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ARTICLE

The Master Limited Liability Partnerships Parity Act: Friend or Foe?

SONIA J. TOSON*

In April of 2013, Democratic Senator Chris Coons of Delaware introduced legislation that seeks to level the playing field between renewable and non-renewable energy companies. Titled the "Master Limited Partnerships Parity Act" (MLPPA), the legislation would amend the federal tax code to allow renewable energy companies to form master limited partnerships and thereby gain valuable financing and tax advantages. This legislation would clear the way for the formation of master limited partnerships investing in renewable energy, which would have significant impact on clean energy production in the United States. This article discusses the Master Limited Partnerships Parity Act and explores the advantages and disadvantages of master limited partnerships as a business organization for renewable energy companies and ultimately argues for the passing of this valuable legislation.

The article is divided into six sections. Part I defines master limited partnerships and examines their corporate structure and how they operate as compared to other types of business organizations. Part II delineates the history and evolution of master limited partnerships over the last thirty years. Part III describes the Master Limited Partnerships Parity Act, including its history, purpose and aims. Part IV then details the

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arguments in support of the Master Limited Partnerships Parity Act, while Part V gives the arguments in opposition to the Act. The article then concludes in Part VI with the author's recommendations and conclusions that the Master Limited Partnerships Parity Act is a step in the right direction for the development of the clean energy sector and environmental protection in the United States.

I. WHAT IS AN MLP?

Master Limited Partnerships (MLPs) are by definition limited partnerships that are publicly traded[1] on a national securities exchange.[2] Ownership interests in MLPs are referred to as "common units" and are similar in nature to common stock in a corporation.[3] MLPs are afforded flow-through taxation while still offering limited liability to unit-holders, which makes them an attractive business structure for investors. According to Senator Coons, a Democrat from Delaware, who proposed initial legislation expanding access to MLPs, "MLPs combine the flexibility of a corporation with the tax benefits of a partnership, creatively stimulating private investment in energy projects."[4] MLPs, however, are statutorily restricted to investments in depletable energy sources such as oil, natural gas, coal extraction, and pipeline projects.[5]

1. A publicly traded company is defined by the Securities and Exchange Commission as "a company that has a class of securities that is registered with the Commission because those securities are widely held or traded on a national securities exchange." *Going Private*, U.S. SEC. & EXCH. COMM'N, http://www.sec.gov/answers/gopriv.htm (last visited Oct. 10, 2014).

2. MLPs are a type of "publicly traded partnership." While most MLPs are limited partnerships, they may also be limited liability companies (LLCs) that are publicly traded. Both types of entities function the same way in terms of limited liability and pass-through taxation. *See MLP Basics for Investors*, NAT'L ASS'N OF PUBLICLY TRADED P'SHIPS, http://www.naptp.org/PTP101/BasicFacts.html (last visited Oct. 10, 2014).

3. John Goodgame, *New Developments in Master Limited Partnership Governance*, 68 BUS. LAW. 81, 82 (2012).

4. U.S. SENATOR CHRIS COONS, MASTER LIMITED PARTNERSHIPS PARITY ACT (2013), *available at* http://coons.senate.gov/download/mlp-white-paper/; *see also* Master Limited Partnerships Parity Act, H.R. 1696, 113th Cong. (2013).

5. I.R.C. § 7704(d)(1)(E) (2012).

Section 7704 of the Internal Revenue Code (IRC) specifically states that a publicly traded partnership is any partnership whose ownership interests are traded on an *established securities market*[6] or are readily tradable on a *secondary or equivalent market*.[7] Section 7704 also mandates that all publicly traded

6. 26 C.F.R. § 1.7704–1(b) (2014). An established securities market is defined is:

> (1) A national securities exchange registered under section 6 of the Securities Exchange Act of 1934 (15 U.S.C. 78f);
>
> (2) A national securities exchange exempt from registration under section 6 of the Securities Exchange Act of 1934 (15 U.S.C. 78f) because of the limited volume of transactions;
>
> (3) A foreign securities exchange that, under the law of the jurisdiction where it is organized, satisfies regulatory requirements that are analogous to the regulatory requirements under the Securities Exchange Act of 1934 described in paragraph (b)(1) or (2) of this section (such as the London International Financial Futures Exchange; the Marche a Terme International de France; the International Stock Exchange of the United Kingdom and the Republic of Ireland, Limited; the Frankfurt Stock Exchange; and the Tokyo Stock Exchange);
>
> (4) A regional or local exchange; and
>
> (5) An interdealer quotation system that regularly disseminates firm buy or sell quotations by identified brokers or dealers by electronic means or otherwise.

Id. § 1.7704–1(b)(1)-(5). For more information on interdealer quotation systems referenced in subsection (5), see *Over-the-Counter Market*, SEC, http://www.sec.gov/divisions/marketreg/mrotc.shtml (last updated May 9, 2013).

7. Secondary or equivalent market, as referenced in the abovementioned definition of publicly traded partnership, is defined in the following manner:

> Interests in a partnership that are not traded on an established securities market… are readily tradable on a secondary market or the substantial equivalent thereof if, taking into account all of the facts and circumstances, the partners are readily able to buy, sell, or exchange their partnership interests in a manner that is comparable, economically, to trading on an established securities market.
>
> …[i]nterests in a partnership are readily tradable on a secondary market or the substantial equivalent thereof if—
>
> > (i) Interests in the partnership are regularly quoted by any person, such as a broker or dealer, making a market in the interests;
> >
> > (ii) Any person regularly makes available to the public (including customers or subscribers) bid or offer quotes with respect to interests in the partnership and stands ready to effect buy or sell transactions at the quoted prices for itself or on behalf of others;

partnerships must generate at least 90% of their income from *qualified sources*.[8] Section 613 of the IRC further specifies that that the source of qualifying income must be *depletable* resources.[9] Qualifying natural resource activities include exploration, development and production, mining, gathering and processing, refining, compression, transportation, storage, marketing and distribution, and propane sales.[10]

As publicly-traded partnerships, MLPs are subject to these qualifying income rules. Here lies the problem: investments in renewable energy sources, such as solar, wind, hydroelectric and geothermal are specifically excluded from this definition and are therefore prevented from organizing as master limited partnerships and acquiring the benefits that accompany this corporate structure.

A. Current MLPs

As of June 2014, there were 117 registered MLPs.[11] Of those, forty-four percent are in the pipeline industry, thirteen percent are exploration production companies, nine percent are designated as "other," five percent are storage companies, five percent are coal companies, five percent are shipping companies, four percent are propane companies, four percent are refining companies, three percent are oil and gas shipping services, three percent are fertilizer companies, three percent are compression

> (iii) The holder of an interest in the partnership has a readily available, regular, and ongoing opportunity to sell or exchange the interest through a public means of obtaining or providing information of offers to buy, sell, or exchange interests in the partnership; or
>
> (iv) Prospective buyers and sellers otherwise have the opportunity to buy, sell, or exchange interests in the partnership in a time frame and with the regularity and continuity that is comparable to that described in the other provisions of this paragraph (c)(2).

26 C.F.R. § 1.7704–1(c)(2) (2014).

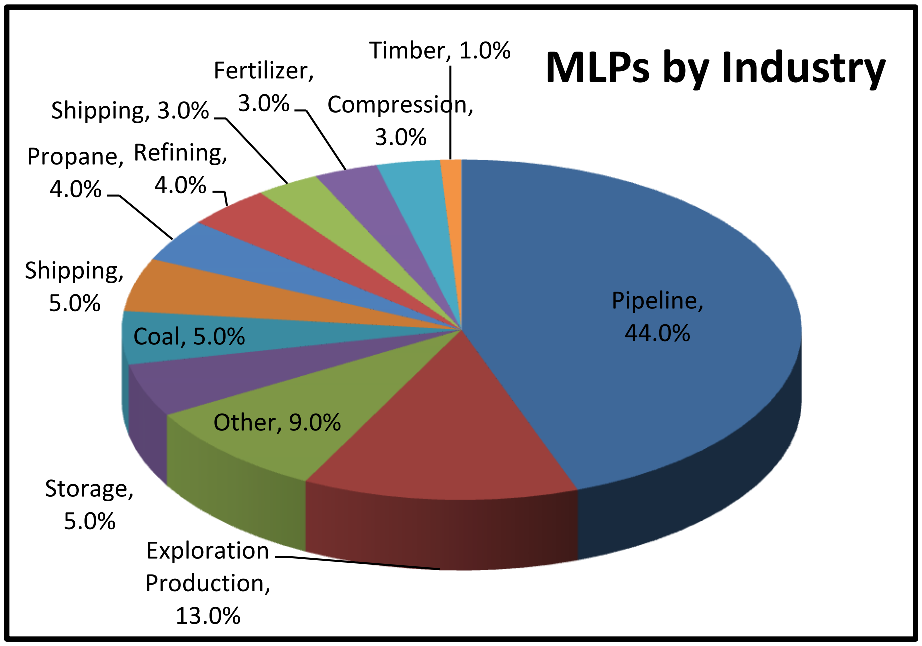
8. I.R.C. § 7704(c), (d).

9. I.R.C. § 613.

10. With the exception of propane, retail sales are not included.

11. *Master Limited Partnerships List*, LATHAM & WATKINS, LLP, http://www.lw.com/MLP-Portal/MLPList (last visited Sept. 18, 2014).

companies, and one percent are timber companies.[12] The figure below depicts the proportion of MLPs within each industry:[13]



B. MLPs Compared with Other Types of Entities

MLPs share some characteristics with other types of business entities, but it is the combination of high-yield distributions and significant tax advantages that set it apart from other business organizations.

Note the comparison between MLPS and other corporate structures below:[14]

12. Latham & Watkins, LLP. *Id.*

13. Chart adapted from data compiled by Latham & Watkins, LLP. *Id.*

14. *See* AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, COMPARISON OF BUSINESS ENTITIES (2009), *available at* http://www.aicpa.org/interestareas/tax/resources/taxpracticeimprovement/2009taxpracticeguidesandchecklists/downloadabledocuments/03_09_comp_of_bus_ent_092009.pdf; *Chart of Entity Comparison*, HENNINGER ACCOUNTING SERVICES, P.C., http://www.henningercpa.com/site/images/PDF/Forms/natpchartentitycomparison.pdf (last visited Oct. 10, 2014); Stephen Maresca et. al., MORGAN STANLEY, MIDSTREAM ENERGY MLPS PRIMER

Feature	General Partnership	Limited Liability Company	Master Limited Partnership	C-Corp.	S-Corp.
Owner Liability	Unlimited	Limited to capital investment	Limited to capital investment	Limited to capital investment	Limited to capital investment
Taxation	Pass-through	Pass -through	Pass - through	Double Taxation	Pass - through
Duration	Cessation of business; ceasing to operate as a partnership; sale or exchange of 50% or more of the profits and capital within a 12-month period; may terminate with death of partner if agreement specifies	Per Articles of Organization or state requirements	Ongoing	Ongoing	Ongoing
Publicly-traded	No	No	Yes	Yes	No
Ability to raise capital	Partner contributions	Member contributions, possibly sale of membership interests subject to operating agreement	MLP units sold on public exchange to raise capital	Shares of stock sold on public exchange to raise capital	Shares of stock sold to raise capital

3.0 1, 3 (2013), *available at* http://www.morganstanleyfa.com/public/projectfiles/4735a09e-c35d-4545-a059-8873c8d057f0.pdf.

In terms of organization, MLPs are structured like any other limited partnership. The composition consists of a general partner responsible for the day-to-day management of the company and several limited partners who are strictly investors.[15] The general partner may be a sponsor company (often a corporation, but sometimes a limited liability company) or a group of individuals who oversee the company's operation on a daily basis.[16] The sponsor company owns whatever shares were not sold publicly plus a two percent general partnership interest and is typically a larger, publicly traded corporation.[17]

The investors consist of unitholders who have purchased units via the stock exchange for the sole purpose of receiving a return on their investment. The primary role of the investors is to infuse capital into the partnership and, as such, the investors are not involved in the routine management and operation of the company.[18] While the general partner has a two percent ownership interest in the company, the investors, or limited partners, typically have a ninety-eight percent ownership interest.[19]

As discussed previously, MLPs are publicly-traded on a national stock exchange, and, thus, units of the MLP are purchased in an initial public offering and then traded and sold much like corporate stock.[20] Most MLPs are traded on the New York Stock Exchange, with a small number being traded on the NASDAQ.[21]

15. Donna D. Adler, *Master Limited Partnerships*, 40 U. FLA. L. REV. 755, 756–57 (1988); Conrad S. Cotello & Chris J. Muscarella, *Matching Organizational Structure with Firm Attributes: A Study of Master Limited Partnerships*, 1 EUR. FIN. REV. 169, 170 (1997).

16. Adler, *supra* note 15, at 756–57.

17. John Goodgame, *Master Limited Partnership Governance*, 60 BUS. LAW. 471, 474 (2005).

18. *Id.*

19. Philip H. Peacock, *Recent Developments in Texas and the United States Energy Law*, 4 TEX. J. OIL GAS & ENERGY L. 363, 440 (2009); Goodgame, *supra* note 17, at 473.

20. *Master Limited Partnerships – 101*, LATHAM & WATKINS, LLP, http://www.lw.com/MLP-Portal/101 (last visited Oct. 10, 2014).

21. *Id.*

There are three significant features that make MLPs attractive to investors from a cash distribution perspective. The first is the requirement commonly found in most MLP partnership agreements that the partnership distribute all "available cash" to its partners.[22] In analyzing several MLP partnership agreements, "available cash" is consistently defined as "all net cash generated by the MLP in the previous quarter less any reserves that the general partner determines to be necessary or appropriate in its reasonable discretion."[23] Although the amount of reserves necessary or appropriate is somewhat subjective, this requirement typically results in the distribution of a "significant portion of the cash generated by the MLP's business operations."[24] These distributions typically substantially exceed the amounts of their dividend counterparts in the corporate setting, making MLPs an attractive option for investors.[25]

Within this distribution structure is an additional "hidden" advantage. While "distributions" may seem like just another name for what corporations call dividends, there is actually a notable difference between the two. While corporate cash dividends are subject to taxation (which is the undesired second level of double taxation), MLP cash distributions are generally not taxed, which is a significant perk for investors.[26]

A second feature that makes MLPs a desired structure for investors is the subordination of the general partner/sponsor company's units. This feature is the successor of the "subordination period" common in early MLPs, prevalent in the 1980s.[27] Historically, MLPs had a subordination period

22. Goodgame, *supra* note 17, at 475.

23. *Id.*

24. *Id.*

25. *Id.* at 475 (citing Conrad S. Costello & Chris J. Muscarella, *Matching Organizational Structure with Firm Attributes: A Study of Master Limited Partnerships*, 1 EUR. FIN. REV. 169, 188 (1997)).

26. *Id.* at 472.

27. TIM FENN, LATHAM & WATKINS, LLP, MASTER LIMITED PARTNERSHIPS (MLPS): A GENERAL PRIMER 1, 6 (2014), *available at* https://www.lw.com/admin/Upload/Documents/MLP/Resources/Latham-Master-Limited-Partnership-Primer-2014.pdf.

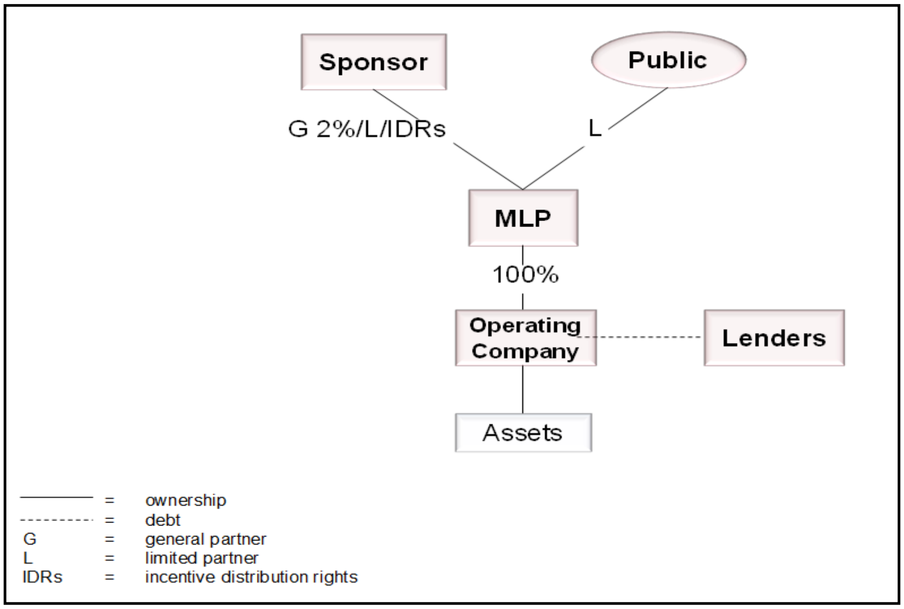
immediately following their initial public offering, in which the general partner/sponsor's interests were subordinate to the limited partners' interests. This preference structure was designed to ensure minimum distribution levels to investors.[28]

Current MLPs still retain vestiges of this feature, in that limited partners by common units in the MLP, while the general partner/sponsor retains subordinated units. Common units are similar to preferred stock in corporations, and subordinated units are comparable to common stock. This means that limited partners are entitled to receive a minimum distribution each quarter, *before* the general partner/sponsor is allowed to receive any distribution of cash.[29] These Minimum Quarterly Distributions are an attractive bonus for MLP investors.

The third attractive feature of MLPs from an investment standpoint, are incentive distribution rights. In addition to receiving distributions resulting from their two percent ownership interest, general partners typically also receive incentive distribution rights (IDRs), which allow the general partner to receive an increasing percentage of quarterly distributions once target distribution levels are met.[30] Incentive distribution rights are designed to incentivize the general partner to rapidly grow the distributions to limited partners. In addition to receiving distributions for any common units owned in the partnership, general partners also receive increasing incentive distributions that grow as the amount of the quarterly distribution grows. Thus, the general partner's distributions can grow from two percent to fifty percent. The quarterly distributions of limited partners are decreased by the amount of the general partners' IDRs.[31]

The following graphic illustrates the basic structure of a typical MLP:[32]

28. Goodgame, *supra* note 17, at 476.
29. *Id.*
30. J.T. Carpenter, *Master Limited Partnerships Shed a Tier*, 53 S. TEX. L. REV. 381, 386 (2011).
31. FENN, *supra* note 27, at 4.
32. *Id.* at 3.



In addition to the cash-distribution benefits, MLPs also attract investors for the tax and capital accumulation benefits. First, MLPs can take advantage of pass-through taxation and are not subject to double taxation.[33] Cash is taxed only once when distributed to unitholders, which effectively lowers the cost of capital and leaves more cash that can be distributed to the general partner and investors.[34] The lower cost of capital provides MLPs with advantages in building and acquiring assets. Next, cash distributions are largely tax-deferrable. Unlike their corporate counterparts, dividends, cash distributions are not taxed when they are received. MLP cash distributions create a reduction in the investment's cost basis, which means they are a tax liability that is deferred until the asset is sold. Since the structure of MLPs produces such significant cash distributions, much of the investor's tax liability is deferred. In addition, since MLPs are publicly traded, they have the ability to raise capital from a broader range of investors.[35] Public investors that would

33. Coons, *supra* note 4.
34. *Id.*
35. *Id.*

typically be limited to investing in corporations exclusively, now have the option of investing in MLPs and trading their units on a national security exchange.

Finally, MLPs can own rate-regulated assets and still give investors an attractive rate of return.[36] Even though assets are heavily regulated by the Federal Energy Regulatory Commission, the aforementioned features (i.e. minimum quarterly distributions, subordination of general partner/sponsor units, and pass-through taxation) combine to ensure that the limited partner still receives the desired rate of return.[37]

It is due to these vast benefits that MLPs have been a preferred business structure for oil and gas companies for many years.

II. THE HISTORY OF MLPS

Traditional limited partnerships have a long tradition in the United States and globally.[38] However, limited partnerships have limitations. Most relevant, they do not lend themselves to growing investment or the frequent changing of partnerships because most states require a certificate of partnership on file that lists each partner.[39] Each time the partnership takes on new investors, the certificate of partnership must be updated with the State.[40] Master limited partnerships were contemplated as a solution to this problem of inflexibility.[41] Under the new structure, a "master" limited partnership can be formed, which only requires the "master" partner to be listed in the certificate of partnership and further allows investors to buy and sell interests in the business without the need to update the certificate of partnership.[42]

36. *Id.*
37. *Id.*
38. Adler, *supra* note 15, at 756.
39. Marvin F. Milich, *Master Limited Partnerships*, 20 REAL EST. L.J. 54, 56 (1991).
40. Gordon B. Shneider, *A Historical View of Limited Partnership Roll-Ups: Causes, Abuses, and Protective Strategies*, 72 DENV. U. L. REV. 403, 406 (1995).
41. Milich, *supra* note 39, at 56.
42. *Id.* at 56; *see also* Adler, *supra* note 15, at 757–58.

The first MLP was formed in 1981 by Apache Corporation.[43] The need to form an MLP arose from Apache Corporation's need to consolidate its general and limited partnership interests in the drilling funds it sponsored.[44] Apache Petroleum Company was formed with Apache Corporation as its general partner, merging thirty-three of the corporation's oil and gas programs formed between 1959 and 1978.[45]

Although early MLPs existed primarily in the oil and gas arena, the business structure quickly caught on in a variety of other industries including everything from motels, real estate and amusement parks to casinos, cable companies and even sports teams.[46] As the number of MLPs rapidly increased, Congress saw a need to prevent a trend in which a significant amount of companies began to form MLPs in order to avoid corporate income taxes.[47]

The solution was found in restructuring the tax code to significantly limit the types of businesses that could organize as MLPs.[48] Through the Tax Reform Act of 1986 and the Revenue Act of 1987, Congress mandated that in in order to be taxed as a partnership, an MLP must derive at least ninety percent of its gross income from qualifying income sources.[49] Under section

43. JOHN KELSO, APACHE CORP., AGAINST THE GRAIN 8 (Roger Plank ed., 1995), *available at* http://www.apachecorp.com/Resources/Upload/file/history/Apache_Against_the_Grain_Apache_at_40.pdf.

44. *Id.*

45. ROBERT M. BROWN, APACHE CORP., JOURNEY INTO RISK COUNTRY: THE FIRST 30 YEARS OF APACHE CORPORATION 65–67 (Madeleine Meers ed., 2004), *available at* http://www.apachecorp.com/Resources/Upload/file/history/Apache_Journey_into_Risk_Country_The_First_30_Years.pdf; *see also* Milich, *supra* note 39.

46. Early MLPs included La Quinta Motor Inns Limited Partnership/Aircoa Hotel Partners, L.P., National Realty L.P., Cedar Fair, L.P. (an amusement park), Falcon Cable Systems Company, Sahara Casino Partners L.P., and Boston Celtics Limited Partnership. *See* FENN, *supra* note 27 at 9–10.

47. By 1987, there were over 100 MLPs in existence. *See* FENN, *supra* note 27, at 10.

48. *Id.*

49. Tax Reform Act of 1986, Pub. L. 99–514, 100 Stat. 2085 (codified as amended at I.R.C. § 7704); Revenue Act of 1987, Pub. L. 100–203, tit. X, §§ 10000-10714, 101 Stat. 1330–382 (codified as amended at I.R.C. § 7704). These legislations resulted in Section 7704 of the Internal Revenue Code, which

7704(d), qualifying income typically includes income and gains derived from the exploration, development, mining or production, processing, refining, transportation (including pipelines transporting gas, oil or products thereof) or the marketing of any mineral or natural resource. Certain passive-type income including interest, dividends, and real property rents, as well as some other forms of income, are also included under section 7704(d).[50]

One year later in 1988, Congress further clarified the tax rules to provide that certain resources such as soil, sod, turf, water, mosses and minerals, seawater, air and other similar inexhaustible sources are excluded from the scope of qualifying income under the tax code.[51] As such, renewable sources, such as agricultural products, or items that are unlimited in supply, such as solar power or wind, do not constitute natural resources under section 7704(d) and, therefore, are not considered qualifying income.

The actions of Congress successfully redirected MLPs back to the energy industry, and the 1990s and 2000s saw an increase of MLPs in midstream oil and gas companies as well as MLPs involving the marine transportation of petroleum, propane distribution, coal, exploration, and production were established.[52] In 2008, in the midst of rising gas prices, Congress further amended the MLP tax rules via the Emergency Economic

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defined and clarified the scope of publicly traded partnerships. *See* I.R.C. §§ 7704, 7704(c)(3) (2012).

50. *See* LATHAM & WATKINS, *supra* note 27, at 12 ("For purposes of the qualifying income rule set forth in the tax code, with respect to natural resource-related activities, the term 'mineral or natural resource' means fertilizer, geothermal energy and timber, as well as any product from which a deduction is allowable, which includes oil, gas, and oil-and-gas related products. Typically, anything that is dug or pumped out of the ground qualifies, which includes coal, lignite, potash, salt, aggregates, limestone, sand and many other hard rock minerals. Moreover, Congress made it clear in the legislative reports accompanying these qualifying income rules that, for purposes of determining the limits of what constitutes oil, gas, or products thereof, such term includes gasoline, kerosene, number-2 fuel oil, refined lubricating oils, diesel fuel, methane, butane, propane and similar products that are recovered from petroleum refineries or field facilities.").

51. I.R.C. § 7704(c), (d) (2012).

52. *Id.*

Stabilization Act, which expanded the definition of qualifying energy sources to include transportation and storage of ethanol, biodiesel, various liquefied fuels, and industrial-source carbon dioxide.[53] However, this amendment does not extend to activities beyond storage and transportation. Therefore, the manufacturing or sale of biodiesel or ethanol does not generate qualifying income.

III. THE MASTER LIMITED PARTNERSHIPS PARITY ACT

As previously discussed, master limited partnerships have been limited to investment in traditional energy projects in the oil, natural gas, coal extraction and pipeline industries. Introduced and drafted by Senator Chris Coons, the Master Limited Partnerships Parity Act would allow investors in renewable energy projects the ability to form MLPs. According to Coons, "[t]hese projects get access to capital at a lower cost and are more liquid than traditional financing approaches to energy projects, making them highly effective at attracting private investment."[54]

By giving investors in renewable energy the opportunity to form MLPs, the Master Limited Liability Partnership Parity Act[55] extends partnership tax treatment under the tax code to these investors. The legislation extends the definition of "qualified" sources to include clean energy resources and infrastructure projects.[56] Specifically covered are those renewable energy technologies that are covered under sections 45 and 48 of the tax code.[57]

53. Note that this amendment is limited only to transportation and storage-related sources, making the manufacture or sale of biodiesel or ethanol ineligible as qualifying income. *See* 26 U.S.C. § 30C(c)(2)(A).

54. Coons, *supra* note 4.

55. H.R. 1696, 113th Cong. (2013).

56. *Id.*

57. *See* I.R.C §§ 45, 48, (outlining rules for renewable energy production credit). Under section 45, renewable energy resources include wind, closed-loop biomass, open-loop biomass, geothermal energy, solar energy, small irrigation power, municipal solid waste, qualified hydropower production and marine and hydrokinetic renewable energy. § 45(c)(1).

In order to allow renewable energy investors the abovementioned opportunity to form an MLP, the bill expands the definition of "qualifying income" under § 7704 and § 613 of the tax code to include income and gains from renewable and alternative fuels (in addition to fossil fuels), including energy derived from thermal resources, waste, renewable fuels and chemicals, energy efficient buildings, gasification, and carbon capture in secure geological storage.[58]

Under the current law, traditional energy projects have a distinct advantage over renewable energy sources in that they have the ability to form as MLPs, which affords them significant tax benefits and limited liability. The goal of this bill is to create equity in the access to MLPs for both renewable and non-renewable energy investments. This goal for equity is not new, as this is not the first time a bill designed to expand the tax code to give renewable energy investors access to MLPs has been introduced. Senator Coons introduced similar legislation in 2012.[59] The 2012 proposed legislation was less specific than the current legislation and simply sought to amend the tax code to "extend the publicly traded partnership ownership structure to energy power generation projects and transportation fuels, and for other purposes."[60] H.R. 6437 was introduced on September 19, 2012 and was referred to the House Ways and Means Committee.[61] Unfortunately, the bill was never scheduled for a hearing and died there. In 2013, the bill was reworked producing the current legislation.

IV. THE CASE FOR THE MASTER LIMITED PARTNERSHIPS PARITY ACT

Supporters of the MLPPA cite various benefits of the Act. The primary argument in support of the MLPPA is that the MLP structure would increase investment in the renewable energy market. The theory is that the many advantages of the MLP

58. I.R.C. § 613, 7704.
59. H.R. 6437, 112th Cong. (2012).
60. *Id.*
61. *Id.*

structure will have the same overwhelmingly positive impact on the renewable energy market that it has had on the traditional non-renewable energy industry.[62] With access to partnership tax treatment, the ability to trade units on a public stock exchange and limited liability, the MLP structure has a much lower cost of capital than a corporation, for example. This makes it easier to attract investors who are looking for a flexible investment vehicle that offers tax advantages and still protects investors' personal assets through limited liability.[63]

A second argument in support of the MLPPA is that a significant influx of capital is required to support investment in renewable energy projects and the MLP business structure can help. Individual investment in renewable energy is not enough to move the country toward clean energy in a significant way.[64] Access to MLPs brings large-scale investors such as corporations, retirement funds, and trust accounts. These large-scale investors bring significant dollars to the renewable market, which is what is needed to make significant progress in the renewable energy industry and advance the clean energy agenda in the United States.[65]

Most importantly, there is an issue of equity with the current state of the law. Allowing non-renewable energy companies access to master limited partnerships as a choice of entity while denying renewable energy companies that same access is clearly discriminatory. The original fear was that the huge growth in the MLP industry in an effort to avoid corporate tax liability would lead to the erosion of the corporate tax base.[66] Nearly thirty years later however, this "threat" has not materialized. While MLPs are projected to cost the federal government a total of approximately $1.2 billion from 2011-2015, a recent study by Southern Methodist University anticipates that

62. Coons, *supra* note 4, at 2.

63. *Id.*

64. *See* Richard Caperton, *Master Limited Partnerships (MLPs) will Bring More Investment to Clean Energy*, THINK PROGRESS (June 10, 2013, 12:19 PM), http://thinkprogress.org/climate/2013/06/10/2127651/master-limited-partnerships-mlps-will-bring-more-investment-to-clean-energy/.

65. *Id.*

66. Adler, *supra* note 15, at 762.

renewable energy MLPs could raise approximately $7 billion in additional capital in the period from 2013-2020, which means that renewable energy MLPs will actually have a net positive economic impact.[67] Therefore, there is no bona fide economic reason to continue this discriminatory practice at this point in our history.[68] Not only is there no viable economic reason for the disparity, the current tax code hinders the United States from making significant and critically-needed progress toward reaching our clean energy goals. According to Senator Coons,

> [a]t a time when the United States needs to increase domestic energy production and leaders of both political parties say they support an "all of the above" energy strategy, Congress should level the playing field and give all sources of domestic energy – renewable and non-renewable alike – a fair shot at success in the marketplace.[69]

V. THE CASE AGAINST THE MASTER LIMITED LIABILITY PARTNERSHIP ACT

While the MLPPA has many supporters, there are those who are not proponents of the legislation, and several arguments have been made in opposition to the proposed Act.

One of such argument is that allowing renewable energy companies access to the many tax advantages provided by MLPs would erode the federal tax base.[70] The theory is the same as the original fear of the IRS in the late 1980s. If companies other than non-renewable energy companies are allowed to take advantage of this choice of entity, there would be a huge rush to organize as MLPs. Given the significant tax advantages that come with this choice of entity, namely that MLPs do not pay taxes at the

67. *See* Felix Mormann & Dan Reicher, *Smarter Finance for Cleaner Energy: Open Up Master Limited Partnerships (MLPs) and Real Estate Investment Trusts (REITs) to Renewable Energy Investment*, BROOKINGS REMAKING FEDERALISM/RENEWING THE ECON. SERIES, 2012 at 4 (2012), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2174650 (discussing the need to "level the playing field" between renewable and non-renewable energy sources).

68. *Id.* at 3.

69. Coons, *supra* note 4, at 1.

70. *See generally* Mormann & Reicher, *supra* note 67.

company level and the tax liability generated is largely deferred until the sale of the investment, open access to MLPs would have the effect of reducing the overall federal tax revenue generated, resulting in a shrinking federal tax base.[71]

Supporters of the legislation, however, disagree. One counterargument is that individual investors would still pay taxes on distributions received, which would counteract the erosion of the federal tax base.[72] In addition, access to master limited partnerships as a choice of entity would still be limited to energy companies as opposed to any company in any industry, which was the goal of the IRS when it initially limited access to this business structure.[73] Furthermore, the attractiveness of this business structure from an investment standpoint would likely draw more investors to the renewable market, and therefore would actually increase the tax revenue generated.[74]

Another criticism of the MLPPA is that if partnership tax treatment is extended to renewable energy investments, MLPs may be abused as tax shelters.[75] The fear is that MLPs would be used solely to generate tax benefits and not necessarily to further progress in the renewable energy industry.[76] There is yet another counterargument against this premise. Revisions to the tax code can always be structured in such a way that mandates that tax benefits gained as a result of MLP status actually result in bona fide renewable energy activities.[77]

Yet another criticism of the MLPPA is that when looking at the model of traditional MLPs in the oil and gas sector, the

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71. *Id.*

72. *Id.*

73. *Id.*

74. *Id.* at 4.

75. Critics have said the situation would be similar to the 1980s "wind rush." *See* Felix Mormann & Dan Reicher, *How to Make Renewable Energy Companies Competitive*, N.Y. TIMES, June 1, 2012, http://www.nytimes.com/2012/06/02/opinion/how-to-make-renewable-energy-competitive.html?pagewanted=all&_r=0&pagewanted=print (noting that the possibility of abuse of MLPs as tax shelters is a more valid concern than some of the other arguments against the MLPPA).

76. *Id.*

77. *Id.*

lower cost of capital and the cost-savings generated by it have not trickled down to consumers.[78] According to John Farell of the Institute for Local Self-Reliance, MLPs will lead to more large-scale projects from large-scale investors, not individuals, and individual progress is not enough to produce the type of substantial progress we need to truly move forward with clean energy in the United States.[79] This argument is flawed as well. Businesses are not designed to save consumers money. They are designed to increase the profits of the company and provide a desired return to investors. In fact, large-scale projects from large-scale investors are exactly what are needed to make the significant progress in the renewable energy industry that is so desperately needed in this country.[80] Consider the example provided by Richard Caperton, Managing Director of Energy at the Center for American Progress. Using the National Renewable Energy Laboratory's Renewable Electricity Futures Study, he states:

> [G]etting to 80 percent renewable energy in the United States will cost just under $2 trillion . . .. Since there are about 115 million households in the U.S., that means we would need about $17,000 in investment from every household to pay for new renewable power. Unfortunately, the median net worth of American families was about $77,000 in 2010, which means that we would need the middle-of-the-road family to invest a whopping 20 percent of their wealth in renewable energy. . . . This would be great for renewable energy, but it's almost certainly a bad idea for families to invest 1/5 of their money in once specific industry, when we know the value of diversification. This means that we're going to need money to come from other places, and this is where MLPs come into play. The dominant investors in MLPs are individuals, corporations, and various retirement accounts and trust accounts. These are big pots of

78. John Farrell, *Why Master Limited Partnerships are a Lousy Policy for Solar, Wind, and Taxpayers*, RENEWABLE ENERGY WORLD, June 3, 2013, http://www.renewableenergyworld.com/rea/news/article/2013/06/why-master-limited-partnerships-are-a-lousy-policy-for-solar-wind-and-taxpayers.

79. *Id.*

80. Caperton, *supra,* note 64.

> money, and it's what we need to access if we want to get $2 trillion into clean energy.[81]

A final argument against the MLPPA is that although proponents of the legislation argue that it will have a huge impact on investments in the renewable energy market, it is more likely that this impact will be modest at best.[82] The theory behind this argument is that MLPs are an ill fit for renewable energy investments.[83] According to Robert Rapier,

> [t]he main reason so many MLPs have been successful is their concentration on energy infrastructure, a booming industry with a long history of profitability. This has attracted conservative investors, and MLP tax rules have given them an incentive to stick around for the long run. . . . Most renewable energy investments are in a very different business. The vast majority of renewable energy companies exist as a result of mandates at the federal or state level. I don't mean to suggest that we shouldn't support renewable energy, merely to note that if certain tax credits and mandates were eliminated, the industry would be decimated because for the most part it isn't competitive with fossil fuels. MLPs have a steady source of income from which to pay distributions. . . .

The fact is that unless they can come up with long-term supply agreements that will see them through even if government support disappears, renewable energy MLPs could prove very risky investments.84

81. *Id.* The median net worth of American families has risen to $81,200 as of the most recent census data released in September 2014, however, the calculations in this example remain roughly the same. Middle of the road families would still need to invest just under 20% of their net worth in renewable energy. *See* Jesse Bricker et al., *Changes in U.S. Family Finances from 2010-2013: Evidence from the Survey of Consumer Finances*, 100 FED. RES. BULL. 1, 4 (2014).

82. William Pentland, *MLP Parity Act: Disrupting Distributed Energy*, FORBES (June 10, 2013) http://www.forbes.com/sites/williampentland/2013/06/10/mlp-parity-act-disrupting-distributed-energy/print/ (citing Rapier, *infra* note 84).

83. *Id.*

84. Robert Rapier, *Is MLP Parity Act a Game Changer?*, INVESTING DAILY (May 28, 2013) http://www.investingdaily.com/17512/is-mlp-parity-act-a-game-changer/.

VI. CONCLUSION

It is clear that there are many advantages to allowing renewable energy companies access to master limited partnerships as a choice of entity. The financial and tax advantages of the MLP structure would increase investment in the renewable energy sector. In addition, access to a financially attractive structure such as the master limited partnership structure attracts large-scale investors who will contribute a substantial influx of capital into the renewable energy market. This would bring about significant progress toward the clean energy agenda in the United States. Finally, the current state of the law is inexplicably inequitable. There appears to be no legitimate economic reason to allow non-renewable energy companies to organize as MLPs while denying renewable energy companies the same access.

While there are disadvantages to this proposition as well, these disadvantages appear to be avoidable and easily remedied, if the proposed MLLPA is drafted carefully. The problems with the status-quo, however, can *only* be remedied through expansion of MLPs to include the renewable energy sector. Therefore, the advantages seem to far outweigh the minor, fixable disadvantages. If this country is to truly move toward replacing fossil fuels with renewable energy sources, we must make drastic and significant changes to the portions of our tax code that hinder progress in the renewable energy sector. Ultimately, is there any real downside to exploring this opportunity to stimulate and expand investment in renewable energy?