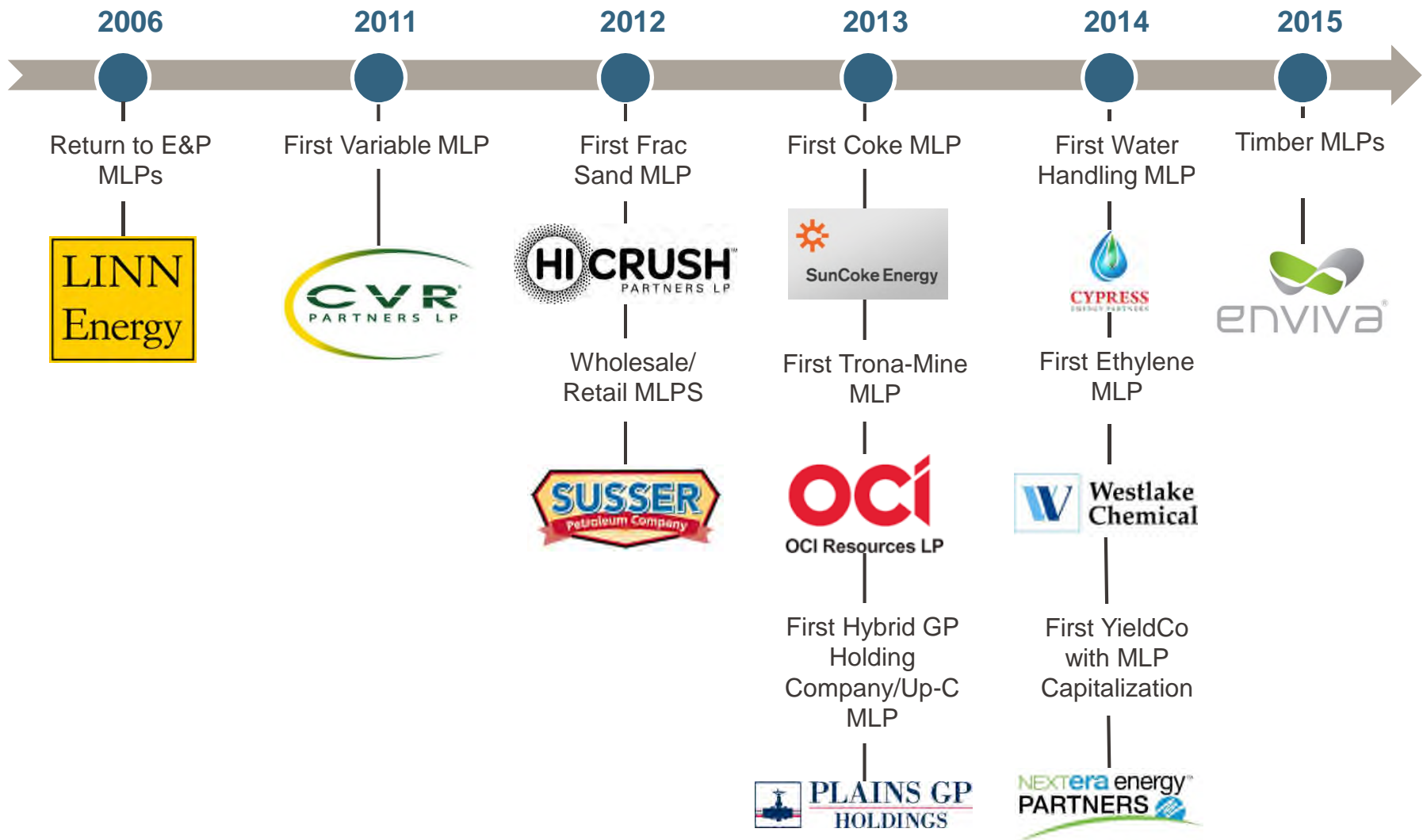
MLP HISTORY



HISTORY OF MLPS



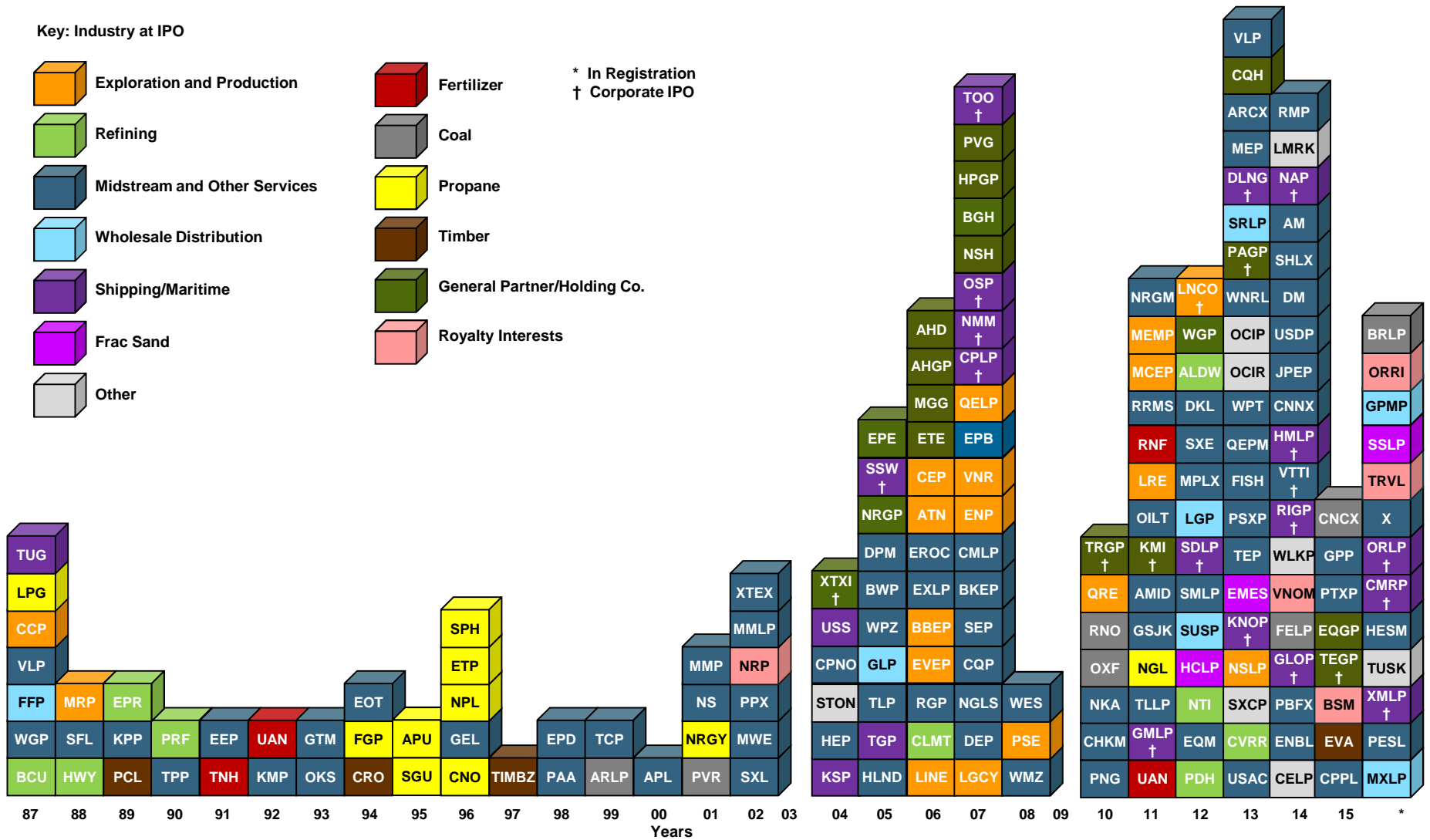
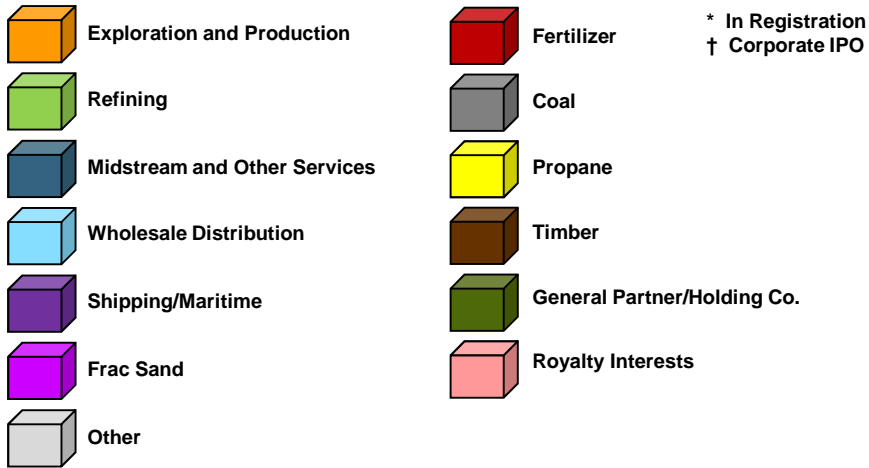
HISTORY OF MLPs



MLP INITIAL PUBLIC OFFERINGS

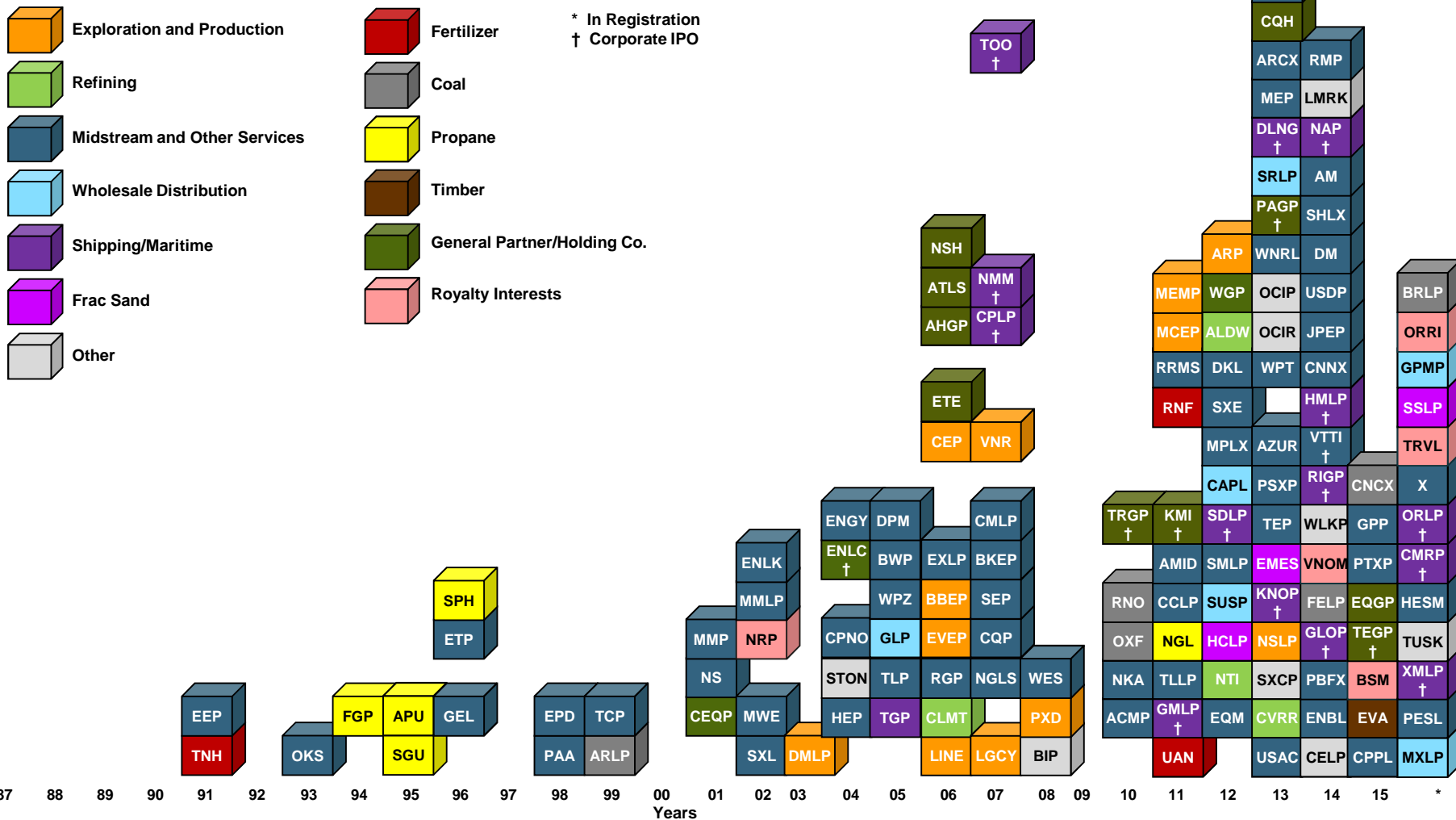
1987-2015

Key: Industry at IPO



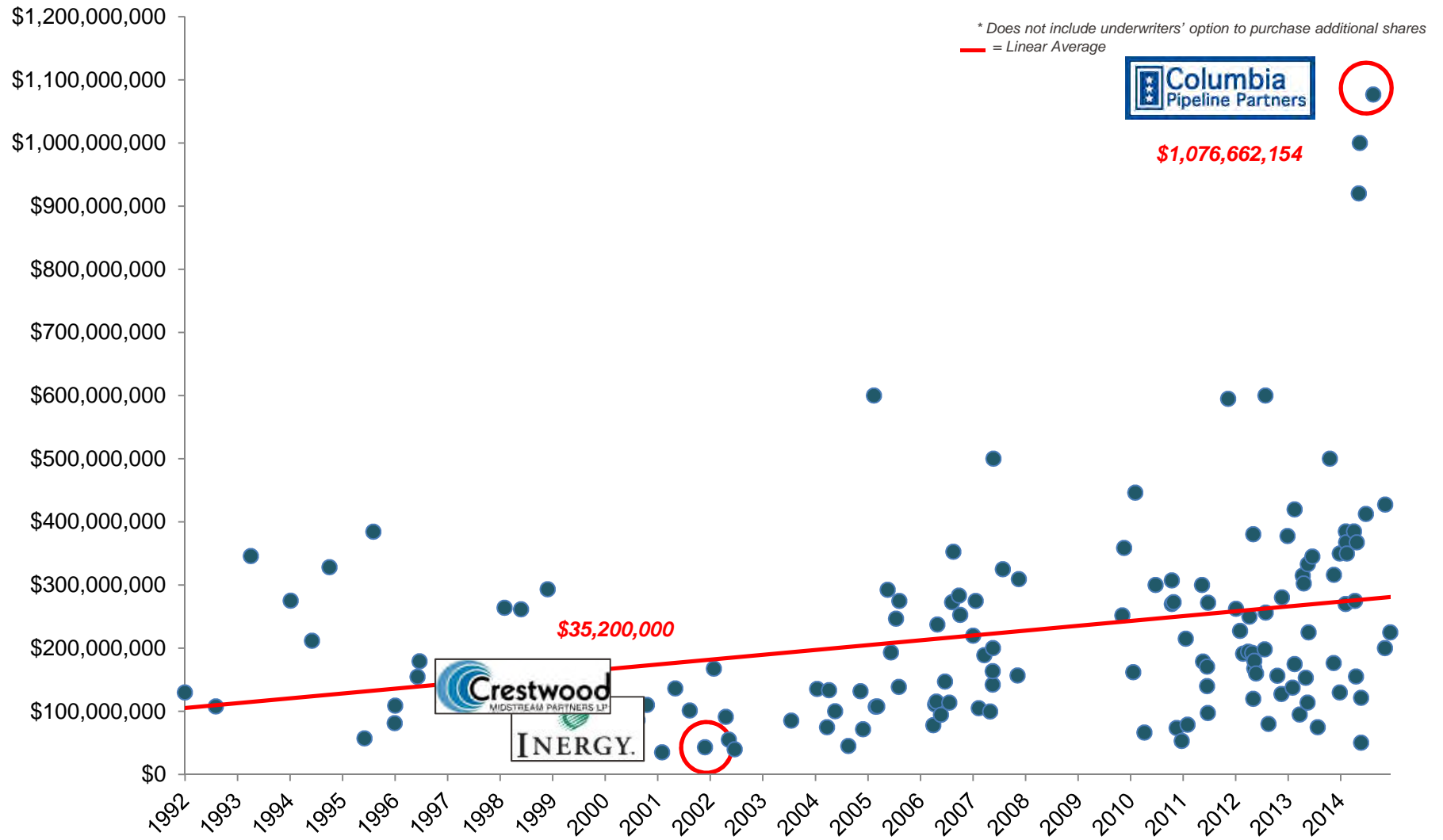
POST-ACT MLPS TRADED OR IN REGISTRATION

Key: Industry at IPO



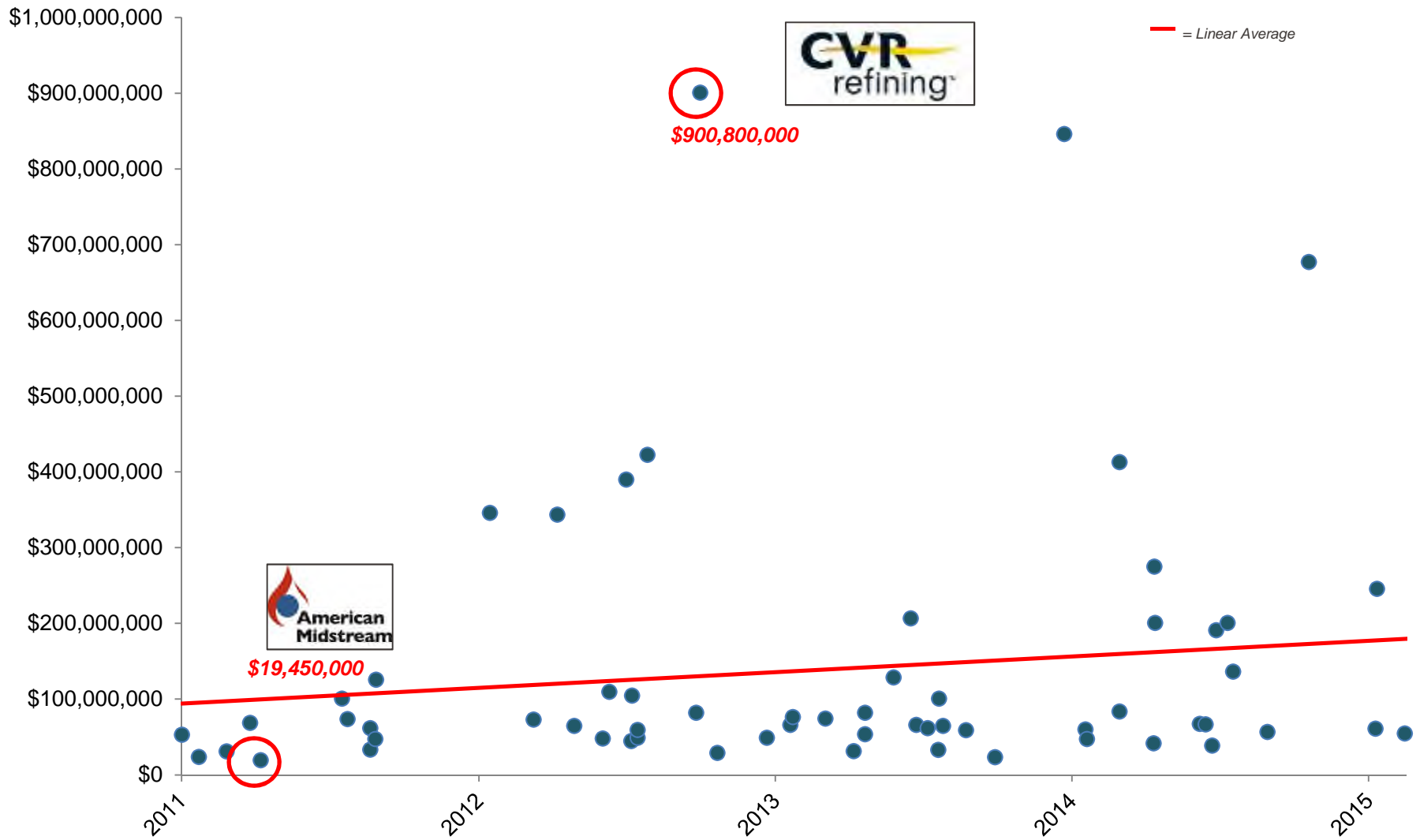
HISTORICAL INITIAL PUBLIC OFFERINGS

GROSS PROCEEDS AT IPO: 1982-2015*



HISTORICAL INITIAL PUBLIC OFFERINGS

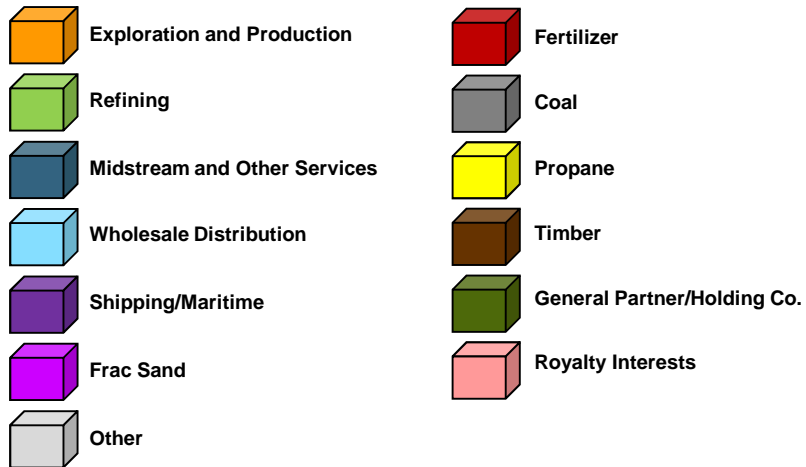
FORECASTED ADJUSTED EBITDA AT IPO: 2011-2015



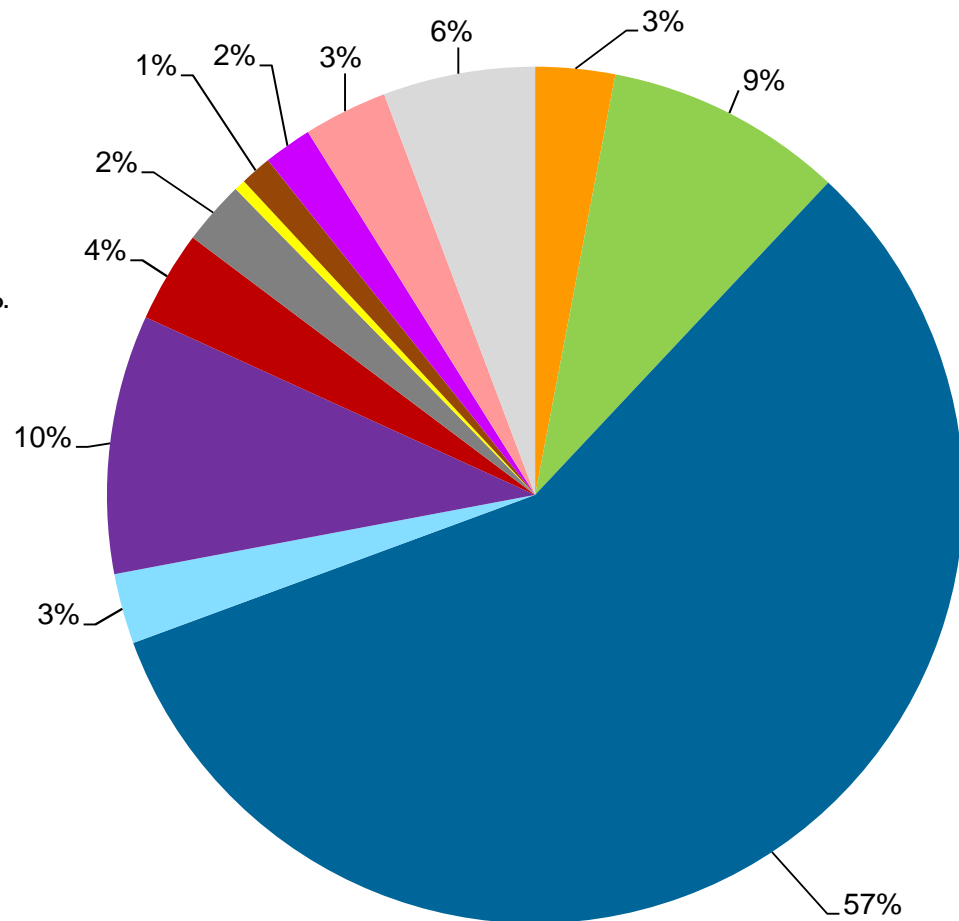
MLP INITIAL PUBLIC OFFERINGS

GROSS PROCEEDS AT IPO: 2011-2015*


Key: Industry at IPO



* Does not include underwriters' option to purchase additional shares

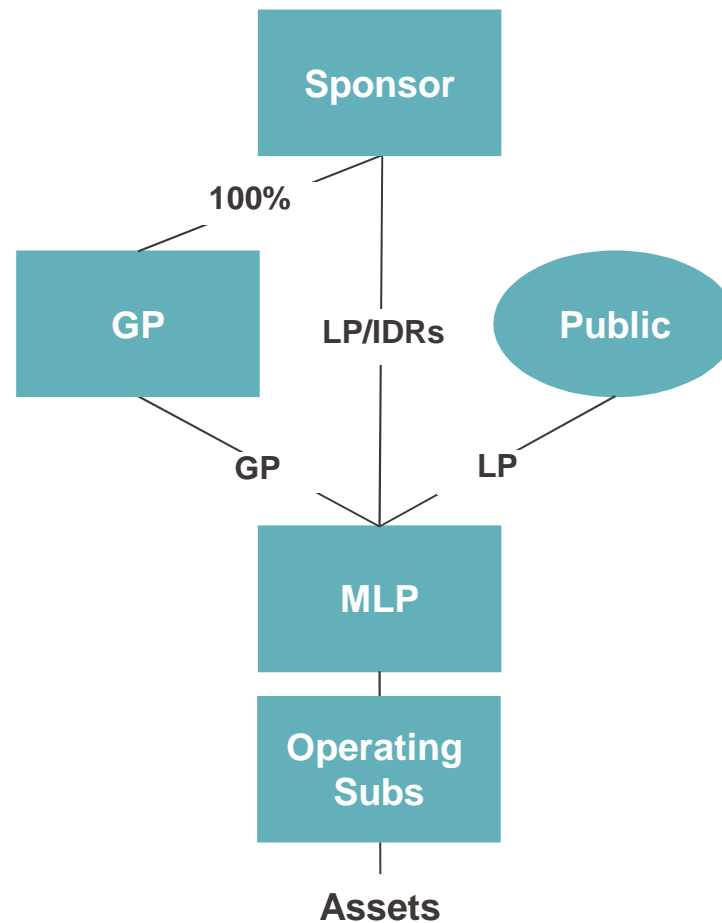


OVER \$17.5 BILLION IN GROSS
PROCEEDS SINCE JANUARY 2011



TRADITIONAL ORGANIZATIONAL STRUCTURE

TYPICAL ORGANIZATIONAL STRUCTURE



- = Ownership
- GP = General Partner
- LP = Limited Partner (units)
- IDR = Incentive Distribution Rights

ECONOMIC STRUCTURE



ECONOMIC STRUCTURE

KEY CONCEPTS

- Distribution Policy
- Common Units and Minimum Quarterly Distribution (“MQD”)
- Subordinated Units
- Incentive Distribution Rights (“IDRs”)
- 100 Unit Example
 - 50 common units
 - 50 subordinated units
 - \$0.25 per unit MQD

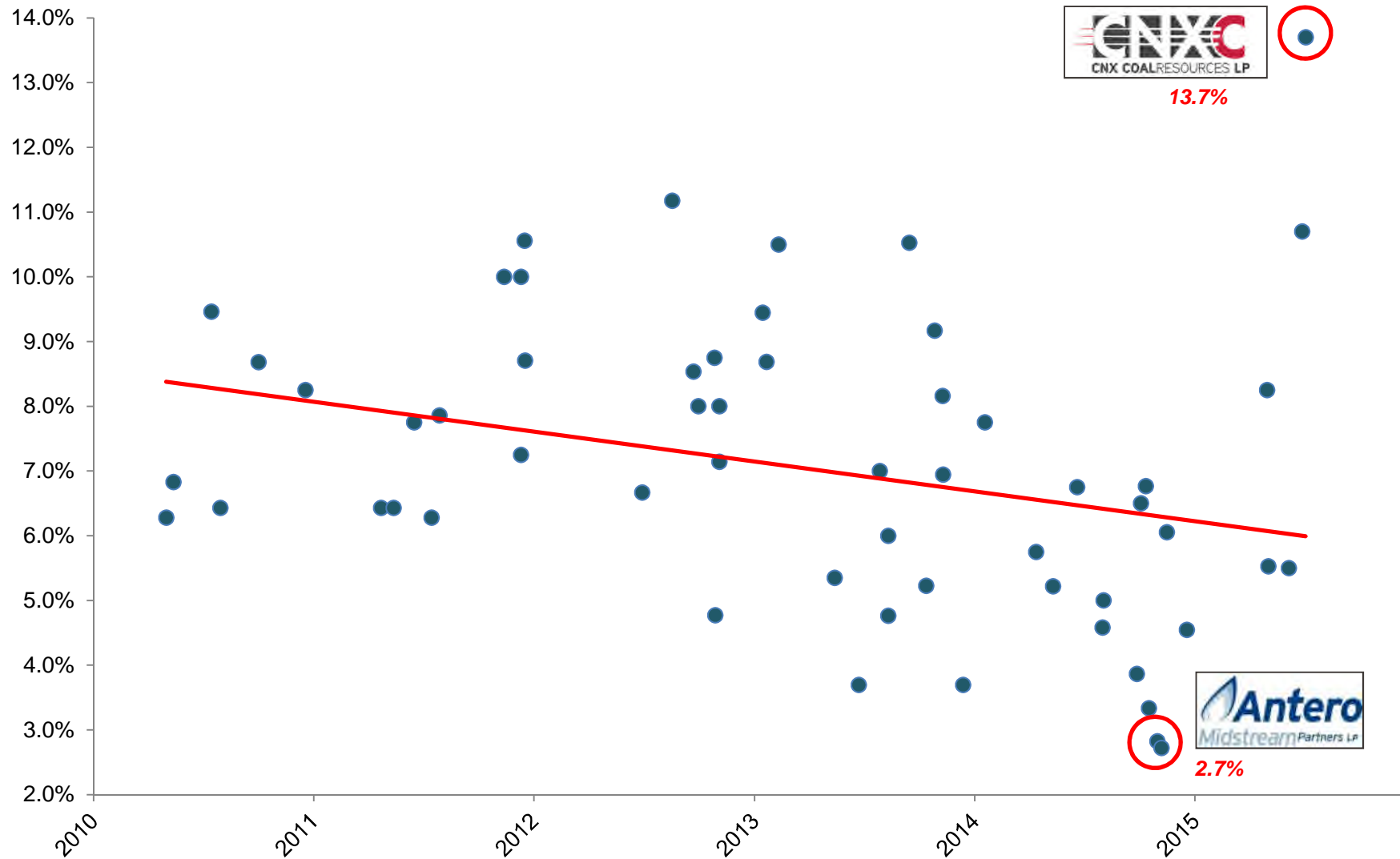
ECONOMIC STRUCTURE

DISTRIBUTION POLICY

- Generate stable (and increasing) cash distributions to unitholders
- Distributions are not a tax requirement, but the expectation of distributions (yield) is a marketing requirement
 - Since 2010, traditional MLPs have had yields at IPO ranging from 2.7% to 13.7% (average of 7.0%)
- In prospectus, the MLP makes a statement as to its intention to distribute a specified MQD per unit basis
 - Basis for yield at which the MLP is marketed
 - Sponsor subordinates a portion of its equity to payment of the MQD on the Common Units (class of equity sold to the public)
 - Sponsor receives IDRs, a special class of equity entitled to a disproportionate share of quarterly distributions in excess of targets above the MQD

HISTORICAL INITIAL PUBLIC OFFERINGS

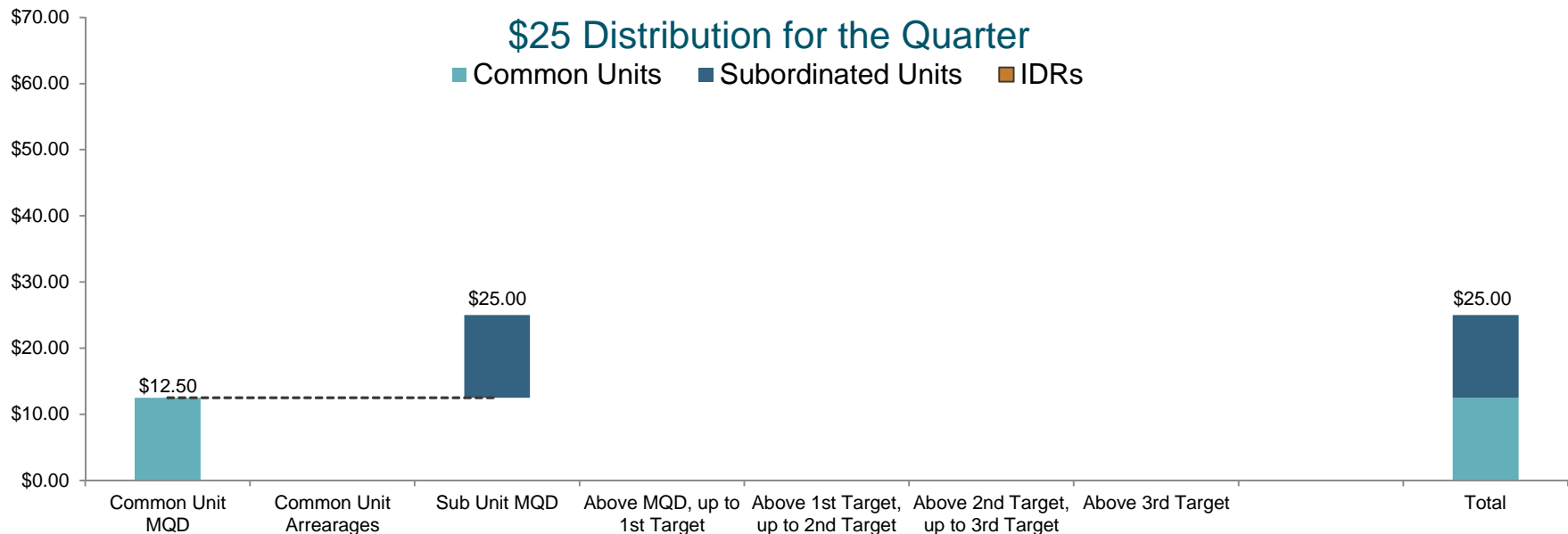
YIELD AT INITIAL PUBLIC OFFERING; TRADITIONAL MLPS



ECONOMIC STRUCTURE

SUBORDINATED UNITS: FORM OF CASH DISTRIBUTION SUPPORT

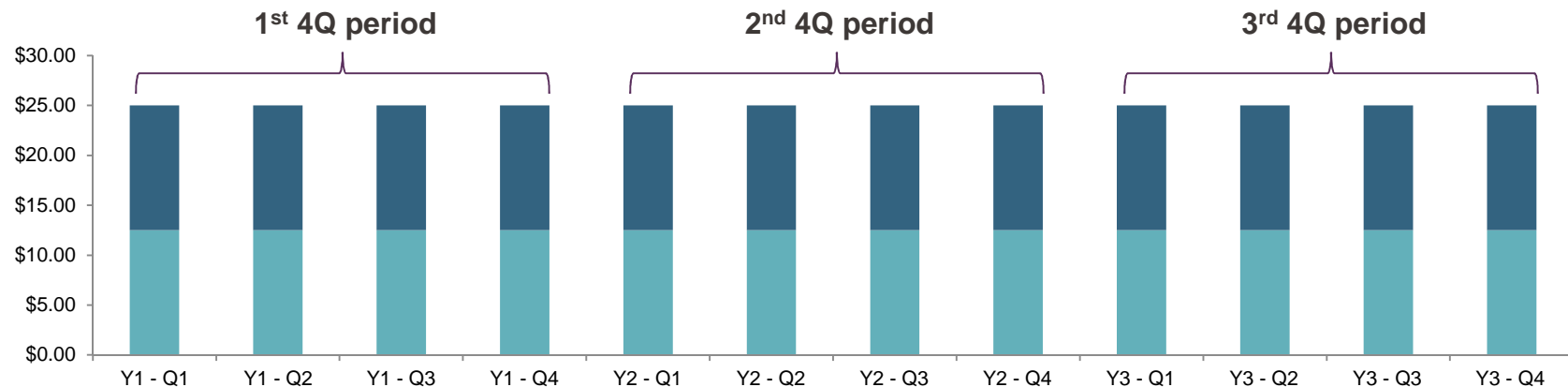
- Sponsor retains Subordinated Units
 - Often 50% of total units
 - Form of cash distribution support - subordinated to Common Units in payment of the MQD
 - Common Units entitled to arrearages in MQD if not paid
- 100 Unit Example



ECONOMIC STRUCTURE

SUBORDINATED UNITS: CONVERSION

- Subordinated Units convert to common at the end of Subordination Period
 - After three four-quarter periods of “earning” and “paying” the MQD on all outstanding units, and there being no existing arrearages on the Common Units
 - First tested approximately three years after IPO, rolls from quarter to quarter thereafter



- Early conversion (bullet test) of the Subordinated Units
 - After one four-quarter period where the MLP has “earned” and “paid” 150% of the MQD on all outstanding units and the corresponding payment on the IDRs

ECONOMIC STRUCTURE

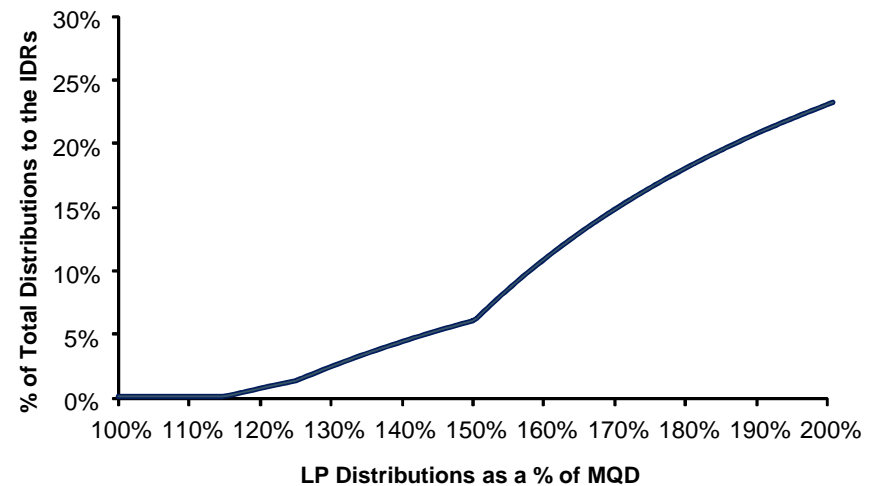
INCENTIVE DISTRIBUTION RIGHTS

- After 115% of the MQD is paid on the Common and Subordinated Units each quarter, the IDR holders have a right to an increasing share of marginal cash distributions as target cash distributions to unitholders are exceeded

Typical IDR Distribution Schedule

| Common Unit Distribution Range versus MQD | Cash Flow Distributions Within Range | |
|---|---|------|
| | LP | IDRs |
| 0.0% to 115.0% | 100% | 0% |
| 115.1% to 125.0% | 85% | 15% |
| 125.1% to 150.0% | 75% | 25% |
| 150.1% and above | 50% | 50% |

IDR Distributions



ECONOMIC STRUCTURE

DISTRIBUTION WATERFALL

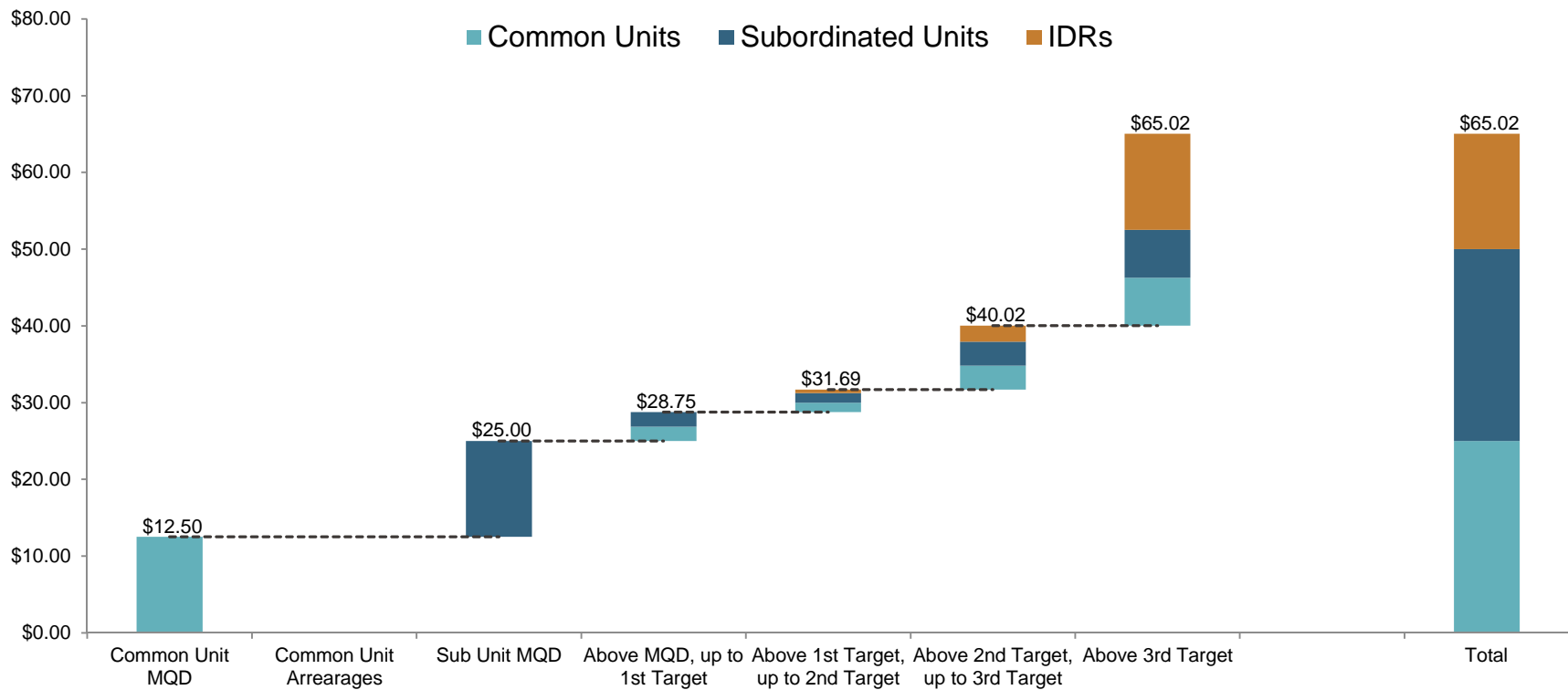
- 100 Unit Example

| Distribution Tier | Distribution Range (per unit) | % Common Units | % Subordinated Units | % IDRs |
|--|-------------------------------|----------------|----------------------|--------|
| Common Unit MQD | \$0.0 - \$0.2500 | 100.0% | -- | -- |
| Common Unit Arrearages | X | 100.0% | -- | -- |
| Sub Unit MQD | \$0.0 - \$0.2500 | -- | 100.0% | -- |
| Above MQD, up to 1st Target (1.15 X MQD) | \$0.2500 - \$0.2875 | 50.0% | 50.0% | -- |
| Above 1st Target, up to 2nd Target (1.25 X MQD) | \$0.2875 - \$0.3125 | 42.5% | 42.5% | 15.0% |
| Above 2nd Target, up to 3rd Target (1.5 X MQD) | \$0.3125 - \$0.3750 | 37.5% | 37.5% | 25.0% |
| Above 3rd Target | > \$0.3750 | 25.0% | 25.0% | 50.0% |

ECONOMIC STRUCTURE

DISTRIBUTION WATERFALL

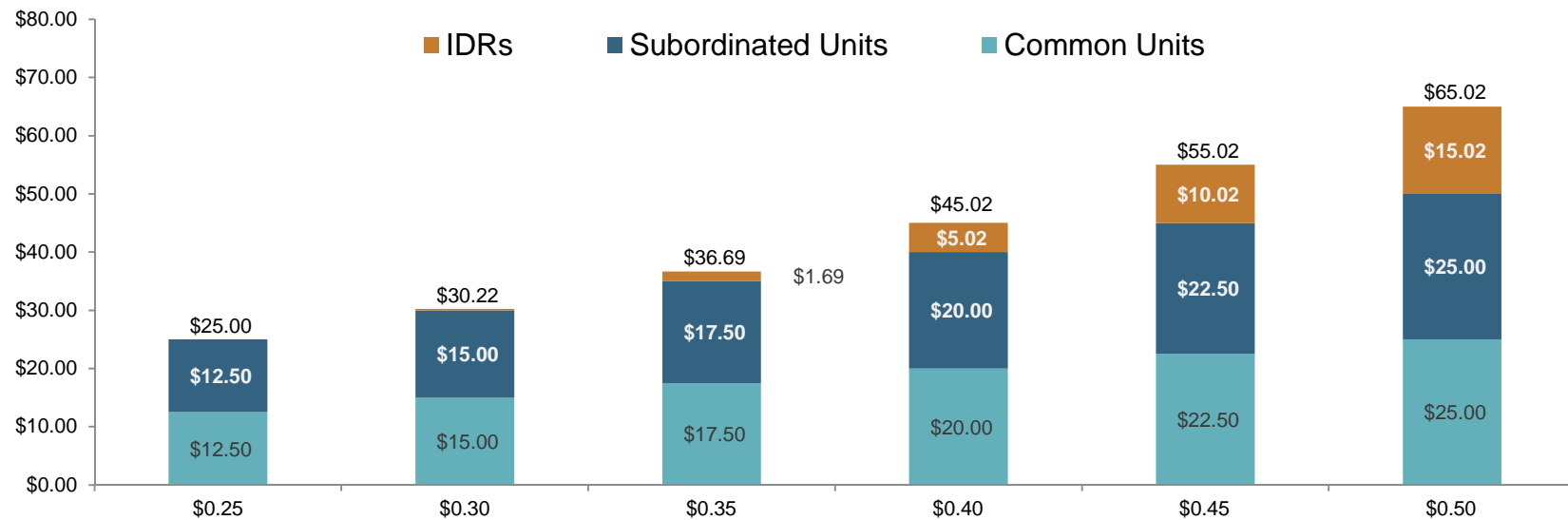
- 100 Unit Example
 - 1 quarter distribution
 - \$0.50 per unit



ECONOMIC STRUCTURE

IDR THEORY

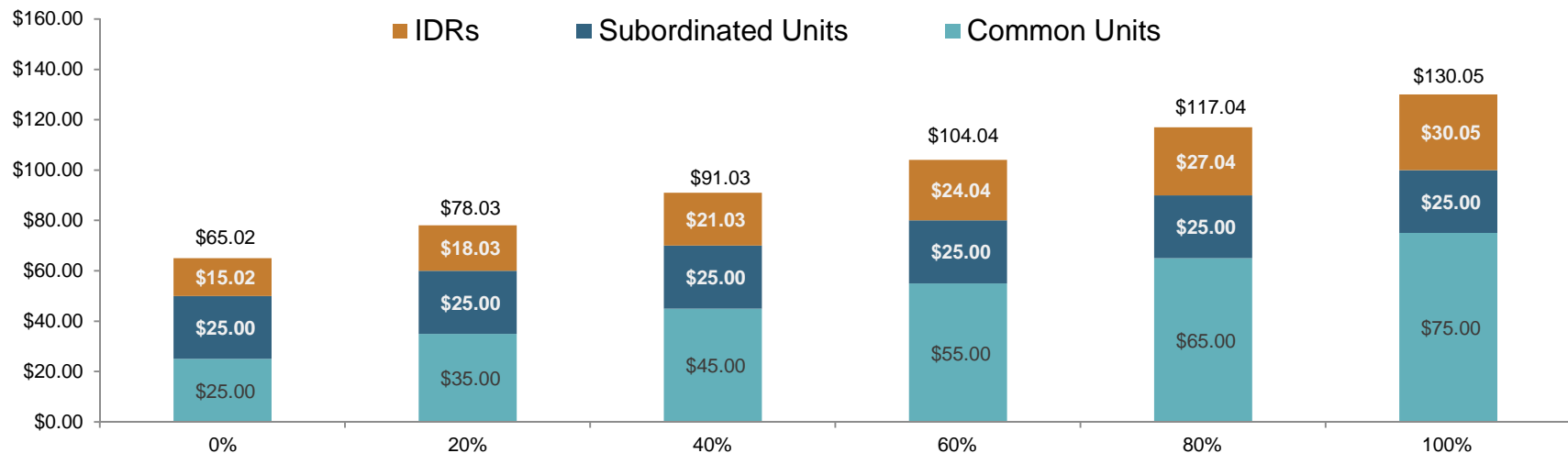
- Provides incentive for the Sponsor to grow distributions and compensation for subordination
- 100 Unit Example
 - \$0.05 per unit distribution increase



ECONOMIC STRUCTURE

IDR GROWTH THROUGH EQUITY ISSUANCES

- Once in the money, IDRs also benefit from increases in unit counts (assuming per unit distribution level is sustainable)
- IDRs are effectively a free carried interest as the MLP grows
- Absent modification, increases cost of MLP equity capital
- 100 Unit Example
 - 20% increases in unit count

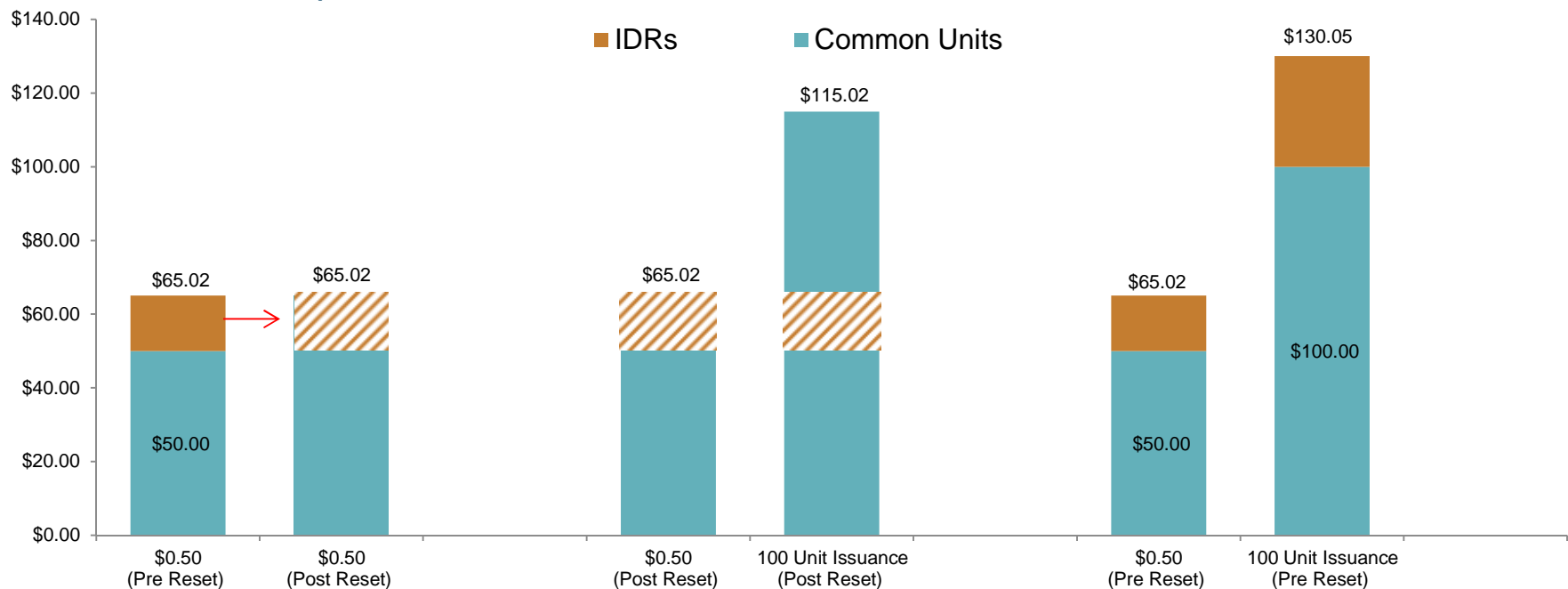


ECONOMIC STRUCTURE

IDR RESET

- IDR reset provision
 - IDR holders exchange old IDRs for new IDRs
 - MQD is reset to current distribution level, target distributions are set based on new MQD
 - IDR holders receive Common Units that will give them distributions roughly equivalent to the recent distributions on the old IDRs

- 100 Unit Example



ECONOMIC STRUCTURE

VARIABLE DISTRIBUTION MLPS

- Recently, businesses that do not have the cash flow to support an MQD have gone public as “Variable Distribution MLPs”
 - Publicly traded partnerships with policies of paying quarterly distributions of all reasonably distributable cash, without maintaining coverage or borrowing to smooth distributions
 - Focus is on optimizing business results and maximizing total distributions, not managing business with a focus on a minimum distribution or stability and growth in distributions
 - Without structural incentives (subordinated units or IDRs) to incent the GP to consistently maintain or increase distributions over time
- Variable MLP IPO yields (based on forecast cash distributions) have ranged from 4.2% to 32.5% (average of 15.4%)

QUALIFYING INCOME



QUALIFYING INCOME – REQUIREMENT

PARTNERSHIP TREATMENT

- Treatment as a partnership for U.S. federal income tax purposes is a fundamental aspect of PTP MLPs
- Required for distribution of pre-tax earnings
- PTP MLPs do not pay U.S. federal income tax
- Unitholders receive cash distributions and pay tax on their share of the MLP's taxable income
- Marketing efforts/underwriters require certainty – “will” level opinions
- Pre-1987 any business could qualify
- Post-1987 most publicly traded partnerships are treated as corporations

QUALIFYING INCOME – REQUIREMENT

STATUTORY REQUIREMENT FOR PARTNERSHIP TREATMENT

- Qualifying Income Test: 90% or More of Gross Income
 - Services (e.g., pipeline transportation): Gross revenue
 - No reduction for cost of services
 - Products (e.g., E&P): Gross margin
 - Gross revenue less costs of goods sold
- Measured each tax year
- Failure results in Corporate tax treatment for that tax year and all tax years going forward
- Mechanisms to handle Non-Qualifying Income
 - Keep below 5% of gross income
 - Put operations in a corporate subsidiary

QUALIFYING INCOME – TYPES

NATURAL RESOURCE QUALIFYING INCOME

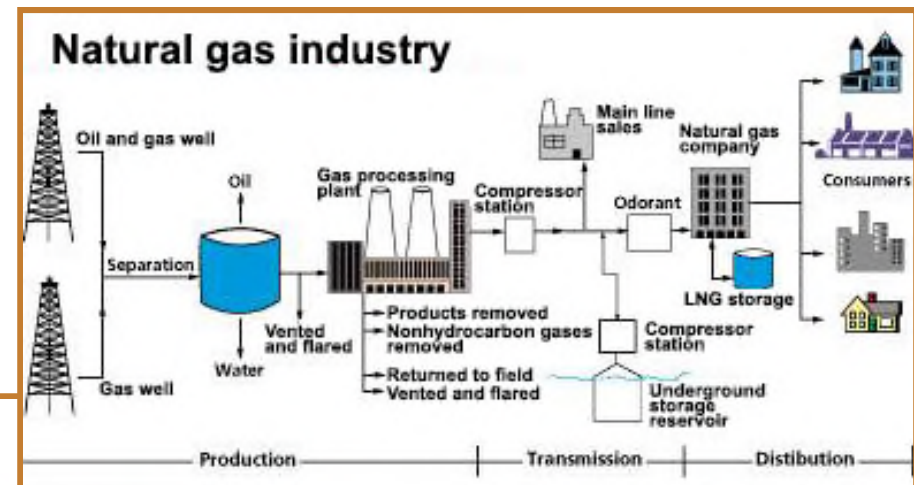
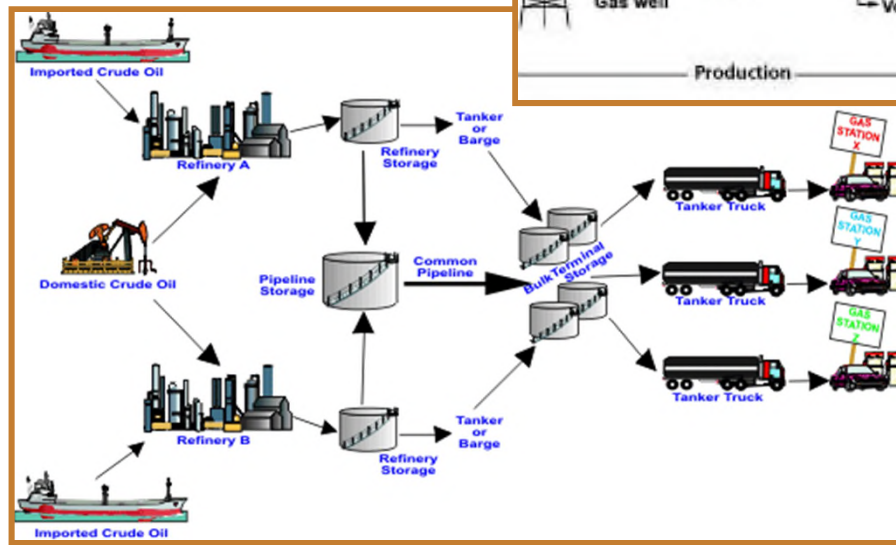
- Qualifying **Products**: Natural Resources and “Green” Fuels
 - Naturally occurring deposits (gas, oil, depletable minerals)
 - Oil and gas products (refinery tailgate or gas processing tailgate) – includes gasoline, kerosene, number 2 fuel oil, refined lubricating oils and diesel fuel
 - Fertilizer
 - Geothermal energy
 - Timber
 - Industrial source CO₂
 - Biodiesel/ethanol (transport and storage only)

QUALIFYING INCOME – TYPES

NATURAL RESOURCE QUALIFYING INCOME

- Qualifying **Activities**: Natural Resources

- Exploration
- Development
- Mining
- Production
- Processing
- Refining
- Transportation
- Storage
- Marketing



QUALIFYING INCOME – TYPES

NON-NATURAL RESOURCE QUALIFYING INCOME

- Real property income
 - Rents from real property (excluding (i) rents for personal property in excess of 15% associated real property and (ii) related party rents)
 - Income from sale of real property (including inventory)
- Gain from sale of assets generating qualifying income
- Interest (not from financial/insurance business)
- Dividends (from qualifying or non-qualifying activities)
- Gain from sale of stock
- Gain from commodities, futures, forwards and options with respect to commodities

QUALIFYING INCOME

LEASE VS. SERVICE ANALYSIS

- Service income from enumerated natural resource activities is qualifying income (even to related parties)
- Personal property rents and related party real property rents are not qualifying income
- The following factors support treating the MLP's income as service income:
 - MLP owns the relevant assets and land upon which the assets are located
 - MLP and its employees control the day-to-day operations and dictate the maintenance and improvement of the assets
 - The service recipient does not have any economic interest in the assets
 - There are no fixed price purchase rights, puts or calls
 - The term of the service contract is less than 60% of the life of the assets
 - The service provider retains the benefit of operating cost savings
 - The service provider bears the risk of loss with respect to the assets
 - The MLP bears risk of nonperformance under the contract
 - The assets are used to provide services to more than a single customer
 - Service revenue substantially exceeds the bare rental value of the assets

PLR PROCESS

- Administrative Process with IRS
 - PLRs are taxpayer-specific and granted at the discretion of the IRS
 - For novel issues, taxpayers often seek a pre-submission conference or call
- PLR Requests
 - 25 page written legal brief with summary of relevant facts, law and analysis
- Timing
 - Drafting typically takes several weeks
 - IRS Response
 - Historically 4-9 months
 - Notable exceptions (several in less than 1 month and one took 27 months)
 - Anticipate extended review while dealing with “pause” backlog and Proposed Regulations
- Costs
 - IRS user fee of \$28,300

QUALIFYING INCOME – IRS PLRS

91 PLRS SINCE 2007

| | | | | | | |
|------|---|---|--|---|--|---|
| 2008 | Power Generation Not Qualifying PLR 2008-21-021 | Oilfield Services – Fluid Handling (Frac) PLR 2008-27-014 | Oilfield Services – Drilling, Workover and Completion PLR 2008-27-022 | Interest Rate Hedging – Locks & Swaps PLR 2008-41-017 | Customer Reimbursements for Pipeline Construction PLR 2008-45-035 | Specialty Refining, Processing, Packaging & Marketing PLR 200848018 |
| 2009 | Licensing Seismic Data PLR 2009-09-006 | Interest Rate Hedging – Locks and Swaps PLR 2009-19-019 | Ethanol Blending at Terminals PLR 2009-21-010 | Production & Marketing of Modified Asphalt PLR 2009-27-002 | Marine Barge Time Charters PLR 2009-39-016 | Leasing Natural Gas LDC as REIT PLR 200937006 |
| 2010 | Leasing Asphalt Terminal PLR 2010-05-018 | Tugboat Marine Services for LNG Terminal PLR 2010-25-037 | Marine Barge Time Charters PLR 2010-27-003 | Oilfield and Mining Services – Fluid Handling (frac and acid) PLR 2010-43-024 | | |
| 2011 | Subpart F Income – Non-U.S. Marketing Subsidiary PLR 2011-13-018 | Sale of Stated Natural Resources PLR 2011-14-001 | Processing, Packaging and Marketing Refined Products PLR 2011-29-028 | Fees and Reimbursements For Managing Qualifying Activities PLR 2011-32-012 | Provision of Butane Blending Services & Automated Systems PLR 2011-32-020 | Oilfield Services – Frac Fluid Transport, Storage & Heating PLR 2011-37-005 |
| | Refinery Services PLR 2011-41-013 | | | | | |
| 2012 | Processing, Marketing and Distributing Stated Products PLR 2012-01-002 | Terminal Additization and Ethanol Blending PLR 2012-06-004 | Interest Rate Hedging – Locks and Forward Swaps PLR 2012-08-021 | Hydrogen Byproduct Sales PLR 2012-16-022 | Oilfield Services – Produced Water Services PLR 2012-22-029 | LNG Processing & Marketing PLR 2012-24-023 |
| | Oilfield and Mining Services – Extraction Logistics Supply PLR 2012-26-018 | Oilfield and Mining Services – Fuel Sales and Deliveries PLR 2012-27-001 | Oilfield Services – Waste & Environmental Services PLR 2012-27-002 | Terminal Additization PLR 2012-32-008 | Sale of EPA Credits for Blending Bio-Fuels PLR 2012-32-020 | Extracting and Marketing a Product to Industrial Users PLR 2012-33-009 |
| | Gas Gathering; Amine Plant; Management Fee NGL Facility PLR 2012-33-010 | Oilfield Services – Water Pipeline PLR 2012-34-005 | Conversion by Catalytic Cracking or Dehydrogenation PLR 2012-36-005 | NGL Processing and Olefin Marketing and Transportation PLR 2012-41-004 | Refined Products and Natural Gas Wholesale Distribution PLR 2012-50-014 | Leasing Offshore Production Platform PLR 2012-50-003 |
| 2013 | Refining, processing, blending & bulk end-user marketing PLR 2013-01-010 | Non-Agricultural Sales of Fertilizer Products & Byproducts PLR 2013-08-004 | Customer Reimbursements for Capital Expansions PLR 2013-14-029 | Operating a Natural Gas Compressor Fleet PLR 2013-13-014 | Processing Natural Gas into DME (Gas-to-Liquids) PLR 2013-14-038 | Fees and Reimbursements for Managing Transportation Assets PLR 2013-13-015 |
| | Updating PLR 2012-33-009 (Frac Sand PLR) PLR 2013-16-005 | Processing Natural Gas into LPG and Gasoline (Gas-to-Liquids) PLR 2013-15-015 | Interest Rate Hedging – Locks and Forward Swaps PLR 2013-15-008 | Hydraulic Fracturing Services PLR 2013-22-024 | Processing Natural Gas into LPG, Gas, Syn Gas & Methanol (gtl) PLR 2013-24-002 | Oilfield Fluids Handling and Sale of Recovered Products PLR 2013-30-024 |
| | Sale of Liquid Urea for Non-Agricultural Use PLR 2013-31-002 | Mining, Processing & Marketing of Sand and Ceramic Products PLR 2013-30-026 | Mining, Processing & Marketing Kaolin Ceramic Proppants PLR 2013-30-027 | Oilfield Fluids Handling and Hot Oil Services PLR 2013-30-023 | Pipeline Relocation, Interconnects and Condensate Sales PLR 2013-28-005 | Brine Disposal and Treatment PLR 2013-36-006 |
| | Oilfield Fluids Management and Technologies PLR 2013-36-016 | Oilfield Fluids Management and Disposal PLR 2013-38-035 | Refining, Processing, Storing and Handling NGLs PLR 2013-37-014 | Wholesale Distribution and Refined Product Sales PLR 2013-38-0001 | Processing a Natural Resource and sale of resulting products PLR 2013-40-011 | Oilfield Fluids Handling including recycling of flowback and skim oil PLR 2013-41-011 |
| | Processing Natural Gas into Methanol and Synthesis Gas (Gas-to-Liquids) PLR 2013-46-007 | Energy Logistics Support Services PLR 2013-47-015 | Oilfield Fluids Management, Storage and Maintenance Services PLR 2013-47-001 | Conversion of Butane into Butadiene PLR 2013-49-004 | Processing Iron Ore into Iron Pellets PLR 2013-51-009 | |

QUALIFYING INCOME – IRS PLRS

91 PLRS SINCE 2007

2014

Terminal Additization
and Blending Activities
PLR 2014-03-004

Grease Blending and
Wholesale Distribution of Grease
PLR 2014-03-008

Redacted Oilfield Services
with Customer Contracts
PLR 2014-05-011

Operating an Air Separation Unit
Within a Refinery
PLR 2014-08-008

Processing Feedstock into
Redacted Products
PLR 2014-08-025

Oilfield Fluids Handling and
Disposal Services
PLR 2014-10-017

Sale of EPA Credits (RINS) and
Fuel Delivery Services
PLR 2014-11-004

Redacted Oilfield Services
with Customer Contracts
PLR 2014-12-007

Energy Infrastructure Services and
Managing Coal JV
PLR 2014-18-021

Time Charters for Natural Resource
Product Tankers
PLR 2014-17-005

Supply and Transportation of
Frac Fluids
PLR 2014-16-003

Marketing and Transportation of
Frac Sand
PLR 2014-14-004

Supply and Transportation of
Frac Fluids
PLR 2014-14-002

Well-site Oilfield Services
and Supervision
PLR 2014-20-012

Processing Iron Ore into
Direct Reduced Iron
PLR 2014-48-019

Midstream Services
Including Rail
PLR 2014-51-002

2015

Interest Rate Hedging
PLR 2015-23-018

Water Delivery, Recycling and
Disposal
PLR 2015-37-014

Liquification of Natural Gas and
Regasification of LNG
2015-37-007

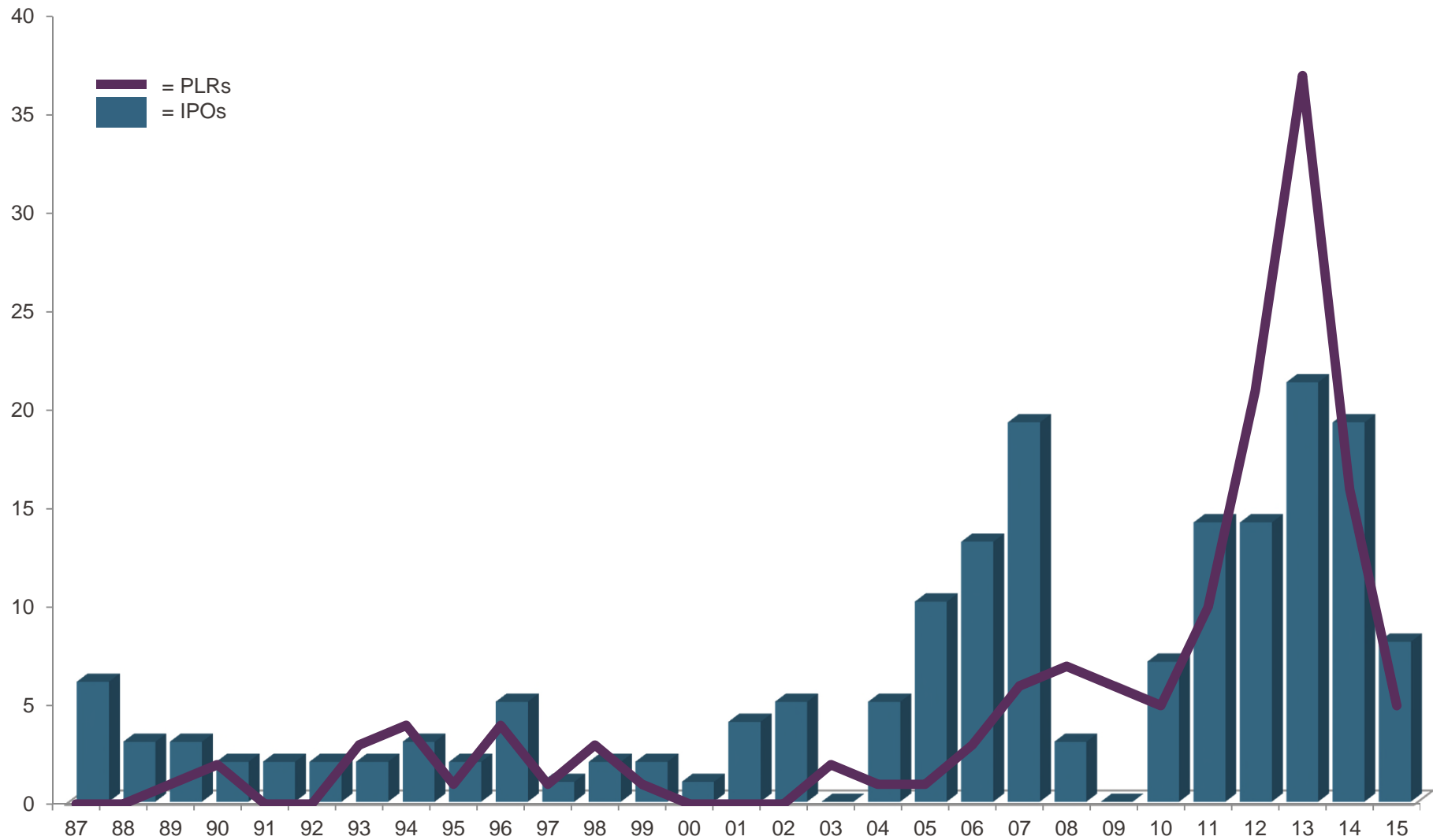
Transportation, Storage and
Marketing of Redacted Product
2015-38-012

Wholesale Fuel Distribution
2015-41-008

A list of, and links to, all qualifying income PLRs are available at www.velaw.com/MLPQualifyingIncome

MLP IPOS V. PLRS: 1987-2015

126 PLRS SINCE 1987





PROPOSED QUALIFYING INCOME REGULATIONS

IRS PAUSE TURNS INTO PROPOSED REGULATIONS

2014

February 15

February 28

March 28



Normal IRS interaction regarding potential Qualifying Income PLRs

IRS attorneys begin notifying taxpayers of a “pause” in considering qualifying income PLRs

Cliff Warren publicly acknowledges the “pause” and indicates that it applies to all qualifying income

2015

March 5

May 5

August 4

October 7

October 27



The Pause ends

IRS and Treasury release proposed regulations, requesting all comments thereto by August 4, 2015

All comments to proposed regulations due, with 131 comments submitted to the IRS

Outline of topics to be discussed at public hearing on final regulations due

Public hearing on final regulations to be held at IRS

All comments to the proposed regulations are available at www.velaw.com/MLPQualifyingIncome

PROPOSED REGULATIONS

AN “EXCLUSIVE LIST”

- Qualifying mineral and natural resource income “includes only [emphasis added] income and gains from qualifying activities with respect to minerals or natural resources.”
 - The preamble emphasizes that the list is intended to be exclusive
- The slides that follow discuss what constitutes “minerals and natural resources” and “qualifying activities”

PROPOSED REGULATIONS

EXCLUSIVE LIST: CONSEQUENCES

- Proposed regulations are an “exclusive list” of qualifying income
- At the margin, the proposed regulations create uncertainty around some traditional midstream and upstream activities
 - Royalties
 - Compression
 - Operation/management of qualifying businesses
 - Facility expansion and interconnect agreements
- Proposed regulations take an extraordinarily narrow position as to what “processing and refining” means
 - Excluding any processing and refining of NGLs beyond separation
 - Limiting the refining of crude oil
 - Severely limiting the processing and refining of timber
 - Severely limiting the processing of hard minerals
 - Ignoring/revoking prior PLRs

PROPOSED REGULATIONS

INTRINSIC ACTIVITIES

- Under the proposed regulations, qualifying income includes **INTRINSIC ACTIVITIES**. An activity is an intrinsic activity only if it:
 - is **specialized** to support a Section 7704(d)(1)(E) activity,
 - Requires that personnel have training unique to the mineral or natural resource industry that is of limited utility other than to perform or support such activity
 - For supply of an injectant to qualify the MLP must also collect and clean, recycle or otherwise dispose of the product (on a well-by-well basis)
 - is **essential** to the completion of the Section 7704(d)(1)(E) activity, and
 - Must be required to physically complete the qualifying activity (including in a cost-effective manner in order to make the activity economically viable) or comply with federal, state or local law regulating the Section 7704(d)(1)(E) activity
 - requires the provision of **significant services** to support the Section 7704(d)(1)(E) activity.
 - Onsite: the activity must be conducted on an ongoing or frequent basis
 - Offsite: in addition to ongoing and frequent, the service must only be offered to those engaged in qualifying activities

PROPOSED REGULATIONS

TRANSITION RULE

- The “Transition Period” ends on the last day of the MLP’s taxable year that includes the date that is ten years after the date that the regulations are published as final regulations
- A partnership may treat income from an activity as qualifying income during the Transition Period if
 - The partnership received a PLR from the IRS holding that the income from that activity is qualifying income;
 - Prior to May 6, 2015, the partnership was publicly traded, engaged in the activity, and treated the activity as giving rise to qualifying income under section 7704(d)(1)(E), and that income was qualifying income under the statute as reasonably interpreted prior to the issuance of the proposed regulations; or
 - The partnership is publicly traded and engages in the activity after May 6, 2015 but before the date the regulations are published as final, and the income from that activity is qualifying income under the proposed regulations

PROPOSED REGULATIONS

IN, OUT OR ON THE FENCE?



IN

- Transportation & storage of crude oil, natural gas, NGLs and fuels
- Field gas processing and NGL fractionation
- Wood pellets
- Affiliated-controlled water supply and disposal
- Saltwater disposal services
- Wholesale sales
- Gas-to-liquid fuels



OUT

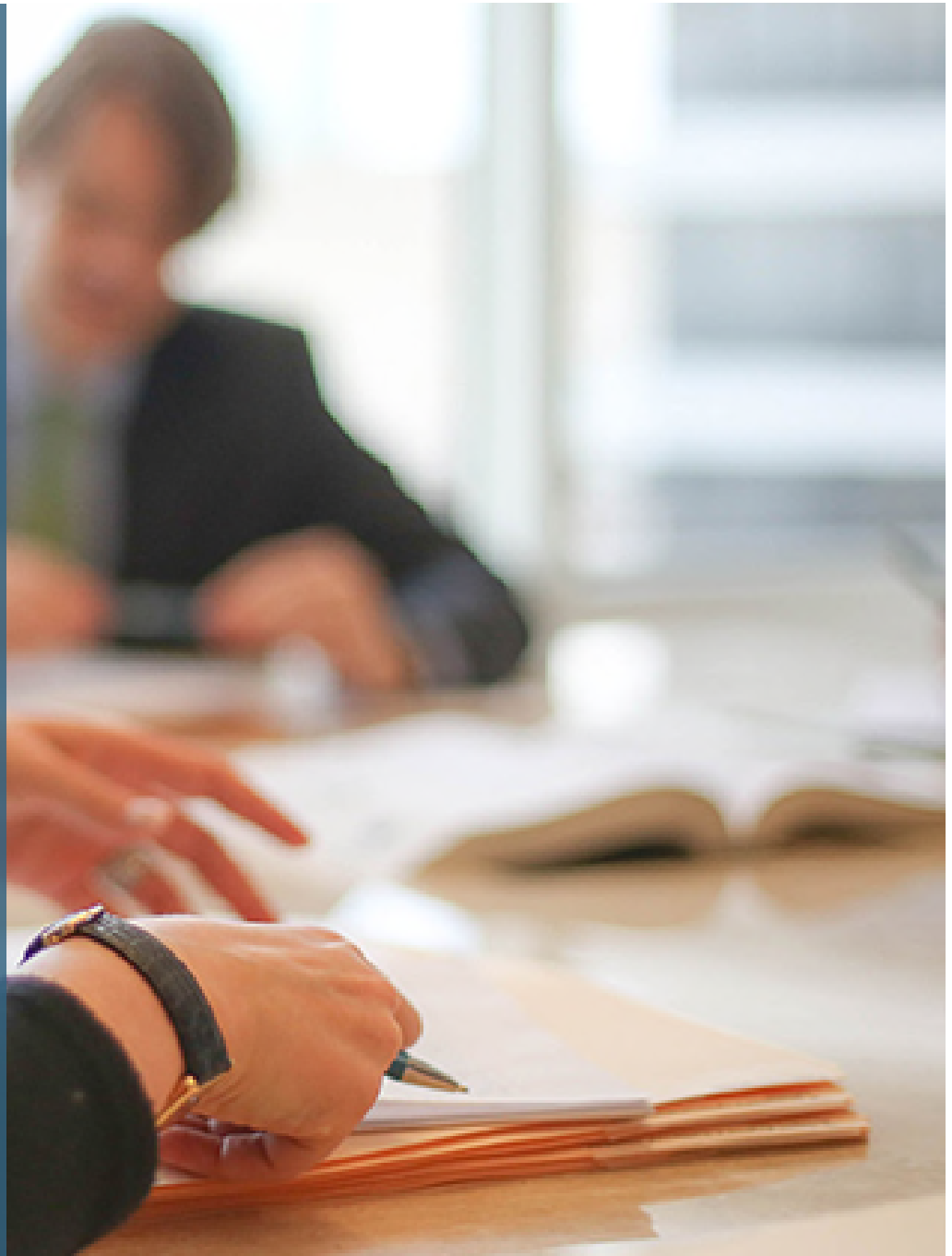
- NGL processing into olefins
- Non-refinery olefin transportation and storage
- Methanol production
- Pulp, paper and containerboard
- Gas-to-liquids (anything other than methane-to-liquid fuels)
- Non-affiliated water supply



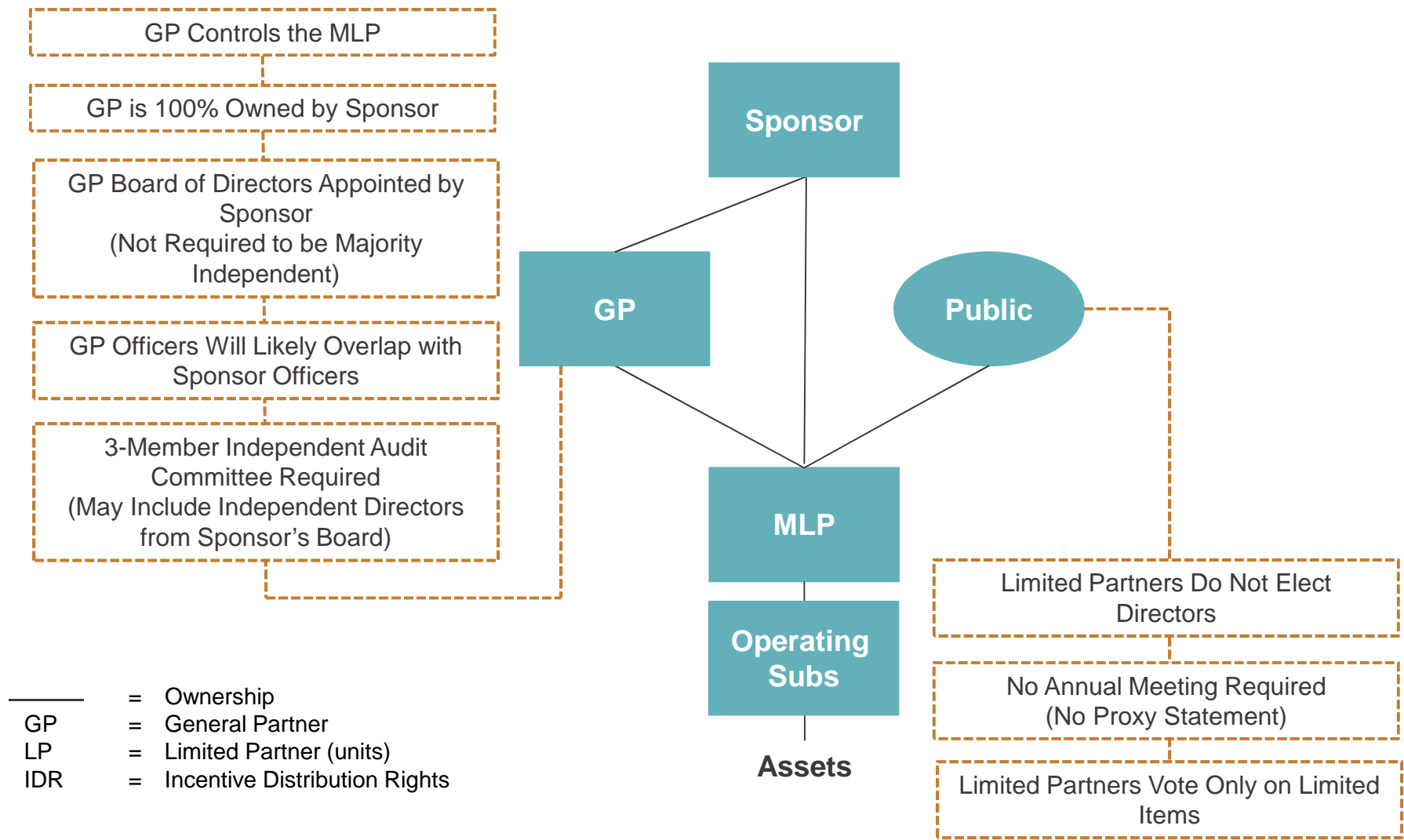
ON THE FENCE

- Hard mineral processing
- Royalty income
- Compression services
- Propane distribution
- CNG and LNG

MLP GOVERNANCE AND ACCOUNTING



SUMMARY OF GOVERNANCE STRUCTURE



GOVERNANCE

“FIDUCIARY-ISH” DUTIES

- Duty is set forth in the limited partnership agreement – a “good faith” standard.
 - When the GP is acting in its capacity as the GP of the MLP, it shall act in good faith and shall not be subject to any higher standard
 - Any action taken (or failure to act) by the GP will be deemed to have been taken in good faith unless the Board believed the action (or failure to act) was adverse to the interests of the MLP
 - Any action taken (or failure to act) by the GP in reliance upon the advice or opinion of a professional expert (lawyer, consultant, investment banker, etc.) is presumed to have been done in good faith and in accordance with such advice or opinion
- Case law states that it is “subjective”, but indicates that the process is the key.

GOVERNANCE

CONFLICTS OF INTEREST

- After the completion of the IPO, conflicts of interest will develop between the MLP and the Sponsor
 - Business opportunities, such as potential acquisitions, that either the MLP or the Sponsor could pursue individually, or when they decide to pursue them jointly
 - Direct dealings between the MLP and the Sponsor, such as in the case of the Sponsor desiring to sell additional assets to or buy assets from the MLP or the MLP and the Sponsor entering into a contractual arrangement
 - Allocations of general and administrative expenses to the MLP
 - Enforcement of indemnification or other agreements between the Sponsor and the MLP
 - The decision to borrow money or sell equity

GOVERNANCE

CONFLICTS RESOLUTION

- The partnership agreement will contain other conflict of interest resolution procedures, which typically provide that the General Partner will not be in breach of its fiduciary duty to the MLP or its unitholders if the resolution of the conflict is:
 - Approved by the Conflicts Committee of the GP (a committee comprised entirely of directors who are independent from the Sponsor); or
 - Approved by the vote of a majority of the outstanding common units, excluding any common units owned by the GP or any of its affiliates.

ACCOUNTING

FINANCIAL STATEMENT REQUIREMENTS

- The timing of an IPO is often driven by the timing of the auditor's annual and interim reviews of the company's financial statements and the staleness dates for the financial statements.
- Generally required for all IPOs:
 - Unaudited financial statements for any stub period
 - Three years of audited financial statements (two of audited balance sheets)
 - Two for Emerging Growth Companies (<\$1bln revenue)
 - Five years of selected financial data
 - Two for Emerging Growth Companies
- Special requirements for MLP IPOs:
 - Cash Distribution Forecast (ability to pay first year's MQD)
 - Cash Distribution Backcast (pro forma ability to have paid MQD during the most recent FY and LTM)
 - Shortfall requires disclosure, but is not a problem

ACCOUNTING ISSUES AND FINANCIAL STATEMENTS

GATING ISSUES TO BE ADDRESSED EARLY IN PROCESS

- Where MLP succeeds to some, but not all, of a Sponsor's business, carve-out financials may be appropriate.
 - Pre-clearance letter to SEC's Office of the Chief Accountant may be advisable.
 - SEC response typically takes 2-3 weeks.
- Two key additional financial statement requirements to monitor are requirements related to recent or probable acquisitions and requirements related to segment reporting.

FORMATION AND IPO CONSIDERATIONS



MLP SUITABILITY AND ADVISABILITY

- Are the assets suitable?
 - Assess the ability to generate qualifying income
 - Consider the near-term and long-term cash generation potential
 - EBITDA/DCF Requirements
 - Review the cash-flow profile and determine whether alternative mechanisms should be used
 - Long-term contracts
 - Hedging
 - High DCF-to-MQD coverage ratio
 - Preferred equity interest
- Assuming the assets are sustainable, is an MLP IPO advisable?
 - Cost and difficulty of conveying the selected assets
 - Existing debt structure limitations
 - Tax consequences



CIRCULAR 230 NOTICE

This presentation was not written or intended to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter addressed herein.

THANK YOU

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