

MLPs and the Tax Code

Rob Baldwin, PricewaterhouseCoopers LLP

Mike Bresson, Baker Botts L.L.P.

Ryan Carney, Vinson & Elkins LLP

James Chenowith, Gibson, Dunn & Crutcher LLP

Tim Fenn, Latham & Watkins LLP

Greg Nelson, Paul Hastings LLP

Angela Richards, Andrews Kurth Kenyon LLP

June 1, 2017

Recent Regulatory Changes: Qualifying Income Rules



STANDARD & POOR'S



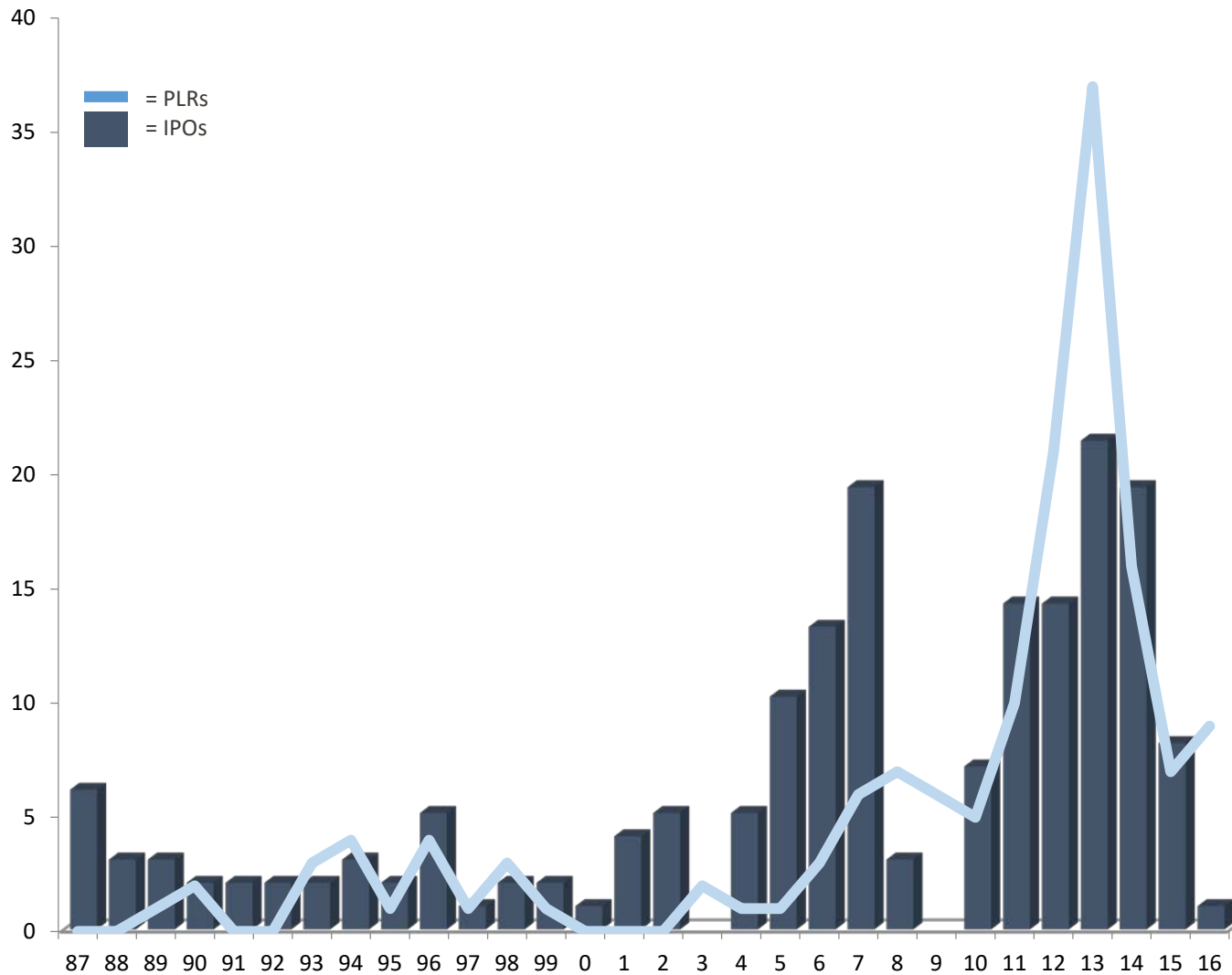
Qualifying Income and PLRs

Qualifying Income and PLRs

- The scope of what is included in “qualifying income” can be complicated to determine.
- Because the public market needs certainty that the MLP will not be taxed as a corporation (because it failed the 90% qualifying gross income test), if the MLP’s advisors cannot give it a “will” level of opinion on qualifying income, the MLP will ask the IRS for a private letter ruling (PLR).
 - The IRS has privately ruled that many forms of natural resource activities, including pipelines and fracking activities, give rise to qualifying income.

MLP IPOs v. PLRs: 1987-2016

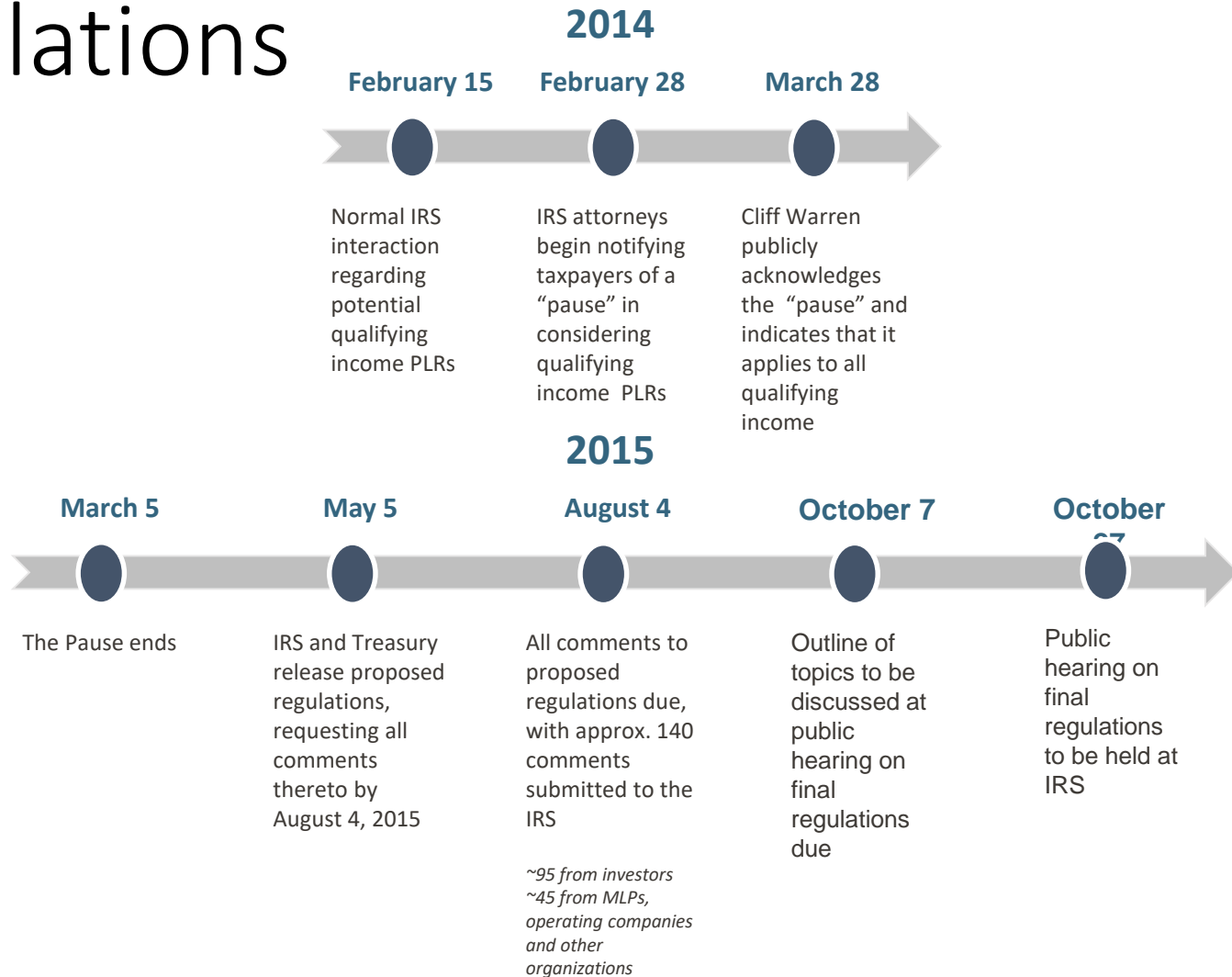
- 151 PLRS SINCE 1987



The PLR “Pause”

- In March 2014, the IRS announced a “pause” for PLRs with respect to certain MLPs, temporarily suspending the issuance of new PLRs on qualifying income unless they were “straight down the fairway.”
 - Driven by recent volume of PTP ruling requests.
 - Industry changes have increased the extent to which natural resource-related income is earned by outside contractors, which caused the IRS to reconsider the scope of the qualifying income exception.
 - IRS focused on whether income is “integrally related.”
 - The “freeze” was expected to last several months (similar to pause for REIT rulings in 2013), but lasted substantially longer than the originally mentioned expectation for guidance in fall of 2014.
 - The IRS announced in early March 2015 that it would immediately begin issuing PLRs again and hoped to publish proposed regulations soon.

IRS Pause Turns Into Proposed Regulations



Publication of the Final Regulations

- On January 19, 2017, the final regulations under section 7704 were released by the IRS and the Treasury Department and filed with the Federal Register.
- On January 20, 2017, the new Trump Administration imposed a government-wide regulatory freeze in a White House memorandum issued by the President's Chief of Staff.
- The memorandum included an instruction to the heads of executive departments and agencies to immediately withdraw regulations that have been sent to the Federal Register, but not yet published, until a department or agency head appointed or designated by the President reviews and approves the regulations.
- On January 24, 2017, in a surprise to many, the final regulations under section 7704 were published in the Federal Register. Because the regulations were published in the Federal Register, the regulations are now final.

Final Regulations

- The final regulations are largely viewed as an improvement over the proposed regulations. They address favorably many, but not all, of the comments to the proposed regulations, but do so largely within the framework of the proposed regulations.
- The most significant changes are as follows:
 - No more “exclusive list” of qualifying activities
 - Greater clarity on the qualifying nature of some activities:
 - LNG liquefaction and regasification
 - Transportation and sale of propane to retail customers
 - Pipeline compression services
 - Many blending and additization activities
 - Reimbursement of costs
 - Hedging activities subject to further guidance

Final Regulations *(cont'd)*

- The most significant changes are as follows *(cont'd)*:
 - Simplified analysis of oil and gas products:
 - “Good list” approach to processing and refining of oil and gas
 - Olefins generate qualifying income
 - Methanol does not generate qualifying income
 - Narrow interpretation of hard mineral processing depending on the type of ore
 - Excludes coking of coal, steelmaking, and aluminum smelting
 - Oilfield services still qualify
 - Basin-by-basin approach for oil field service providers; and clarification that an MLP’s subcontractors are treated as partnership personnel

Final Regulations *(cont'd)*

Proposed Regulations

IN: <ul style="list-style-type: none"> • Transportation and storage of crude oil, natural gas, NGLs, and fuels • Field gas processing and NGL fractionation 	OUT: <ul style="list-style-type: none"> • NGL processing into olefins • Non-refinery olefin transportation and storage • Methanol production • Pulp, containerboard, and paper • Gas-to-liquids (anything other than methane-to-liquid fuels) • Non-affiliated water supply 	ON THE FENCE: <ul style="list-style-type: none"> • Hard mineral processing • Royalty income • Compression services • Propane distribution • CNG and LNG
	<ul style="list-style-type: none"> • Affiliated-controlled water supply and disposal • Saltwater disposal services • Wholesale sales • Wood pellets • Gas-to-liquid fuels 	

Final Regulations

IN: <ul style="list-style-type: none"> • Transportation and storage of crude oil, natural gas, NGLs, and fuels • Field gas processing and NGL fractionation • Saltwater disposal services • Wholesale sales 	<ul style="list-style-type: none"> • Wood pellets • <i>Gas-to-liquids (refinery products)</i> • <i>NGL processing into olefins</i> • <i>Non-refinery olefin transportation and storage</i> • <i>Frac water supply with local disposal business</i> • <i>Royalty income</i> • <i>Compression services</i> • <i>Propane distribution</i> • <i>CNG and LNG</i> • <i>Hard mineral processing – mining processes</i> 	OUT: <ul style="list-style-type: none"> • Methanol production • Pulp, containerboard, and paper • <i>Frac water supply without local disposal business</i> • <i>Hard mineral processing – beyond mining</i>
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Final Regulations – Transition Rule

- A partnership may treat income from an activity as qualifying income during the 10-year transition period if:
 - 1) The partnership has a PLR.
 - 2) The partnership is publicly traded and engaged in the activity after May 6, 2015, but before January 19, 2017, and the income from that activity is qualifying income under the proposed regulations.
 - 3) Prior to May 6, 2015, the partnership was publicly traded, engaged in the activity, and treated the activity as generating qualifying income under a reasonable interpretation.
 - 4) Prior to May 6, 2015, the partnership had entered into a binding agreement for the construction of assets to be used in an activity that generated qualifying income under a reasonable interpretation.

Recent M&A for MLPs



**Recent Mergers & Acquisitions
Publicly Traded Partnerships**

**Angela T. Richards
Gregory V. Nelson**

June 1, 2017

Dropdown Transactions

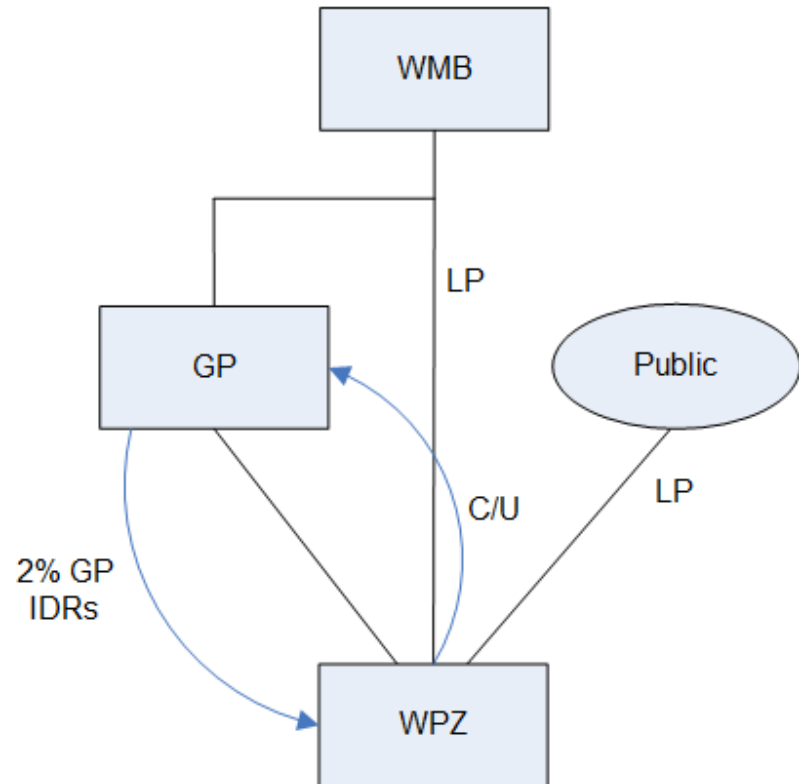


**Shell Midstream
Partners**



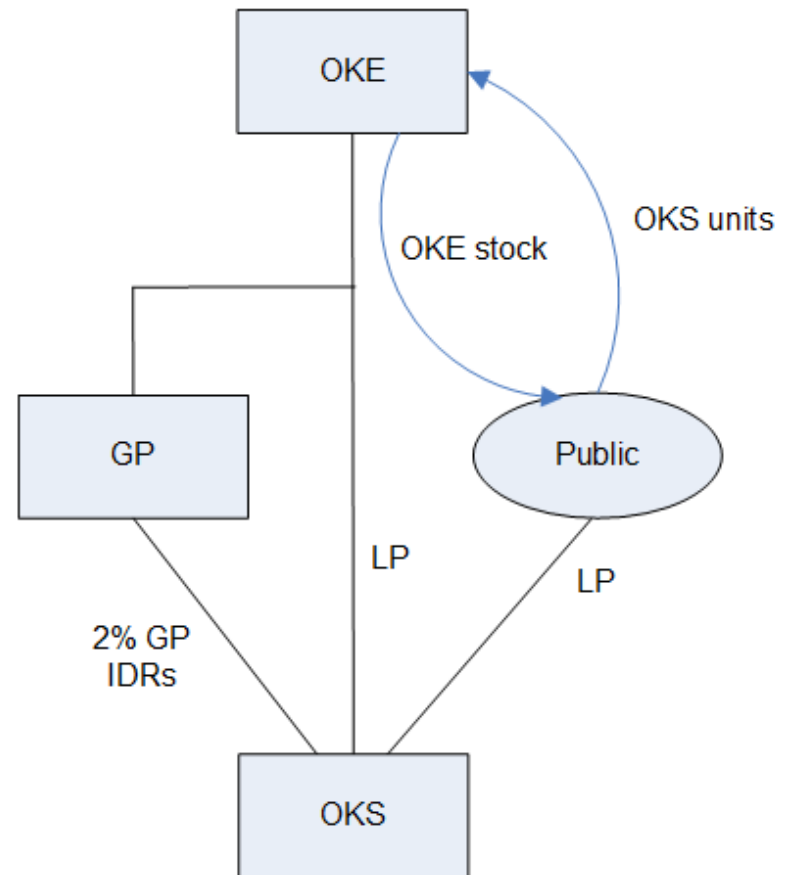
Williams Partners LP

- Equity recap
- Permanent waiver of IDRs, conversion of 2% GP interest
- Tax consequences to public unitholders?

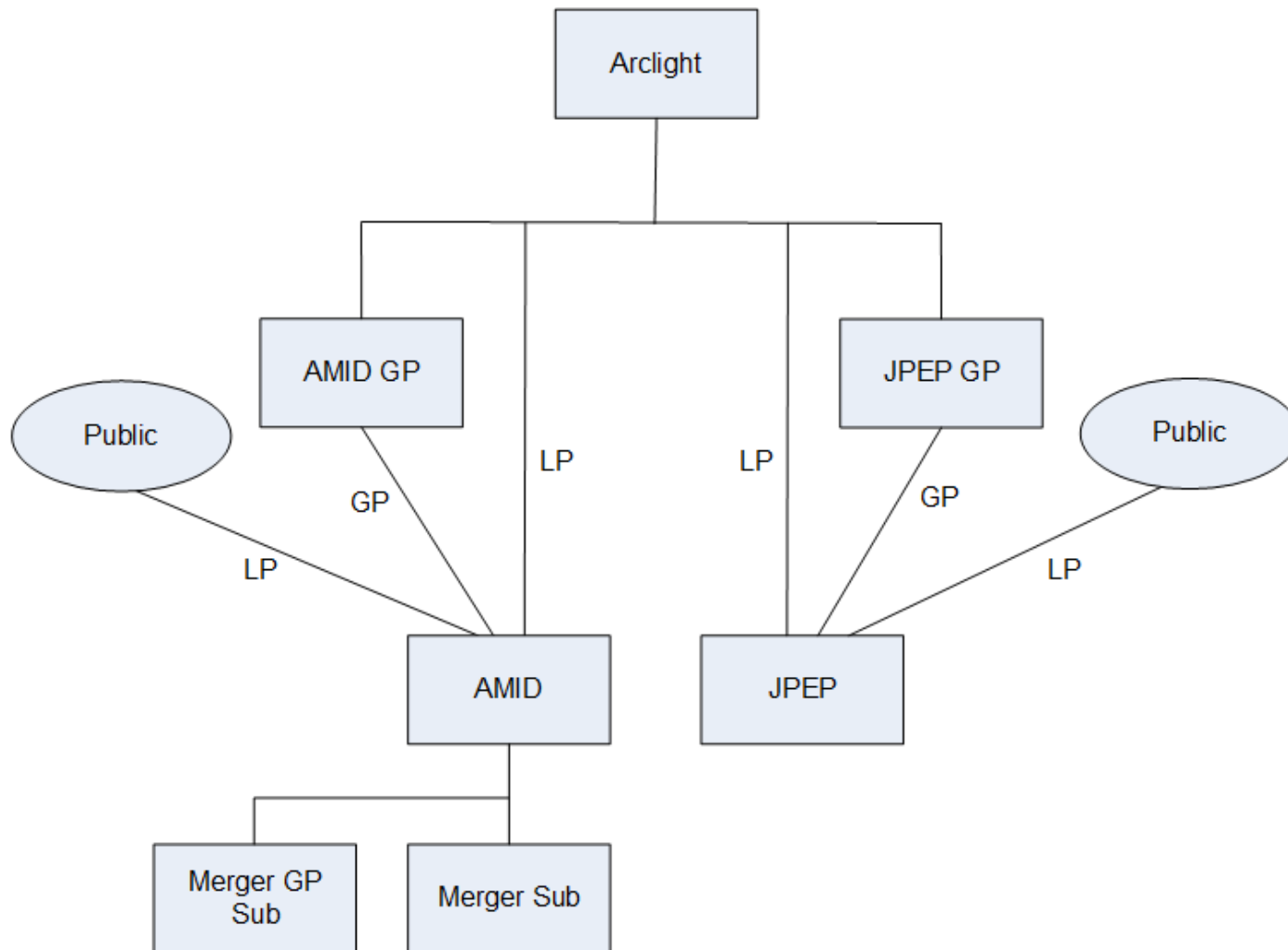


ONEOK Partners LP

- Roll-up
- Exchange of OKS units for OKE stock
- Tax consequences to public unitholders?

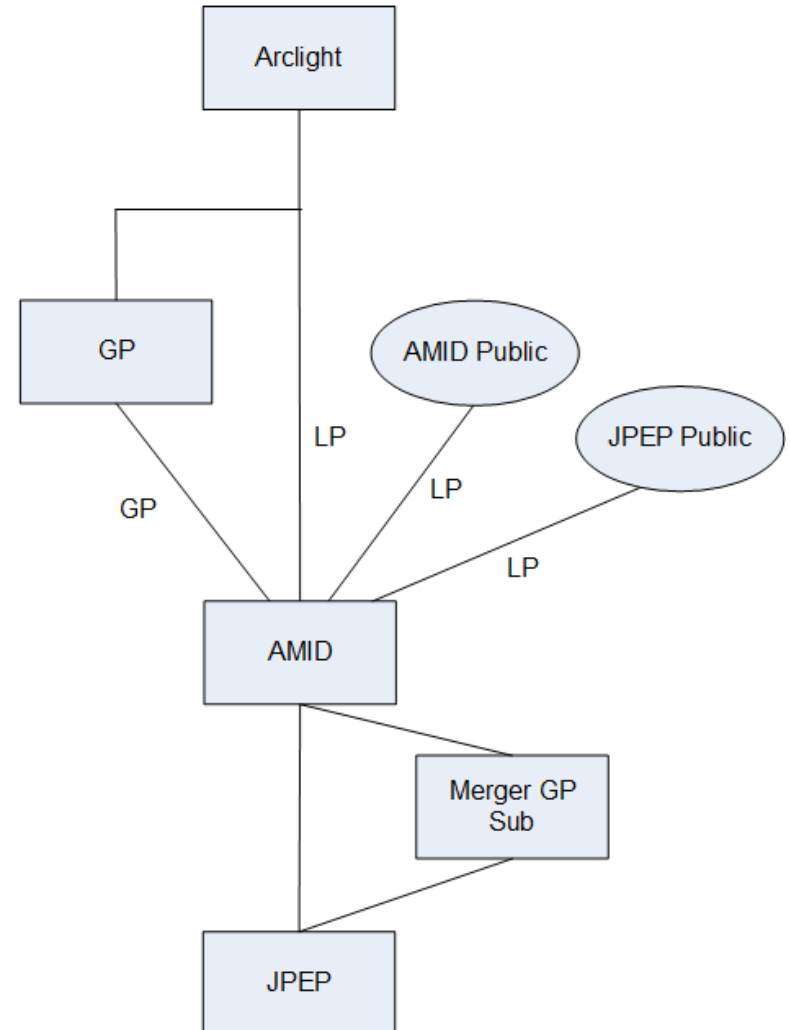


JP Energy Partners LP – American Midstream Partners, LP



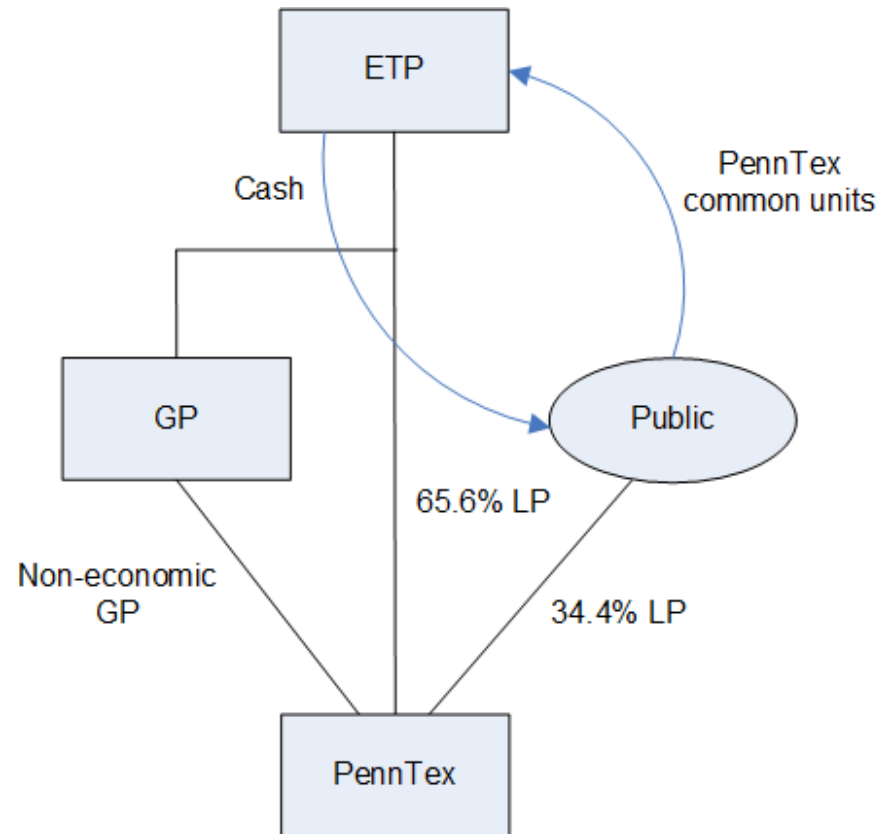
JP Energy Partners LP – American Midstream Partners, LP

- Merger
- JPE public receives AMID common units
- Tax consequences to public unitholders?

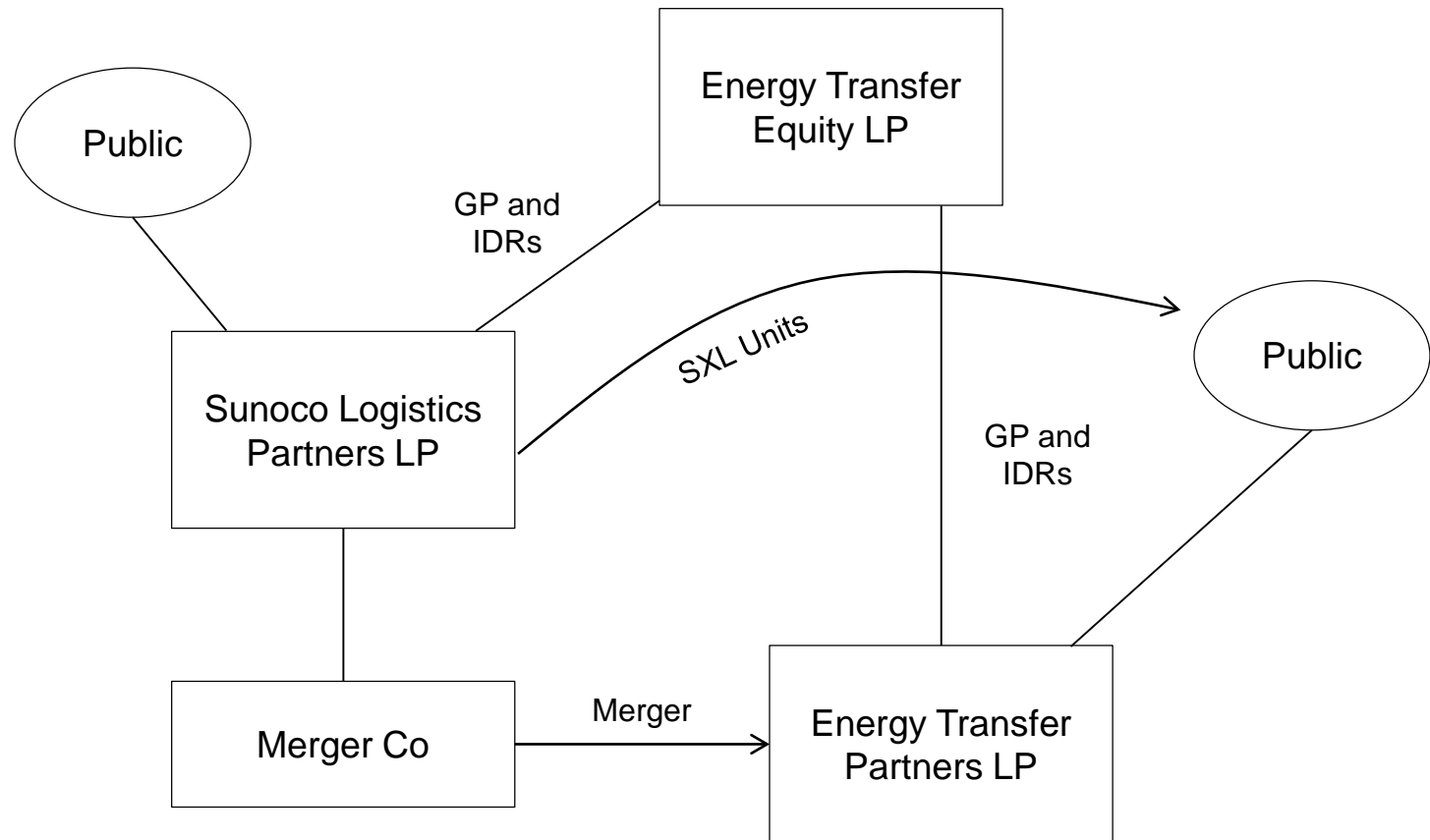


Energy Transfer Partners, L.P. – PennTex Midstream Partners, LP

- Cash tender offer
- Exercise of call right upon acquisition by ETP of 80% of PennTex common units
- Tax consequences to public unitholders?

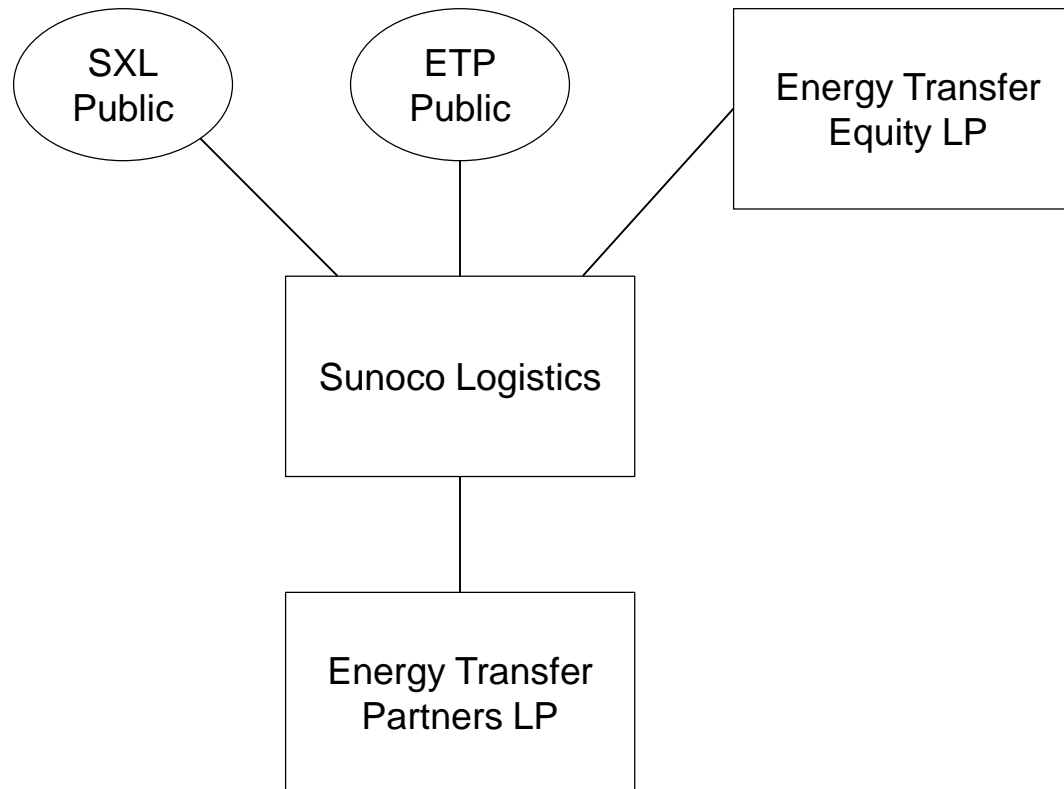


Energy Transfer – Sunoco Logistics



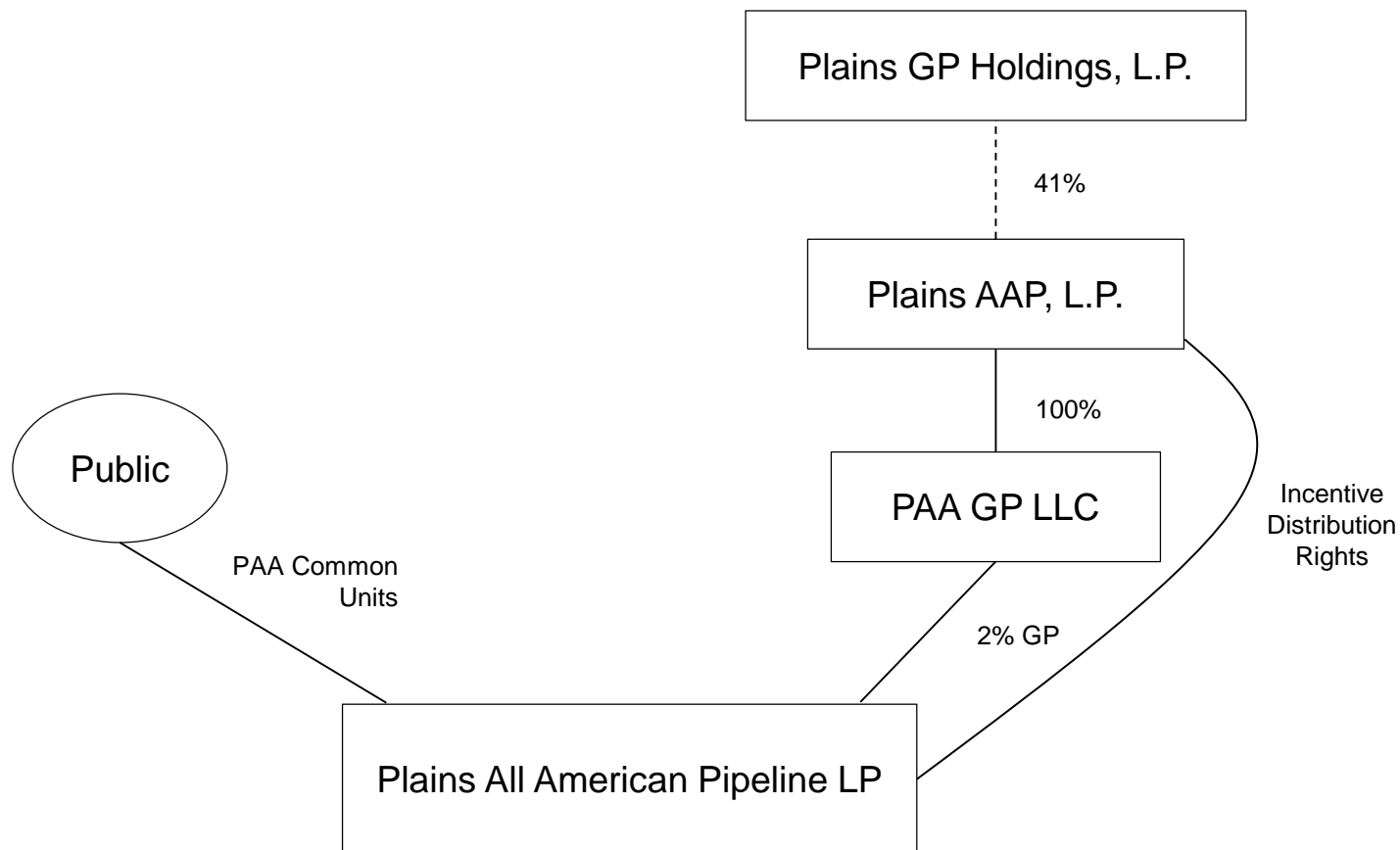
April 2017

Energy Transfer – Sunoco Logistics



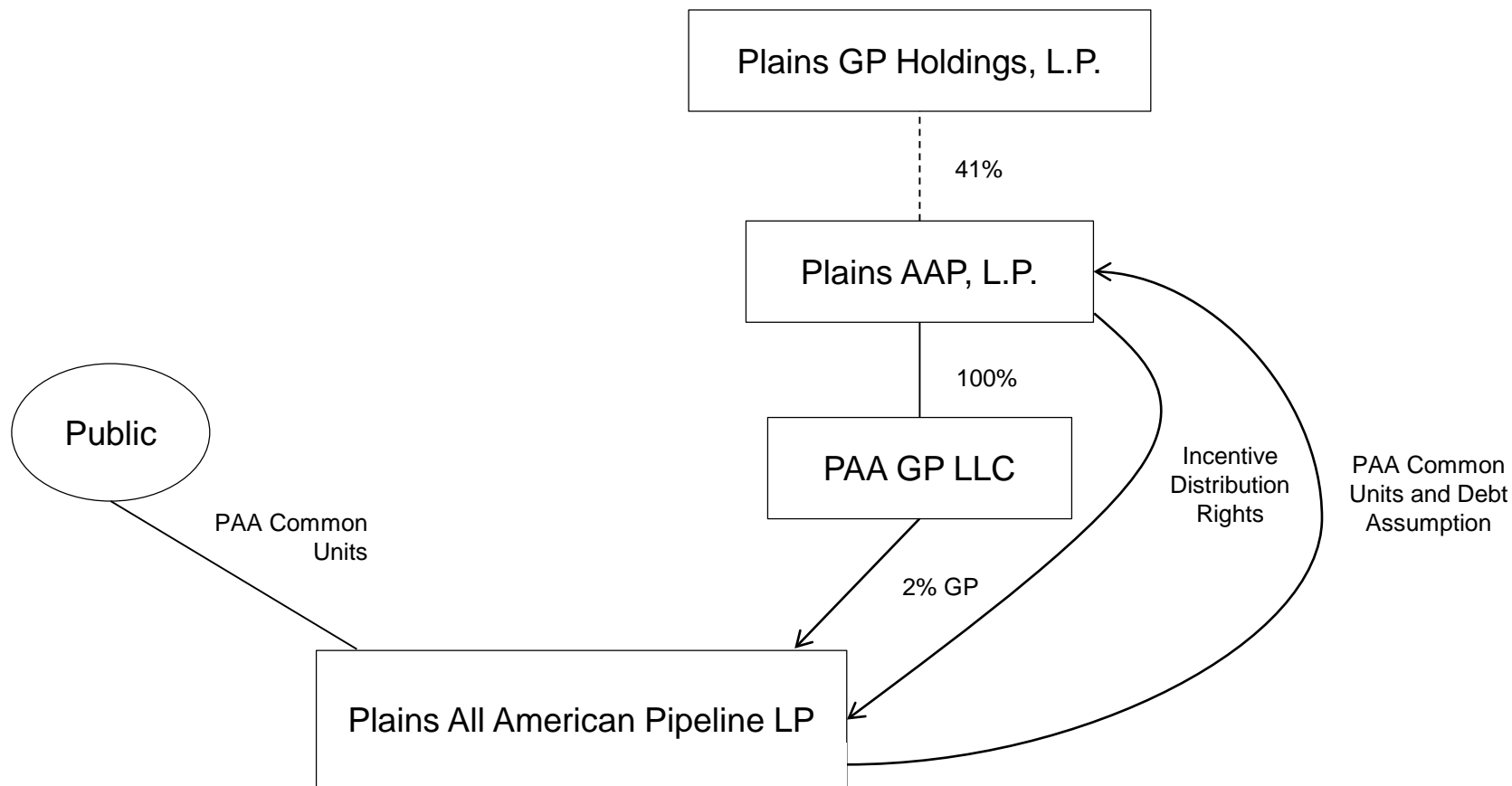
- Sunoco Logistics changes its name to Energy Transfer
- For tax purposes, Sunoco is deemed to merge into Energy Transfer

Plains All American Simplification



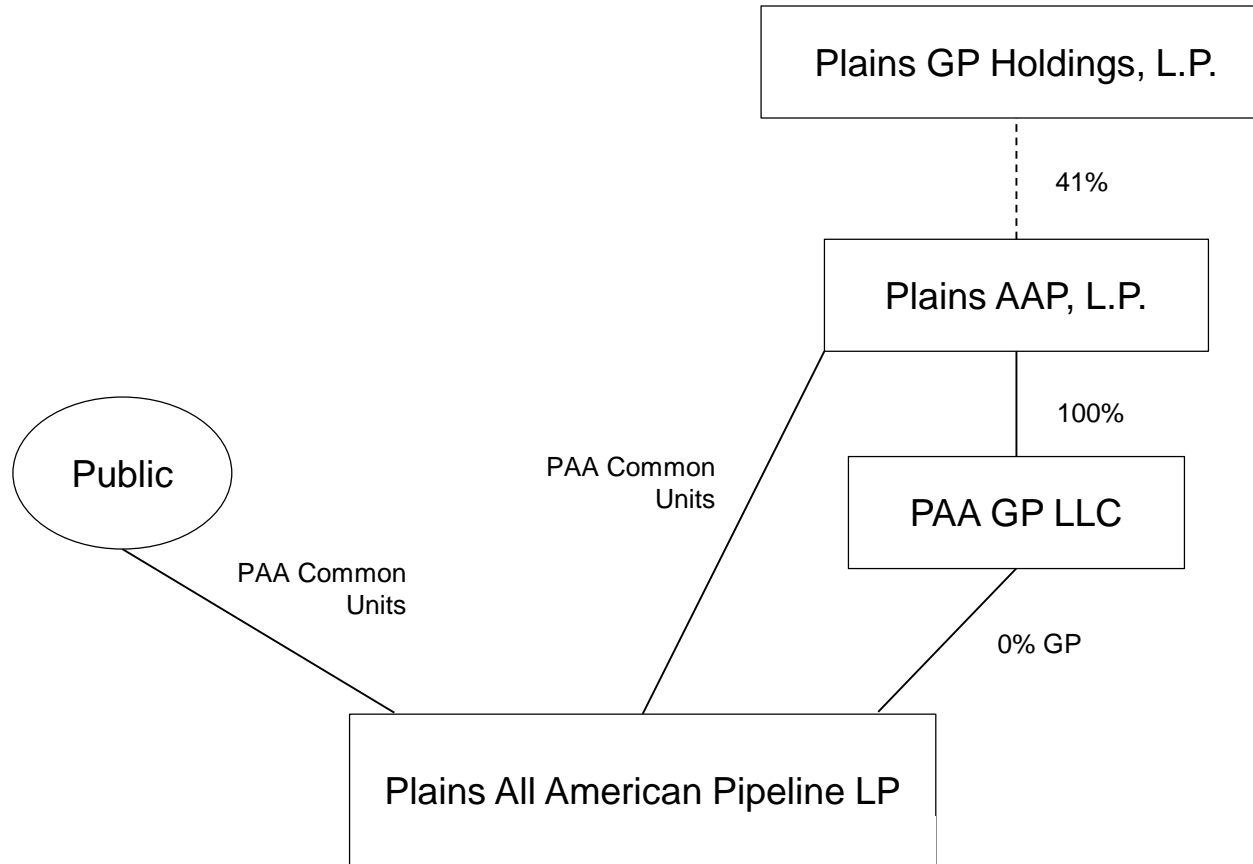
November 2016

Plains All American Simplification

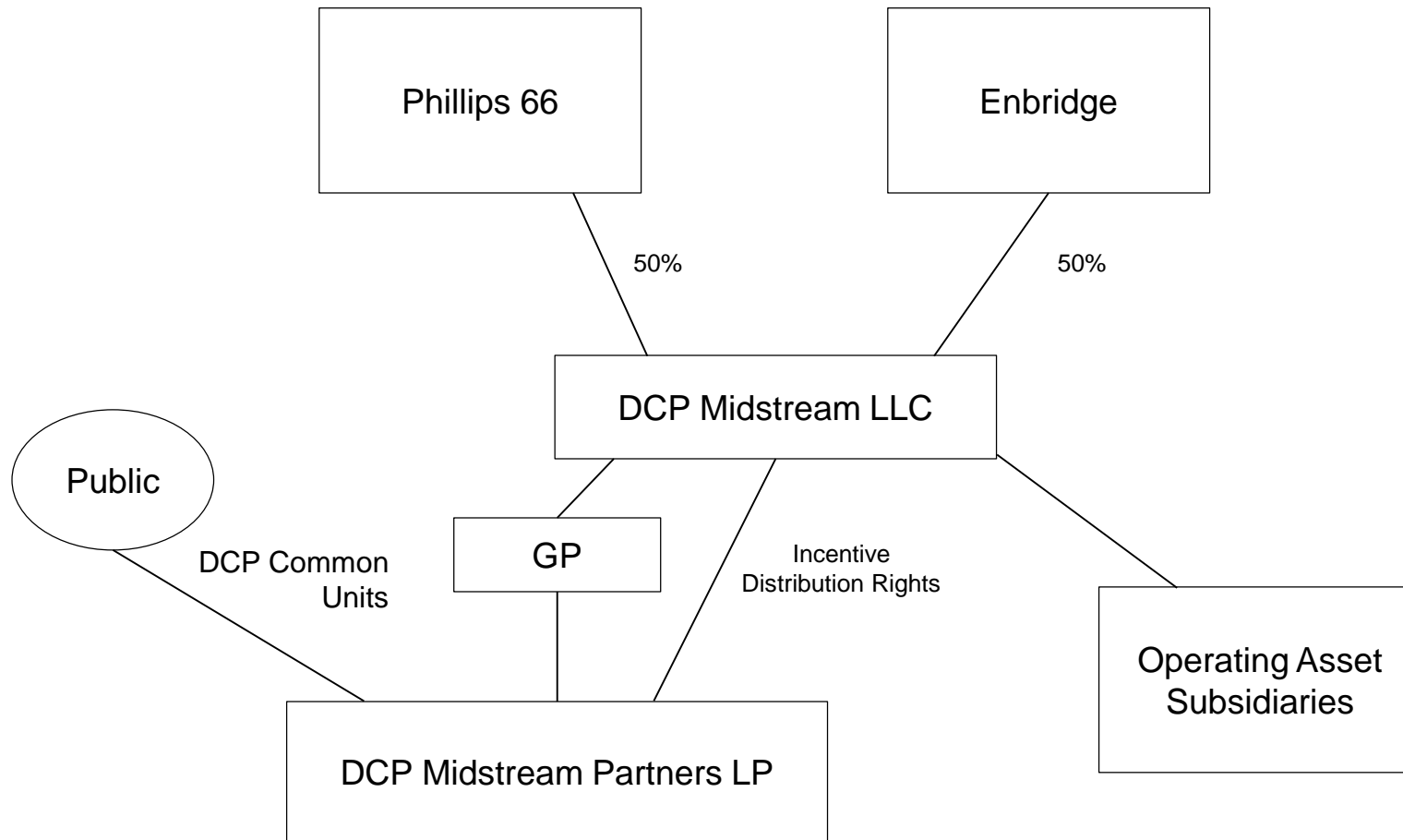


- Plains AAP, L.P. surrenders IDRs
- PAA GP LLC surrenders the 2% economic interest attached to the GP interest
- Plains All American Pipeline LP issues PAA Common Units and assumes indebtedness of Plains AAP, L.P.

Plains All American Simplification

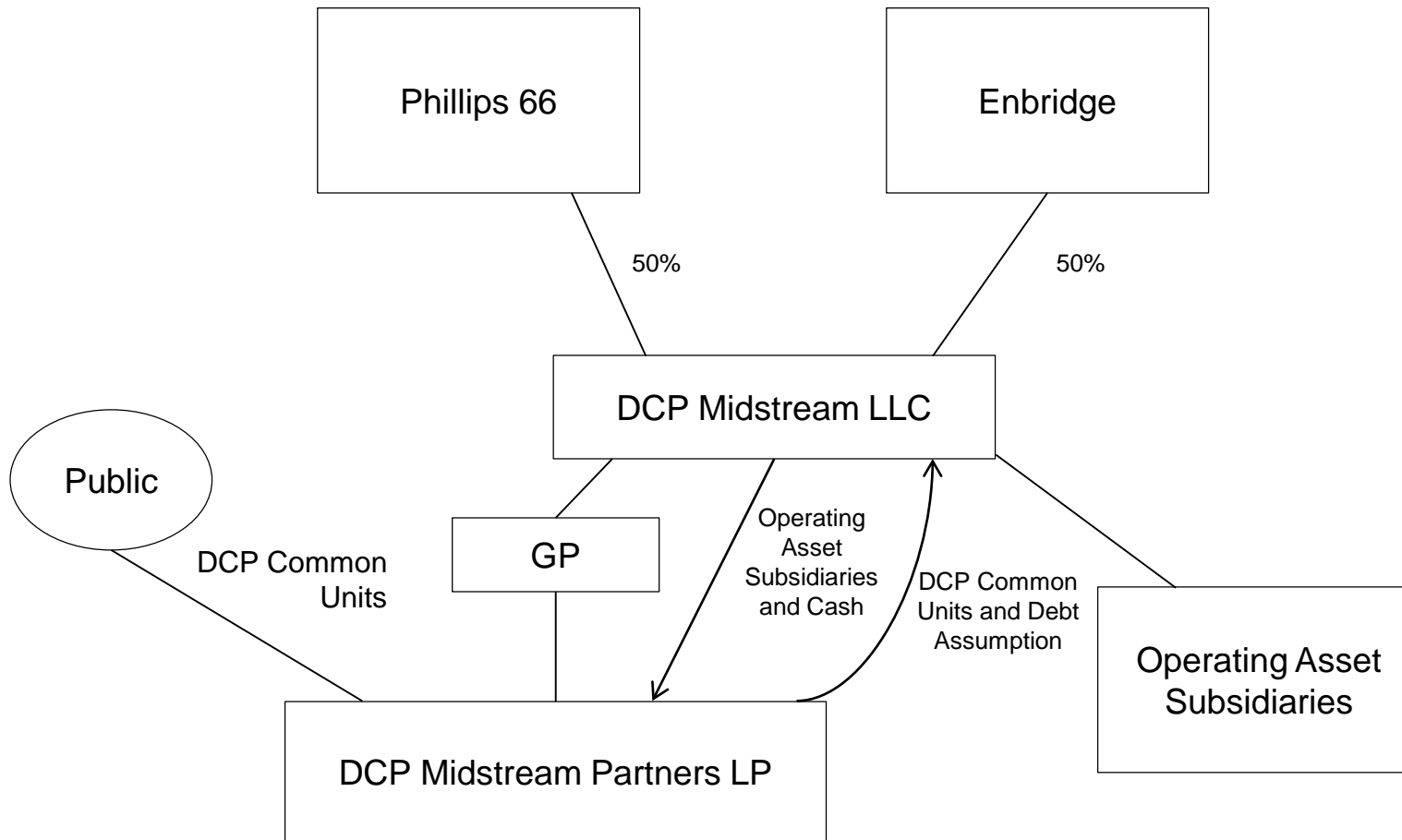


DCP Midstream Drop Down



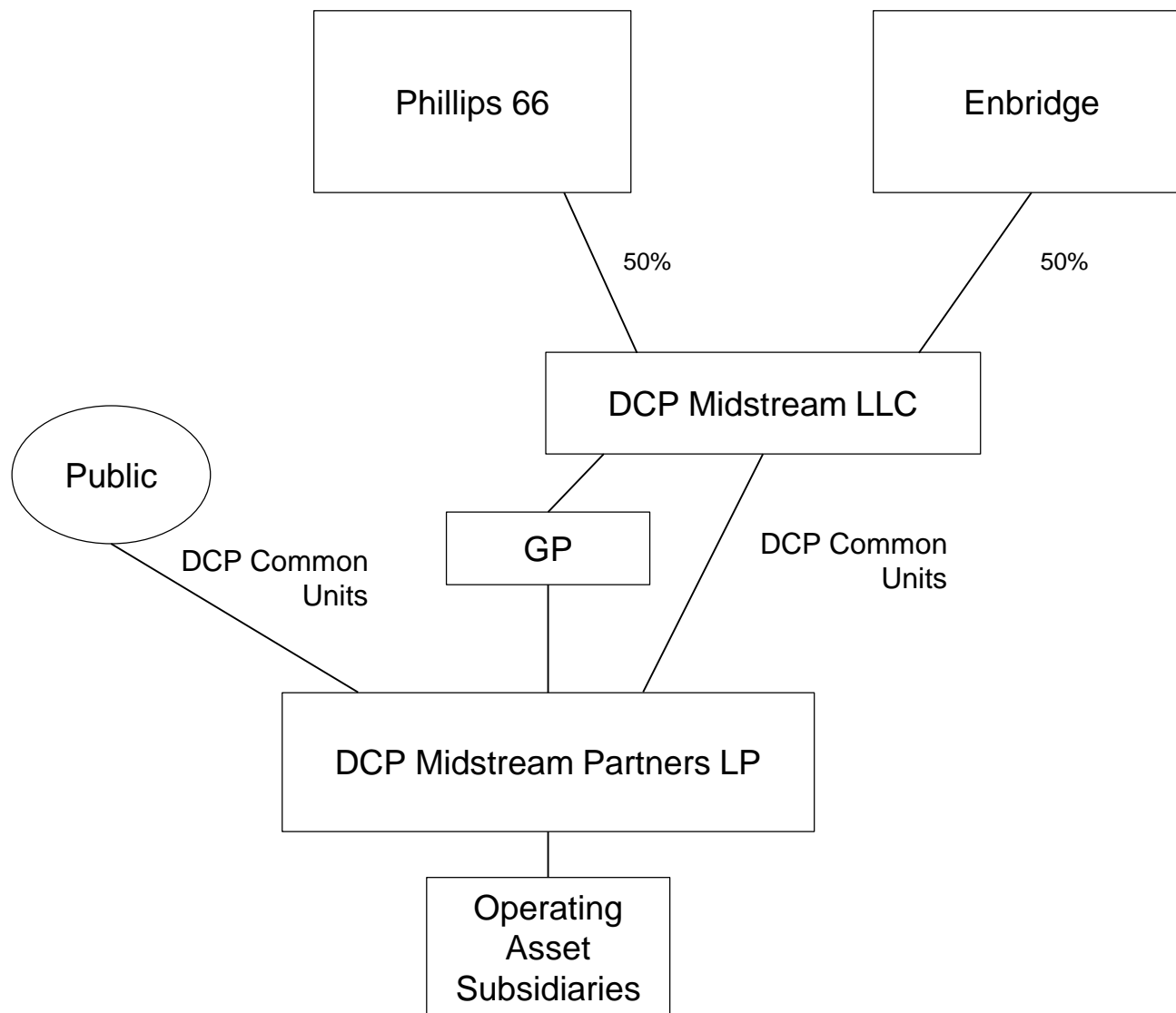
January 2017

DCP Midstream Drop Down



- DCP Midstream transfers cash and interests in its operating subsidiaries to DCP Midstream Partners LP
- DCP Midstream Partners LP issues DCP Common Units to DCP Midstream LLC

DCP Midstream Drop Down



When Should I be Worried: Legislation in the Trump World





Questions?
